Court of Appeal No. COA-22-CV-0451
Court File No. BK-21-02734090-0031

**COURT OF APPEAL FOR ONTARIO**

IN THE MATTER OF THE *BANKRUPTCY AND INSOLVENCY ACT,* R.S.C. 1985, C. B-3 AS AMENDED

IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF YG LIMITED PARTNERSHIP AND YSL RESIDENCES INC. OF THE CITY OF TORONTO, IN THE PROVINCE OF ONTARIO

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**BOOK OF AUTHORITIES OF THE PROPOSAL TRUSTEE KSV RESTRUCTURING INC.**

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March 23, 2023

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**INDEX**

# IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Asian Concepts Franchising Corporation (Re),* 2018 BCSC 1022

Date: 20180621
Docket: B131424
Registry: Vancouver



Between:

**In Bankruptcy and Insolvency**

**In the Matter of the Proposal of Asian Concepts Franchising Corporation**

Before: The Honourable Madam Justice Fitzpatrick

## Reasons for Judgment

| | |
|---|---|
| Counsel for Grant Thornton Limited, Trustee in the Proposal of Asian Concepts Franchising Corporation: | Kimberley A. Robertson<br>Blair McRadu |
| Counsel for Adrenaline Drive Inc.: | Jeremy H. H. Hockin, Q.C.<br>Heather A. Frydenlund |
| Counsel for Asian Concepts Franchising Corporation: | Gordon G. Plottel |
| Place and Date of Hearing: | Vancouver, B.C.<br>March 27, 2018 |
| Place and Date of Judgment: | Vancouver, B.C.<br>June 21, 2018 |

## INTRODUCTION

[1] These proceedings concern the proposal of Asian Concepts Franchising Corporation ("ACFC"), which was filed pursuant to the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "*BIA*").

[2] One of ACFC's creditors, Adrenaline Drive Inc. ("Adrenaline"), is vigorously opposed to this proposal. Adrenaline has advanced its opposition in a number of ways. It has voted against the proposal and it has magnified its opposition by successfully appealing the Trustee's determination as to the amount of its claim, although the newly determined amount of its claim was not sufficient to carry the vote. Adrenaline also intends to oppose any court approval of the proposal, if approved by the creditors, pursuant to s. 59 of the *BIA*.

[3] This application by Adrenaline is another means by which it can oppose the proposal process. It amounts to a challenge to the amount of the claim of another creditor, WB Heartland Restaurant Inc. ("Heartland"), in terms of its right to vote in favour of the Amended Proposal (as later defined in these reasons) and any later distribution.

## BACKGROUND

### a) The Adrenaline Litigation

[4] On September 9, 2008, Adrenaline and ACFC, the franchisor of the Wok Box Fresh Asian Kitchen franchise, entered into a Master Developer Agreement (the "MDA") governing the operation and development of "Wok Box" franchise locations located within a territory. The territory initially included all of northern Alberta, Saskatchewan and Manitoba.

[5] The initial term of the MDA was for a period of 10 years. Upon expiry, the MDA provided that Adrenaline had the option of renewing the MDA for an unlimited number of additional 10-year terms upon, among other things, payment of a $25,000 renewal fee. Adrenaline earned substantial royalty fees under the MDA, with average monthly payments of approximately $35,000.

[6] By February 2012, Adrenaline had expanded the number of Wok Box restaurants in its territory to include at least 26 locations.

[7] ACFC ceased making royalty payments to Adrenaline in January or February 2012. On February 27, 2012, ACFC purported to terminate the MDA. Two days later, ACFC notified all franchisees in Adrenaline's former territory that the franchises had been assigned to WB Franchising Ltd. (“WB Franchising”).

[8] On June 11, 2012, Adrenaline filed a statement of claim in the Alberta Court of Queen's Bench. One of its claims was that ACFC had breached the MDA and wrongfully terminated it without cause. Adrenaline claimed liquidated damages of $166,774.82 and unliquidated damages of $8 million. Adrenaline filed its claim against both ACFC and WB Franchising and also, Scott Bender, the principal of both companies.

[9] In its Alberta action, Adrenaline alleged that the defendants conspired to deprive it of the benefit of the MDA. Adrenaline was aware that, in 2011, ACFC was also facing court actions or claims by other creditors, including that of 1448244 Alberta Inc., in excess of $1.7 million. Adrenaline alleged in its action that, to avoid all these potential claims, Mr. Bender, as the directing mind of ACFC, WB Franchising and 0839297 B.C. Ltd. (“839”) developed a scheme. 839 is an entity also controlled by Mr. Bender. It holds the Wok Box trademark license, which is an important asset within the Wok Box franchising system.

[10] Adrenaline alleges that Mr. Bender’s scheme involved: firstly, terminating the master development agreements, including Adrenaline’s MDA, so that the income or royalty streams would revert to ACFC; and, secondly, arranging to transfer the trademarks, franchise agreements and the other assets required to operate the Wok Box franchise from ACFC to WB Franchising. Adrenaline alleges that WB Franchising paid a small amount for the tangible assets and that it paid nothing for the transfer of the franchise agreements and intellectual property that WB Franchising received from ACFC.

[11] The MDA contained a term that required arbitration of any dispute to take place in British Columbia. In accordance with this provision, Adrenaline commenced arbitration proceedings against ACFC in British Columbia.

