Court File No. CV-24-00716511-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

B E T W E E N:

KINGSETT MORTGAGE CORPORATION

Applicant

- and -

MAPLEVIEW DEVELOPMENTS LTD., PACE MAPLEVIEW LTD and 2552741 ONTARIO INC.

Respondents

IN THE MATTER OF AN APPLICATION UNDER SUBSECTION 243(1) OF THE *BANKRUPTCY AND INSOLVENCY ACT,* R.S.C. 1985, c. B-3, AS AMENDED, AND SECTION 101 OF THE *COURTS OF JUSTICE ACT*, R.S.O. 1990, c. C.43, AS AMENDED

REPLY FACTUM OF THE RECEIVER
(Motion Returnable September 17, 2024)

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TO: **SERVICE LIST**

1. This Factum is filed by the Receiver in reply to the Responding Factum of Sunbelt Rental of Canada Inc. and Mykon Electric North Ltd., and the Responding Factum of the Fuller Landau Group Inc., each of which was filed September 5, 2024 (collectively, the "**Responding Factums**"). The Receiver continues to rely on the fact and law set out in its Initial Factum dated August 28, 2024 (the "**Initial Factum**"), and terms not defined herein have the same meaning as in the Initial Factum.

2. In their Responding Factums, the Objecting Lien Claimants advance a number of arguments in favour of granting themselves complete priority over the KingSett Mortgage. Among other things, the Objecting Lien Claimants argue that: (i) section 78 of the *Construction Act* is to be interpreted exclusively in favour of lien claimants; (ii) a building mortgagee can never obtain priority over lien claimants under section 78(2) of the *Construction Act*; and (iii) the re-registration of the KingSett Mortgage (as discussed in the Initial Factum) has completely re-ordered priority, such that the lien claimants should obtain an unexpected windfall of over $10 million.

3. As is set out below, these arguments are fundamentally misconceived and are contrary to both existing jurisprudence and the policy purposes underlying the *Construction Act*. As a result, the KingSett Mortgage continues to enjoy priority over the Lien Claims (except with respect to the holdback) under both sections 78(2) and 78(6).

4. It must be emphasized that the arguments of the Objecting Lien Claimants rest entirely on their assertion that the re-registration of the KingSett Mortgage disentitles KingSett from retaining its existing priority over the Lien Claims, catapulting it from enjoying priority except for the holdback, to being entirely subordinate to the Lien Claims. As is set out in more detail below, the re-registration of the KingSett Mortgage was a procedural step which was executed solely to consolidate the Prior Commitment Letters and, in connection therewith, to charge certain

additional lands. The re-registered mortgage involved the same lender, the same borrower, the same advances and the same intention on the part of the mortgagee, being entirely to fund construction. As established by the uncontroverted evidence filed by the Receiver, this re-registration was required in order to add the additional lands to the charge, as this cannot be completed by way of amending a mortgage, but requires re-registration.[1]

5. If the arguments of the Objecting Lien Claimants are accepted, the absurd result would be that a mortgagee would never be able to re-register or amend a mortgage to include additional lands without losing its existing priority position entirely to an unknown, future class of lien claimants who may later lien the project. This simply cannot be the intended result under the *Construction Act*, which as will be shown below is designed to balance the interests of lien claimants and mortgagees by giving lien holders priority over the holdback, while at the same time facilitating construction financing by ensuring that mortgagees retain priority for amounts beyond the holdback. The interpretation advanced by the Objecting Lien Claimants would have the exact opposite effect to this careful balancing, and would introduce substantial uncertainty into the priority position of mortgagees, chilling the ability to amend or refinance construction projects.

6. Further, none of the Objecting Lien Claimants address the central issue of whether the Lien Claims are Priority Payables. Pursuant to paragraph 12 of the AVO, only Priority Payables are entitled to be paid from the Lien Claimants' Reserve. As set out in the Receiver's Factum, the term "Priority Payables" is defined in the Sale Agreement as:

> any payables that have priority over the Assumed Mortgages, excluding any Harmonized Sales Tax owing by the Debtors, but including amounts that have priority pursuant to s.78(2) of the Construction Act, RSO 1990, c C30, as

[1] See the Affidavit of Daniel Pollack sworn August 14, 2024 [Pollack Affidavit], at para. 19, in which the affiant states that the re-registration was done on the advice of counsel, who advised that an existing mortgage may not be amended to include additional charged lands. This evidence has not been addressed or refuted by the Objecting Lien Claimants, who did not file responding affidavit evidence, nor cross-examine on the affidavit.

> determined by the Receiver in consultation with the Purchaser, both acting reasonably, or as determined by the Court, after application of any amount of cash on hand of the Debtors, excluding the Deposit, immediately prior to Closing.

7. The Assumed Mortgages have priority to the Lien Claims (except with respect to valid holdback claims) pursuant to section 78(6) of the *Construction Act* for the simple reason that they were registered after the time when the first lien arose, and (as acknowledged by the Objecting Lien Claimants) neither of the section 78(6) exceptions applies.

8. Finally, the Responding Factum of Fuller Landau Group Inc. additionally argues that it is somehow inappropriate for the Receiver to have taken a position on this motion. As is set out below, this objection is entirely baseless and is inconsistent with both the role of the Receiver and common practice in receiverships.

A. Section 78 is Intended to Balance the Interests of Lien Claimants and Mortgagees

9. Contrary to the submissions of the Objecting Lien Claimants, section 78 of the *Construction Act* is not intended to be interpreted to favour the interests of lien claimants, to the detriment of all other parties. The text of section 78 contains no such requirement; further, such a requirement would be fundamentally inconsistent with the purpose underlying section 78, which is intended to balance the legitimate interests of all parties, including both contractors and mortgagees.[2] Rather than being interpreted solely in favour of lien claimants, section 78 should be interpreted in a manner consistent with balancing the interests of all concerned parties.

10. Section 78 balances the interests of lien claimants and mortgagees by providing a general priority for lien claimants under section 78(1), which is in turn subject to a number of exceptions

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[2] *BCIMC Construction Fund Corp. et al. v. 33 Yorkville Residences Inc et al.*, 2022 ONSC 2326 at para. 27 [*BCIMC* (SC)], aff'd 2023 ONCA 1 [*BCIMC* (CA)].

in favour of mortgagees found in the remainder of section 78.[3] In order to ensure that the interests of the lien claimants remained protected, the drafters of section 78 further ensured that lien claimants retained their priority over the holdback required to be kept under the *Construction Act*, even where a mortgagee otherwise has priority.[4] These "exceptions to exceptions"[5] ensure that "when [a mortgagee] makes an advance with a clear title it retains its priority for that advance,"[6] while still ensuring that the lien claimants retain priority with respect to the holdback. Accordingly, to characterize (as the Objecting Lien Claimants do) the priorities regime under section 78 as giving lien claimants assumed full priority, subject to a limited number of discrete exceptions, is not in accordance with the way section 78 is drafted, nor the way it operates in practice.

11. This balancing act between the various interested parties was designed above all else to preserve lien claimants' rights to the holdback, with section 78 being deliberately drafted in order to remedy prior issues which had resulted in lien claimants routinely losing *any right* to the holdback.[7] The courts have accordingly held that the *Construction Act* does not include "any overarching intention to favour lien claimants above the interests of mortgagees beyond the value of the holdbacks the legislation requires."[8] As a result, and contrary to the submissions of the Objecting Lien Claimants, there is no general principle that establishes that section 78 is to be interpreted in favour of lien claimants; in particular, there is no reason that the scope of the priority granted to mortgagees under section 78(2) and 78(6) should be interpreted in such a manner, given

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3 *Bianco v. Deem Management Services Limited*, 2021 ONCA 859, at para. 11 [*Bianco* (CA)]; *BCIMC* at para. 9.
4 Ontario, Ministry of the Attorney General, Report of the Attorney General's Advisory Committee on the Draft Construction Lien Act (April 1982) at p. xxxvi-xxxvii [Advisory Committee Report].
5 *Dal Bianco v. Deem Management Services et al*., 2020 ONSC 1500 at para. 38 [*Bianco* (SC)]
6 *Boehmers v. 794561 Ontario Inc.,* 1995 CanLII 660 (ON CA), at para. 7
7 Advisory Committee Report, at pp. xxxvi.
8 *RSG Mechanical Inc. v. 1398796 Ontario Inc*., 2015 ONSC 2070 at para. 29 (Div Ct) (emphasis added).

that lien claimants retain priority with respect the holdback regardless of the application of those sections.

B. Section 78(2) Grants Priority to Building Mortgagees

12. As is set out above, section 78 grants lien claimants a general priority under section 78(1), while at the same time providing a number of exceptions whereby mortgagees obtain priority over lien claimants. One of these exceptions is found in section 78(2), which sets out the priority scheme which governs in the case of a "building mortgage":

> **Building mortgage**
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> **(2)** Where a mortgagee takes a mortgage with the intention to secure the financing of an improvement, the liens arising from the improvement have priority over that mortgage, and any mortgage taken out to repay that mortgage, to the extent of any deficiency in the holdbacks required to be retained by the owner under Part IV, irrespective of when that mortgage, or the mortgage taken out to repay it, is registered. (emphasis added)

13. There is no doubt that section 78(2) is not drafted as clearly as it could be; indeed, the Court of Appeal in *Bianco* commented on the section's "lack of clarity."[9] Nevertheless, the Court in *Bianco* held that the effect of section 78(2) is clear, namely, to restrict the general priority enjoyed by lien claimants, as an exception to the general priority found in section 78(1):[10]

> […] notwithstanding that lack of clarity, I reach the same conclusion on the facts of this case. I accept that the thrust of section 78(2), and the wording "[w]here a mortgagee takes a mortgage with the intention to secure the financing of an improvement", is to restrict the priority of the lien claims relating to that improvement solely to any deficiency in the holdback amount, and not over the mortgage generally.

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9 *Bianco* (CA), at para. 29.

10 *Bianco* (CA), at para. 29 (emphasis added).

14. This accords with a number of previous cases,[11] which held that "section 78(2) addresses the extent of lien claimants' priority when the mortgage is what is commonly referred to as a "building mortgage""[12] with the effect that lien claimants have only a "limited priority" over building mortgages.[13] Secondary sources describe the effect of section 78(2) in the same manner, noting that the practical effect of section 78(2) is to limit the exposure of a mortgagee under a building mortgage to approximately 10% of the value of the work done on an improvement.[14]

15. The Court of Appeal's guidance with respect to interpreting section 78(2) further accords with the intention of the drafters of the section, who viewed section 78(2) as balancing the interests of the parties by ensuring that lien claimants retain priority over the holdback, while at the same time ensuring that a mortgagee's exposure is limited to the holdback:

> […] subsection 2 provides a reasonable balance between the interests of the mortgagees who finance the construction of improvements and the lien claimants who do the actual work on the improvement. It should be noted that building mortgagees enjoy the benefit of the lien claimants' work: as a result of the improvement, the mortgagee's interest will usually be secured against a property which has been enhanced in value. Therefore, it is only fair that the mortgagee's interest be partly subordinated to the liens of the suppliers to the improvement.[15]

16. Despite this extensive authority, the Objecting Lien Claimants argue that section 78(2) does not in any way restrict the extent of a lien claimants' priority, and instead operates solely and exclusively to the benefit of lien claimants. In particular, the Objecting Lien Claimants argue that section 78(2) is not an "exception" to the general priority established by section 78(1), owing to

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11 In addition to the cases cited below, see *New Generation Woodworking Corp. v. Arviv*, 2021 ONSC 1166 at paras. 132-134; *Rosedale Kitchens Inc. v. 2114281 Ontario Inc. et al*, 2012 ONSC 3161 at para. 54 (Master), motion to set aside dismissed 2013 ONSC 3015, aff'd 2014 ONSC 7143.

12 *BCIMC* (CA), at para. 2.

13 *Simpson v. Bridgewater Bank*, 2012 ONSC 714 at para. 33;

14 Justice Leonard Ricchetti and Timothy J. Murphy, *Construction Law in Canada* (Toronto: LexisNexis Canada, 2010) at Chapter 12, IV.A(1). For a full discussion of this issue, see Initial Factum, at paras. 26-29.

15 Advisory Committee Report, at p. 180 (emphasis added).

the differences in language between section 78(2) and other provisions containing exceptions, such as section 78(4) and 78(6).[16]

17. This argument is surprising, given that the Court of Appeal in *Bianco*, which the Objecting Lien Claimants extensively rely upon, clearly states that section 78(2) constitutes an exception to section 78(1). In rejecting the mortgagee's argument that it had priority under section 78(2), the Court explicitly referred to section 78(2) as an "exception" to section 78(1)[17] and further treated section 78(2) and 78(6) in precisely the same manner:

> If a secured party wishes to propel its claim past the general priority given to lien claimants, then it bears the onus of bringing itself clearly within one of the exceptions set out in section 78. In this case, the appellant has failed to discharge that onus, both with respect to section 78(6) and section 78(2).[18]

18. The meaning of the Court of Appeal could not be clearer: section 78(2), like section 78(6) and other provisions containing exceptions, grants a mortgagee priority over lien claims, except with respect to holdback.

19. This conclusion is consistent with prior jurisprudence. In *BCIMC*, for example, the court treated section 78(2) as the "applicable exception" to section 78(1).[19] Similarly, in *Basic Drywall Inc. v. 1539304 Ontario Inc.*,[20] where a subcontractor claimed priority over a mortgagee with respect of the entire amount of its lien, the court found that such a claim was precluded because section 78(2) set the limits of the subcontractor's priority:

> The difficulty with Basic Drywall's position is that under subsection 78(2) of the *Construction Lien Act*, it is clear that the priority of the lien claimants over the lender under the building mortgage does not extend

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16 Responding Factum of Sunbelt Rental of Canada Inc. and Mykon Electric North Ltd., at paras. 29-36.
17 *Bianco* (CA), at paras. 12, 30.
18 *Bianco* (CA), at para. 31 (emphasis added).
19 *BCIMC* (SC), at para. 10.
20 2012 ONSC 1155 [*Basic Drywall*], aff'd 2012 ONSC 6391.

> beyond the deficiency in the amounts required to be withheld by the owner under Part IV of *Construction Lien Act*.[21]

20. The conclusion of the Court of Appeal is also consistent with the intentions of the drafters of section 78, who understood subsections 78(2) and 78(6) as establishing two separate situations in which the priority of a lien claimant would be restricted to the holdback deficiency:

> […] the Committee is of the opinion, that there is a need to secure the holdback […] Since the relative priority between mortgages and the liens are the cause of the problem, we believe that the best way to resolve the problem is to adjust those relative priorities so as to protect the lien claimant's rights in the premises. To do this, we propose to give lien claimants priority to the extent of any deficiency in the holdback over every mortgagee who takes a mortgage for the purpose of securing the financing of the improvement ("building mortgage"); and also over any mortgagee who acquires an interest in the premises subsequent to the commencement of the making of the improvement, irrespective of the purpose of that mortgage.[22]

21. Again, the meaning could not be clearer: the Committee, in order to specifically protect lien claimants' entitlement to the holdback, established, by way of subsections 78(2) and 78(6), two separate, limited priorities, whereby lien claimants would enjoy priority over the holdback only, over building and subsequent mortgages, respectively.

22. It is notable that, despite many of the authorities discussed above being cited in the Receiver's Initial Factum, the Objecting Lien Claimants have entirely failed to address any of these authorities, including the Court of Appeal's statement in *Bianco*. Instead, the Objecting Lien claimants rely solely on alleged language inconsistencies between section 78(2) and other subsections, assumptions regarding the intentions of the drafters of section 78 (which are disproven by the excerpts quoted above), and various other entirely hypothetical concerns.[23] Notably, in addition to failing to address any of the authorities cited above, the Objecting Lien Claimants failed

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21 *Basic Drywall*, at para. 13. As noted by the Objecting Lien Claimants, Section 78 remains the same under the *Construction Act* as it was under the *Construction Lien Act*. Part IV of both Acts is the part dealing with Holdback.

22 Advisory Committee Report, at pp. xxxvi-xxxvii (first emphasis in original).

23 See Responding Factum of Sunbelt Rental of Canada Inc. and Mykon Electric North Ltd., at paras. 38-45.

to cite any authorities of their own with respect to these arguments, and ignore the language in section78(1) of the *Construction Act* which provides that any priority to the lien claimants is expressly subject to the rest of s.78, and ignore the language in subsections 78(2) and (5) of the Construction Act that the priority afforded to lien claimants is expressly only "to the extent" of any deficiency in holdback.

23. The interpretation of section 78(2) advanced by the Objecting Lien Claimants is untenable. It contradicts not only an unambiguous decision of the Court of Appeal addressing the very provision at issue, but also the clear and consistent statements found in the prior jurisprudence, secondary sources, and legislative history. These sources make clear that section 78(2) operates to protect a building mortgagee by limiting lien claimants' priority to the extent of the holdback deficiency.

24. Turning to the facts of this case, undisputed evidence has been provided on this motion demonstrating that the Original Kingsett Mortgages and the Kingsett Mortgage are construction financing, taken with the intention to finance an improvement (the Project).[24] The Objecting Lien Claimants have not taken issue with this evidence, nor with the resulting conclusion that factually, these mortgages qualify as "building mortgages" under section 78(2). No contrary evidence has been provided, and no cross-examinations on the affidavits filed were conducted by the Objecting Lien Claimants.

C. The Re-Registration of the KingSett Mortgage Does Not Alter Priority

25. The Objecting Lien Claimants make much of the fact that the Original KingSett Mortgages were amended and restated in 2022. In effect, the Objecting Lien Claimants argue that, despite the

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[24] Pollack Affidavit at paras. 17-18.

fact that KingSett would have enjoyed undisputed priority under the Original KingSett Mortgages, the procedural re-registration of the Original KingSett Mortgages effectively transformed them into an entirely new mortgage, such that KingSett cannot, under any circumstances, retain its existing priority under either section 78(2) or 78(6).

26. The argument advanced by the Objecting Lien Claimants, if accepted, would represent a complete triumph of form over substance. The KingSett Mortgage is fundamentally a continuation of the Original KingSett Mortgages which exclusively secures Loan Facilities that were already secured under the Original KingSett Mortgages. At all times, the Loan Facilities were secured against title to the Lands, and were visible as registered instruments on the publicly-accessible title to the lands, in a manner which could be reviewed and confirmed by any prospective contractor.[25] At all times, therefore, the reasonable expectations of both KingSett and the Objecting Lien Claimants were that the KingSett Mortgage, as a registered building mortgage securing financing for construction on the lands in question, would rank above any lien claims, except with respect to the holdback.

27. The Objecting Lien Claimants seek to entirely subvert these reasonable expectations, and instead to obtain an unprecedented and unearned windfall entirely on the basis of the procedural re-registration of the KingSett Mortgage. As will be shown below, this extraordinarily formalistic approach is unsupported in the case law, and would undermine the commercial certainty and balancing of the interests which the *Construction Act* seeks to accomplish.

28. Finally, in the alternative, should the re-registration of the KingSett Mortgage be found to otherwise affect KingSett's priority, the doctrine of equitable subrogation (discussed below)

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[25] The Original KingSett Mortgages were not discharged until the day after the KingSett Mortgage was registered: see Initial Factum, at para. 9.

ensures that the KingSett Mortgage retains priority, by subrogating KingSett's position to the priority held by the Original KingSett Mortgages.

(a) The KingSett Mortgage is a Continuation of the Original KingSett Mortgages

29. As is discussed in more detail in the Receiver's Initial Factum, the purpose of the A&R Commitment Letter was solely to consolidate and restate the Prior Commitment Letters and to include certain additional lands as security.[26] The fundamental continuity between the Prior Commitment Letters and the A&R Commitment Letter can be easily observed from the fact that they share all essential details:[27]

(a) In each case, the Lender under the Prior Commitment Letters and the A&R Commitment Letter is "KingSett Mortgage Corporation."

(b) In each case, the borrower under the Prior Commitment Letters and the A&R Commitment Letter is "Mapleview Developments Ltd."

(c) The Prior Commitment Letters and the A&R Commitment Letter deal with the same advances, advanced under substantially the same Loan Facilities, which were in each case intended to be used to finance the same construction: the Project.

30. The Original KingSett Mortgages, which secured the Loan Facilities under the Prior Commitment Letters, were themselves subsequently consolidated by way of the KingSett Mortgage, which exclusively incorporates and secures amounts secured under the Original KingSett Mortgages. The re-registration of the KingSett Mortgage was a purely procedural step

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[26] Pollack Affidavit at para. 19.

[27] The A&R Commitment Letter is found at Pollack Affidavit, Exhibit "D." The Prior Commitment Letters are found at Pollack Affidavit, Exhibit "E."

which was taken to reflect the consolidation of the Prior Commitment Letters, and to facilitate the adding of additional lands to the security, which cannot be done by way of an amendment.[28]

(b) The Re-Registration Does Not Alter Priority Under Section 78(2)

31. The Objecting Lien Claimants argue that the re-registration of the KingSett Mortgage prevents the KingSett Mortgage from retaining its priority under section 78(2). In support of this position, the Objecting Lien Claimants rely entirely on the Court of Appeal's decision in *Bianco*, which the Objecting Lien Claimants allege imports a strict "timing element" into section 78(2).

32. *Bianco* quite simply does not apply in this case. *Bianco* dealt with a priority contest between lien claimants and a third mortgagee. The third mortgagee had advanced funds on an entirely unsecured basis to the owner between 2012 and 2015. A mortgage purporting to secure these advances was both given and registered 3-6 years later, in February 2018. It was in this context that the Court found that the mortgage was retrospective:

> […] the wording of section 78(2) suggests that the intention to secure the financing operates prospectively. In other words, to fit within section 78(2), the mortgagee must take the mortgage with the intention to secure financing of an improvement, which financing is then made. It does not operate retrospectively, that is, with respect to an intention to secure financing of an improvement that has already been made.[29]

33. The facts in the present case could not be more different from *Bianco*. In *Bianco*, the initial advances were entirely unsecured. It was only 3-6 years later, on the eve of insolvency, that the unsecured creditor sought to reorder priority by obtaining security. By proceeding in this way, the unsecured creditor clearly sought to obtain an advantage that it had neither initially bargained for, nor could reasonably expect – indeed, at the time of the Court of Appeal's decision in *Bianco*, there were ongoing proceedings regarding whether the mortgage was entirely invalid under the

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28 Pollack Affidavit at para. 19.
29 *Bianco* (CA), at para. 30.

Fraudulent Conveyances Act and the *Assignment and Preferences Act*.[30] It was in this context that the motion judge noted that a mortgagee is not entitled to "lie in the weeds", advancing funds without registering its mortgage, and then later, surprise lien claimants by purporting to register a mortgage securing those funds retrospectively, after the lien claimants have supplied work to the project without any notice of the fact that the mortgagee had a claim:

> […] an important point must be made in this case regarding the overall priority of lien claimants and subsequent mortgagees. Particularly in large projects, sub trades must be able to adequately assess their risk before undertaking work. If mortgagees are entitled to "lie in the weeds" while advancing funds for the project and then attempt to gain priority later by registering mortgages after liens arise, this would be unfair to lien claimants and contrary to the overall protection intended by the *Act*.[31]

34. In contrast, the Loan Facilities secured under the KingSett Mortgage were from the very beginning secured by charges granted prospectively under the Original KingSett Mortgages. The mere fact that the KingSett Mortgage was subsequently re-registered does not change this fact or transform KingSett's security interest into a retrospective one.

35. Further, unlike in *Bianco*, recognizing the priority of the KingSett Mortgage would not in any way be unfair to the Objecting Lien Claimants. KingSett did not "lie in the weeds," as the unsecured creditor in *Bianco* did. There was no period in which the Loan Facilities were unsecured, and no period in which a mortgage in respect of the Loan Facilities was not registered on title to the Lands. As a result, contractors were at all times able to accurately assess their risk by searching title, and suffered no unfairness as a result of the re-registration of the KingSett Mortgage.

36. Finally, and in the alternative, it is important to note that section 78(2) does not only apply to prospective building mortgages; rather, it also applies to "any mortgage taken out to repay" a

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30 *Bianco* (CA), at fn. 2.
31 *Bianco* (SC), at para. 42 (emphasis added).

building mortgage. This element of the provision was not at issue in *Bianco*, since *Bianco* dealt with a mortgage taken out to secure previously unsecured debt.

37. As is set out above, the KingSett Mortgage consolidates existing debts under the Original KingSett Mortgages, which were indisputably building mortgages taken with the intention to secure financing for the Project.[32] As a result, even to the extent that the KingSett Mortgage is not a building mortgage (which is expressly denied), it retains its priority under section 78(2) since it was taken out to repay the Original KingSett Mortgages, each of which were building mortgages in respect of which the Objecting Lien Claimants priority was restricted to the holdback deficiency.

(c) The Re-Registration Does Not Alter Priority Under Section 78(6)

38. The Objecting Lien Claimants further argue that the re-registration of the KingSett Mortgage prevents the KingSett Mortgage from retaining priority under section 78(6), on the basis that the re-registration means that the advances under the Loan Facilities were not advances "made in respect of" the KingSett Mortgage. It is important to note that this appears to be the only objection raised by the Objecting Lien Claimants with respect to 78(6), as neither dispute that the KingSett Mortgage was registered subsequent to the first lien arising, and that neither of the statutory exceptions set out in section 78(6) applies.[33] As a result, the Objecting Lien Claimants base their entire argument in respect of section 78(6) on the premise that the re-registration of the KingSett Mortgage was sufficient to entirely re-order priority among creditors.

39. It is a well-established principle of statutory interpretation that the words "in respect of" are of the widest possible scope, conveying only some link or connection between two related

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[32] As noted in para. 21, above, the Objecting Lien Claimants have not taken any issue with the evidence establishing that the Original KingSett Mortgages were building mortgages.

[33] See Responding Factum of Sunbelt Rental of Canada Inc. and Mykon Electric North Ltd, at para. 53, in which this is expressly acknowledged.

subjects.[34] The cases cited by the Objecting Lien Claimants do not displace this principle. Rather, the cases cited are clearly distinguishable, as they deal with classic "collateral mortgages," in which an initial debt was subsequently guaranteed by a party other than the initial debtor, who provided a collateral mortgage as security for the guarantee. In a collateral mortgage of this type, no amounts are ever advanced to the collateral mortgagee (or anyone else), as the mortgage is intended to secure advances which have already been made to the initial debtor.

40. The Receiver does not dispute that the courts have held that a classic collateral mortgage cannot obtain priority under section 78(6). The reasoning for this conclusion is clear and unsurprising: under a collateral mortgage, no advances are ever made to the collateral mortgagor nor the initial debtor, neither of whom acquires control over any funds, nor obtains any direct benefit as a result of the mortgage.

41. For example, in *XDG Ltd. v. 1099606 Ontario Ltd.*,[35] the owner of real property ("109") guaranteed the debts of a related party ("Euro United") to a lender. The owner granted a collateral mortgage over its lands to secure past advances made by the lender to Euro United..[36] At issue was whether the mortgage securing the guarantee held priority over various construction lien claims over the property. The court found that it did not, as "no advance was made to 109 nor did 109 benefit in any manner whatsoever."[37]

42. Similarly, in *Jade-Kennedy Development Corporation (Re)*., the owner of a condominium project ("Jade-Kennedy") had granted a number of mortgages in respect of the project lands,

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[34] *R v Nowegijick*, 1983 CanLII 18 (SCC) at p. 39. See also *Sino-Forest Corporation*, 2012 ONCA 816 at para 41. See also *Jade-Kennedy Development Corporation (Re)*., 2016 ONSC 7125.at paras 50-51 [*Jade-Kenndy*], in which the court stated that "it is also clear that the phrase 'in respect of' is intended to be broader than 'under' insofar as 'under' refers to advances made directly by a mortgagee to a mortgagor pursuant to a mortgage loan."

[35] 2002 CanLII 22043 (ON SC) [*XDG*].

[36] *XDG*, at paras. 2-5

[37] *XDG*, at para. 94.

including a collateral mortgage in favour of Laurentian Bank which secured a guarantee given in respect of past advances from Laurentian Bank to a third party.[38] The court found that the collateral mortgage did not have priority under section 78(6), as any advances had been made to the third party under the existing debt facility, not to Jade-Kennedy.[39]

43. The *561861 Ontario Ltd. v. 1085043 Ontario Inc.* case also involved a collateral mortgage (it also involved s.78(3) of the *Construction Act*, a subsection not at issue on this motion).[40] In that case, a sister loaned money to her brother to buy out his ex-wife's interest in a matrimonial home. The loan was secured by a mortgage. Upon the brother taking sole title to the home, the land merged with the neighbouring farm owned by the brother. The brother then sold the land to a third party. The sister's mortgage was discharged, and she was granted a new collateral mortgage over the third party's land (to secure repayment by the brother). Like in *XGD* and *Jade-Kennedy*, the mortgage in *561861* was a collateral one – there were no advances to the owner of the liened property, and the new collateral mortgage was granted to a different mortgagor.[41]

44. The recent decision in *Clarkson Road Developments GP Inc. et al (Re)*[42] further made clear that the primary concern is not the timing of the advances; rather, it is the fact that the mortgage secures a guarantee of third-party debt, such that the mortgagee never receives any advances at all:

> Although the collateral mortgage in Jade-Kennedy secured advances made to the principal borrower before and after the registration of the collateral mortgage, the application judge did not hold that this was a material factor in relation to his conclusion that there was no advance under the collateral mortgage. There is no reason, in principle, why a mortgage must secure a guarantee of existing indebtedness to qualify as a "true" collateral mortgage. The significant factor is that the mortgage secures the guarantee given by the mortgagor of indebtedness owed by another entity, the

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38 *Jade-Kennedy*, at para. 24.
39 *Jade-Kennedy*, at paras. 55-56.
40 *561861 Ontario Ltd v 1085043 Ontario Inc*, 1998 CarswellOnt 2935 (Ont Gen Div) [*561861*].
41 *561861* at paras 3, 4, 6, 8 and 12.
42 2024 ONSC 4625 [*Clarkson Road*].

> principal debtor. In such circumstances, the advance is made to the principal debtor, not to the guarantor.[43]

45. Again, the differences from the present case could not be starker. In both *XDG* and *Jade-Kennedy*, the mortgages in question were granted by strangers to the initial debt in order to secure a third-party guarantee. As result, there could be no doubt that the mortgages were true collateral mortgages which were fundamentally distinct from the underlying debt. Further, as true collateral mortgages, no amounts were ever advanced under them, whether to the mortgagee or any another party. In these circumstances, it is hardly surprising that the court found that no advances had been made "in respect of" the mortgages.

46. In contrast, the advances made under the Loan Facilities were not granted to an unrelated party, but rather directly to Mapleview, which benefitted from the advances and used them to finance construction of the Project. The KingSett Mortgage does not secure a guarantee; rather it directly secures the amounts owing under the same Loan Facilities. The mere fact that the KingSett Mortgage was re-registered does not change this fact, as the KingSett Mortgage directly secures the same advances as the Original KingSett Mortgages, made under the same Loan Facilities, to the same borrower.

47. *Bianco* also does not assist the Objecting Lien Claimants. As discussed above, *Bianco* dealt with a situation in which a mortgage was both given and registered more than three years after the final advance of unsecured debt. As a result, the Court of Appeal unsurprisingly found that the unsecured advances were not made "in respect of" the mortgage. In contrast, the KingSett Mortgage is the continuation of the Original KingSett Mortgages, which were indisputably in existence, and registered on title, at the time the advances were made.

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[43] *Clarkson Road*, at para. 72 (emphasis added).

(d) The Objecting Lien Claimants' Approach Would Undermine the Operation of the *Construction Act*

48. In addition, the overly-technical interpretive approach adopted by the Objecting Lien Claimants is contrary to the purpose and policy underlying the *Construction Act*.

49. Section 78, like the *Construction Act* as a whole, is designed to balance the interests of the various parties involved in construction in a manner that facilitates construction.[44] This balancing act animated the entirety of the drafting of the *Construction Lien Act*, with the Attorney General noting that the "entire thrust of the revision has been to prevent needless impediments to the flow of money on a construction project while protecting the interests of those who have contributed services and materials."[45] In particular, the Attorney General stated that while section 78 was designed in part to protect the interests of lien claimants, it endeavoured to do so "without destroying the desire to build."[46]

50. The approach urged by the Objecting Lien Claimants would directly interfere with this key objective of the *Construction Act*. The current certainty – in which lien claimants know they retain priority with respect to the holdback, while mortgagees know their exposure is limited to the holdback amount, so long as they do not advance in the face of a lien – would be undermined. Mortgagees advancing construction financing would find themselves unable to refinance mortgage debt, or to add to the existing land offered as security (which requires re-registration[47]), without

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44 *BCIMC* (SC), at para. 27.

45 Ontario, Legislative Assembly, "Bill 216, An Act to revise the Mechanics' Lien Act," 2nd reading, *Hansard*, 32-2 (25 January 1983) (Hon. Mr. McMurtry) [*Hansard*] (emphasis added).

46 *Hansard*.

47 The evidence referred to in the Pollack Affidavit at para. 19 on this point is unrefuted on this motion.

entirely losing their normal priority over lien claimants. Particularly on multi-year projects, the chilling effect on the ability to refinance or otherwise re-register would be substantial.

51. It must also be noted that there is no prejudice whatsoever to the lien claimants through the re-registration of the KingSett Mortgage. This motion simply represents an attempt to parlay a minor procedural step on the part of a mortgagee into a huge and unjustified alteration of priority for the lien claimants, upon the basis of a creative process of statutory interpretation.

(e) The Doctrine of Equitable Subrogation Applies

52. Finally, even if the re-registration of the KingSett Mortgage affected the priority of the current KingSett Mortgage (which is expressly denied), the doctrine of equitable subrogation ensures that the KingSett Mortgage would not in fact lose its priority, as it would be subrogated to the position and priority of the Original KingSett Mortgages.

53. The doctrine of equitable subrogation permits a mortgagee that pays offs or replaces a prior mortgage to stand in the shoes of the prior mortgagee. In *Midland Mortgage Corp. v. 784401 Ontario Ltd*., the Court of Appeal accepted the following summary of equitable subrogation:

> ...where a third party at the request of a mortgagor pays off a first mortgage with a view to becoming himself a first mortgagee of the property, he becomes, in default of evidence of intention to the contrary, entitled in equity to stand, as against the property, in the shoes of the first mortgagee.[48]

[48] 1997 CanLII 1946 (ON CA) at para. 14 [*Midland Mortgage Corp*.], citing *Crosbie-Hill v. Sayer*, [1908] 1 Ch. 866 (Eng. Ch. Div.).

54. The Court of Appeal made clear that this doctrine did not only apply to third parties, but also applies to "a first mortgagee who renews, replaces, refinances, amends or increases his mortgage,"[49] and applies even where the prior mortgage has been discharged.[50]

55. The fundamental purpose of equitable subrogation is to ensure fairness to the lender by permitting them to retain the priority enjoyed by the prior mortgagee:

> The fundamental principle underlying the equitable right of subrogation is one of fairness for a lender who renews, replaces, refinances or amends its mortgage or gives a new mortgage […] by subrogation the mortgagee of the new mortgage is entitled in priority for the part of the amount advanced to pay off the outstanding mortgage or mortgage with interest at the original rate.[51]

56. As a result of this emphasis on fairness, the courts have held that equitable subrogation is granted where doing so would restore the parties to the priorities they would have enjoyed absent the replacement of the prior mortgage, as "[w]here the parties have been replaced to their former positions by subrogation, no injustice is done."[52]

57. The doctrine of equitable subrogation applies regardless of whether the land in question is also subject to a specific statutory regime,[53] which does not abolish the doctrine in the absence of specific language to the contrary.[54] Further, the doctrine is not confined to issues of priority

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49 *Midland Mortgage Corp.*, at para. 15. See also *Mutual Trust Co. v. Creditview Estate Homes Ltd* 1997 CanLII 1107 (ON CA) at para. 35 [*Mutual Trust* (CA)], in which the court held that "whether it is a third party or the first mortgagee itself should make no difference having regard to the rationale underlying the doctrine."

50 *Mutual Trust* (CA), at para. 34.

51 Donald Lamont, *Lamont on Real Estate Conveyancing*, 2nd Edition, (Toronto: Thomson Reuters Canada, 2020), at § 23:35 (emphasis added).

52 *O'Brien v. Royal Bank*, 2008 CanLII 6422 (ON SC) at para. 27.

53 See, e.g., *Mutual Trust Co. v. Creditview Estate Homes Ltd.*, 1994 CarswellOnt 312 (ONSC) at paras. 11-12, 16 [*Mutual Trust* (SC)], in which equitable subrogation was found to still apply regardless of the fact that the lands in question were subject to the priority scheme found in the *Registry Act*, R.S.O. 1990, c. R.20. This reasoning was adopted by the Court of Appeal in *Mutual Trust* (Appeal Decision) at para. 32.

54 *Mutual Trust* (SC), at para. 16.

between mortgagees; rather it applies broadly to relation to other types of prejudicial instrument, such as construction liens.[55]

58. This was the case in *Coupland Acceptance Ltd. v. Walsh*.[56] In *Coupland*, a first-ranking mortgage had been registered against a property. Subsequently, mechanics liens under the *Mechanics Lien Act*[57] had been registered against the property. Finally, a third mortgage had been registered against the property, following the registration of the mechanics liens. Part of the third mortgage represented new advances, while another part was used to pay out the first mortgage.

59. It was not disputed that the lien claimants had priority with respect to the new advances, which had been advanced in the face of a lien. At issue was whether the third mortgagee had priority over the lien claimants with respect to the amounts used to pay out the first mortgage. The Supreme Court found strongly in favour of the third mortgagee, holding that to do otherwise result in an obvious injustice in favour of the lien claimants:

> While s. 13(1) of the [*Mechanics Lien Act*] gives priority to the lien over all payments or advances made under a mortgage after registration of the lien, the section is not to be construed as affecting the right relied upon here by the appellant. The appellant does not rely upon its mortgage for priority as to the moneys here in question but upon the equitable right to stand in the place of the Kerbel mortgagees whose priority to the lien is unquestionable. The position of the lienholder remains the same as it was before the appellant intervened and it would, in my opinion, require more than is to be found in the section to bring about a result so unjust that it would […] permit the lienholder, by a mere accident, to obtain priority at the expense of people who never intended to benefit him.[58]

60. *Coupland* closely parallels the present facts and is dispositive. The Objecting Lien Claimants, who suffered absolutely no prejudice as a result of the re-registration of the KingSett

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55 *Mutual Trust* (SC) at para. 14, which reasoning was adopted in full by the Court of Appeal in *Mutual Trust* (CA) at para. 25.
56 [1954] SCR 90 (SCC) [*Coupland*].
57 R.S.O., 1950, c. 227
58 *Coupland*, at para. 6 (emphasis added).

Mortgage, seek to obtain priority at the expense of KingSett, despite the fact that KingSett and Mapleview, as parties to the A&R Commitment Letter, never intended to benefit the Objecting Lien Claimants.

61. Granting the Objecting Lien Claimants the priority they seek would result in a massive and wholly unearned, unfair and inequitable windfall to the Objecting Lien Claimants. As a result, to the extent that the re-registration of the KingSett Mortgage affected KingSett's priority (which is not admitted), the doctrine of equitable subrogation can, and should, be applied to restore the parties to the priorities enjoyed under the Original KingSett mortgages.

D. The Receiver Has Acted Appropriately

62. In addition to their submissions regarding the priority of the KingSett Mortgage, Fuller Landau Group Inc. argues that, by making submissions on this motion and taking a position on the scope of the Priority Payables, the Receiver has somehow violated its fiduciary obligations.

63. This attack on the impartiality of the Receiver is entirely meritless. There is no inter-creditor dispute on this motion, and neither the Receiver nor KingSett has any financial stake in the outcome of this motion. KingSett has been repaid in full from the proceeds of the transaction contemplated by the Sale Agreement. On this motion, the Receiver simply seeks a determination of priorities, which is relevant to the calculation of the purchase price under the purchase agreement it negotiated with Dunsire Homes Inc. (the "**Purchase Price**"). It is within the Receiver's rights (and obligations) to do.

64. Under the terms of the order appointing the Receiver, the Receiver was specifically authorized to "deal with any lien claims" arising under the *Construction Act*, and to make any

"required distributions" in respect of those lien claims.[59] In order to ascertain the priority of the claims against Mapleview – and therefore the Purchase Price and the extent of any "required distributions" to lien claimants – the Receiver, acting in good faith, consulted its counsel regarding the priority granted to lien claimants under the *Construction Act*, and was advised that lien claimant's priority was limited to the holdback deficiency.[60] Distributions, which are a function of priority, cannot proceed without a Court Order, and motions for such Orders are routinely brought by receivers (including Fuller Landau Group Inc.), even where the priorities remain disputed among creditors, and implicitly require receivers to take a position on priority in such motions.[61] The Receiver was therefore required to take a position on this issue; had it not done so, it would have been shirking its duty to stakeholders and to the court.

65. It does not somehow violate the Receiver's neutrality to stand by its recommendation and to defend it in court. The AVO expressly provides that "the Receiver is authorized and directed to pay from time to time from the Lien Claimants' Reserve any amounts in respect of Priority Payable Claims […] that […] is ordered by this Court […]". It is proper for the Receiver to seek an order from this Court regarding priority of the Priority Payable Claims asserted by the Lien Claimants in order for the Receiver to discharge its duties under the AVO. As the courts have stated, the "fact that a receiver recommends a course of action does not mean that it has lost its neutrality. The Receiver has a duty to exercise its judgment under the mandate given to it by the Receivership Order and to make recommendations to the court."[62] In *BCIMC*, for example, the Receiver acted

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59 *KingSett Mortgage Corporation v. Mapleview Developments Ltd. et al.*, (March 21, 2024) Ont. S.C.J. [Commercial List] Court File No. CV-24-00716511-00CL (Order Appointing Receiver), at para. 4(i) (emphasis added).

60 Second Report of the Receiver dated July 26, 2024, at sections 7.1.3 and 7.1.6.

61 See, e.g. *Royal Bank of Canada v. Atlas Block Co.*, 2014 ONSC 1531, in which the recommendation of the Receiver regarding the allocation of the proceeds of transactions between two secured creditors was accepted by the court, despite the objections of one of the secured creditors (at paras. 1, 39).

62 *2403177 Ontario Inc. v. Bending Lake Iron Group Ltd.*, 2016 ONSC 199 at para. 102, leave to appeal ref'd 2016 ONCA 485.

as respondent on the priority motion and made direct submissions regarding the scope of lien claimant's priority.[63] Neither the motion judge nor the Court of Appeal expressed any concern with this process.

66. Further, it is highly disingenuous for Fuller Landau, itself acting in its capacity as receiver of certain Lien Claimants, to claim that the Receiver is somehow unable to make a recommendation to the Court, to defend its recommendation once it is made, to take a position with respect to the Purchase Price under the agreement which the Receiver negotiated and serves as vendor, or to take a position with respect to priority. Fuller Landau, based on its extensive experience as a receiver, knows full well that receivers can, and must, take a position in these circumstances. Nevertheless, Fuller Landau has opted to waste this Court's time by making frivolous attacks on the Receiver's integrity.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 11th day of September 2024.

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63 *BCIMC* (CA), at paras. 4, 7.

SCHEDULE "A": LIST OF AUTHORITIES

Cases

1. *2403177 Ontario Inc. v. Bending Lake Iron Group Ltd.*, 2016 ONSC 199
2. *561861 Ontario Ltd. v. 1085043 Ontario Inc.*, 1998 CarswellOnt 2935 (Ont Gen Div)
3. *Basic Drywall Inc. v. 1539304 Ontario Inc.*, 2012 ONSC 1155
4. *BCIMC Construction Fund Corp. et al. v. 33 Yorkville Residences Inc et al.*, 2022 ONSC 2326
5. *BCIMC Construction Fund Corporation v. 33 Yorkville Residences Inc.*, 2023 ONCA 1
6. *Bianco v. Deem Management Services Limited*, 2021 ONCA 859
7. *Boehmers v. 794561 Ontario Inc.,* 1995 CanLII 660 (ON CA)
8. *Coupland Acceptance Ltd. v. Walsh*, [1954] SCR 90 (SCC)
9. *Clarkson Road Developments GP Inc. et al (Re)*, 2024 ONSC 4625
10. *Dal Bianco v. Deem Management Services et al.*, 2020 ONSC 1500
11. *Jade-Kennedy Development Corporation (Re).*, 2016 ONSC 7125
12. *Midland Mortgage Corp. v. 784401 Ontario Ltd.*, 1997 CanLII 1946 (ON CA)
13. *Mutual Trust Co. v. Creditview Estate Homes Ltd.*, 1994 CarswellOnt 312 (ON SC)
14. *Mutual Trust Co. v. Creditview Estate Homes Ltd* 1997 CanLII 1107 (ON CA)
15. *New Generation Woodworking Corp. v. Arviv*, 2021 ONSC 1166
16. *O'Brien v. Royal Bank*, 2008 CanLII 6422 (ON SC)
17. *R v Nowegijick*, 1983 CanLII 18 (SCC)
18. *Rosedale Kitchens Inc. v. 2114281 Ontario Inc. et al*, 2012 ONSC 3161
19. *Royal Bank of Canada v. Atlas Block Co.*, 2014 ONSC 1531
20. *RSG Mechanical Inc. v. 1398796 Ontario Inc.*, 2015 ONSC 2070
21. *Simpson v. Bridgewater Bank*, 2012 ONSC 714
22. *Sino-Forest Corporation*, 2012 ONCA 816
23. *XDG Ltd. v. 1099606 Ontario Ltd.*, 2002 CanLII 22043 (ON SC)

Secondary Sources

1. Donald Lamont, *Lamont on Real Estate Conveyancing*, 2nd Edition, (Toronto: Thomson Reuters Canada, 2020)

2. Justice Leonard Ricchetti, Timothy J. Murphy, *Construction Law in Canada* (Toronto: LexisNexis Canada, 2010)

SCHEDULE "B"
TEXT OF STATUTES, REGULATIONS & BY-LAWS

CONSTRUCTION ACT

R.S.O. 1990, c C.30, as amended

Priority over mortgages, etc.

78 (1) Except as provided in this section, the liens arising from an improvement have priority over all conveyances, mortgages or other agreements affecting the owner's interest in the premises.

Building mortgage

(2) Where a mortgagee takes a mortgage with the intention to secure the financing of an improvement, the liens arising from the improvement have priority over that mortgage, and any mortgage taken out to repay that mortgage, to the extent of any deficiency in the holdbacks required to be retained by the owner under Part IV, irrespective of when that mortgage, or the mortgage taken out to repay it, is registered.

Prior mortgages, prior advances

(3) Subject to subsection (2), and without limiting the effect of subsection (4), all conveyances, mortgages or other agreements affecting the owner's interest in the premises that were registered prior to the time when the first lien arose in respect of an improvement have priority over the liens arising from the improvement to the extent of the lesser of,

(a) the actual value of the premises at the time when the first lien arose; and

(b) the total of all amounts that prior to that time were,

(i) advanced in the case of a mortgage, and

(ii) advanced or secured in the case of a conveyance or other agreement**.**

Prior mortgages, subsequent advances

(4) Subject to subsection (2), a conveyance, mortgage or other agreement affecting the owner's interest in the premises that was registered prior to the time when the first lien arose in respect of an improvement, has priority, in addition to the priority to which it is entitled under subsection (3), over the liens arising from the improvement, to the extent of any advance made in respect of that conveyance, mortgage or other agreement after the time when the first lien arose, unless,

(a) at the time when the advance was made, there was a preserved or perfected lien against the premises; or

(b) prior to the time when the advance was made, the person making the advance had received written notice of a lien.

Special priority against subsequent mortgages

(5) Where a mortgage affecting the owner's interest in the premises is registered after the time when the first lien arose in respect of an improvement, the liens arising from the improvement have priority over the mortgage to the extent of any deficiency in the holdbacks required to be retained by the owner under Part IV.

General priority against subsequent mortgages

(6) Subject to subsections (2) and (5), a conveyance, mortgage or other agreement affecting the owner's interest in the premises that is registered after the time when the first lien arose in respect to the improvement, has priority over the liens arising from the improvement to the extent of any advance made in respect of that conveyance, mortgage or other agreement, unless,

(a) at the time when the advance was made, there was a preserved or perfected lien against the premises; or

(b) prior to the time when the advance was made, the person making the advance had received written notice of a lien.

IN THE MATTER OF AN APPLICATION UNDER SUBSECTION 243(1) OF THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, c. B-3, AS AMENDED, AND SECTION 101 OF THE *COURTS OF JUSTICE ACT*, R.S.O. 1990, c. C.43, AS AMENDED

KINGSETT MORTGAGE CORPORATION	**and**	**MAPLEVIEW DEVELOPMENTS LTD., PACE MAPLEVIEW LTD. and 2552741 ONTARIO INC.**
Applicant		Respondents

Court File No.: CV-24-00716511-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

PROCEEDING COMMENCED AT TORONTO

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