### b) The *BIA* Proposal Proceedings

[12] On November 20, 2013, shortly after the arbitration proceedings were scheduled, ACFC filed a notice of intention to make a proposal to its creditors pursuant to Division I of Part III of the *BIA* (s. 50.4). In the usual course, this filing resulted in a stay of proceedings in relation to Adrenaline's arbitration proceedings. Grant Thornton Limited was to act as the Trustee under the proposal.

[13] On December 20, 2013, ACFC filed its proposal pursuant to s. 62 of the *BIA*. On that date, Mr. Bender, described by the Trustee as ACFC's "sole" director, executed ACFC's statement of affairs. The statement disclosed total unsecured claims of $361,312.74 and the balance of secured claims of $610,000, for total unsecured claims of $971,312.74.

[14] The Trustee's report to the creditors in respect of the proposal indicated that ACFC was no longer carrying on business, having sold its assets in 2012/2013. The only remaining asset indicated was a minimal bank balance of $2,700. Nevertheless, the proposal was that "related third parties" would fund monies into the proceedings in order to create a pool of not less than $300,000 for payment to the unsecured creditors.

[15] On February 14, 2014, ACFC amended its initial proposal (the "Amended Proposal") and it is the Amended Proposal upon which the creditors' would ultimately vote. In substance, the proposal again provided that a sum of money would be funded (then $325,000) in which all the unsecured creditors would share *pro rata* based on their proven claims. On February 27, 2014, the first meeting of creditors was held, although it was adjourned to allow distribution of the Amended Proposal to all creditors for their consideration.

[16] There were some unusual aspects of the Amended Proposal, particularly in light of Adrenaline's allegations in its Alberta action and perhaps allegations by other creditors. The Amended Proposal provided in part:

> 1. In this Proposal:
>
> > (e) "Contributors" means WB Franchising Limited and 0839297 B.C. Ltd., who have Claims or potential Claims for indemnity against the Debtor.
>
> …
>
> 15. Unsecured Creditors will accept the payments provided for in this Proposal in complete satisfaction of all their Claims, as against the Debtor or any of the Contributors .... all of which shall be released upon payment of the amounts provided for in this Proposal….
>
> 16. Upon performance by the Debtor of its obligations under this Proposal, each and every Director of the Debtor shall be released from any and all demands, claims, debts, judgments and other recoveries on account of any potential, contingent or actual statutory liability of whatever nature ....

[17] Accordingly, if the creditors accept the Amended Proposal and it is approved by this Court in accordance with the *BIA*, Adrenaline's ability to pursue its claim in its Alberta action or the arbitration proceedings will be adversely affected, if not eliminated, as against certain persons. This will include Adrenaline's ability to pursue WB Franchising and 839 (since they are "Contributors" under the Amended Proposal). It will also affect Adrenaline's ability to pursue ACFC's directors, being Mr. Bender and Lawrence Eade.

[18] As stated above, the focus of this application is the validity of Heartland's claim against ACFC. A brief history of Heartland's claim both prior to and in the proposal proceedings is as follows:

a) prior to the filing of the notice of intention, Heartland filed a claim in the Ontario Superior Court of Justice against ACFC and three of ACFC's directors, including Mr. Bender, Mr. Eade and another principal of ACFC, Chris Bullock;

b) in its statement of affairs sworn December 20, 2013 by Mr. Bender, ACFC attached no value to Heartland's claim;

c) just one day after the filing of ACFC's initial proposal on December 20, 2013, Heartland was dissolved by way of a certificate of dissolution issued on December 21, 2013;

d) notwithstanding its dissolution, Heartland filed a proof of claim of approximately $2.38 million against ACFC. In addition, on January 7, 2014, Heartland sent in a voting letter indicating that it was voting against ACFC's proposal. On January 8, 2014, Heartland's counsel in particular objected to the releases sought in the proposal in relation to Messrs. Bender, Eade and Bullock;

e) on February 27, 2014, Heartland submitted a replacement proof of claim and voting letter. Heartland's claim was now presented and allowed at $1.6 million and Heartland indicated that it was voting in favour of the Amended Proposal; and

f) the acceptance of Heartland's claim by the Trustee at even this reduced amount was such that it's claim constituted approximately 51% of the overall value of the total claims allowed by the Trustee. As such, Heartland's support contributed greatly to ACFC meeting the 2/3 in value of creditor claims threshold needed to approve the Amended Proposal later on March 10, 2014.

[19] Adrenaline was not particularly aware as to why ACFC and Heartland agreed to reduce Heartland's claim and why Heartland changed its vote at some point after January 7, 2014, and before February 27, 2014. It was on the latter date when the Trustee indicated that Heartland's claim had been "settled." However, there are statements and court filings which give some context and suggest that negotiations between ACFC and Heartland led to this result:

a) the Trustee's minutes of a meeting of creditors on February 27, 2014 states:

> Two other claims from WB Heartland and from 1448244 Alberta Inc. have been admitted pursuant to negotiations and a settlement of amounts between the debtor and respective creditors.

b) according to documents filed in Heartland's Ontario action, a settlement was reached with Mr. Bender and Mr. Eade, which resulted in that action being dismissed as against them on February 21, 2014. The action continued against the remaining parties, including Mr. Bullock, who apparently agreed to settle Heartland's claim for $50,000. In February 2016, when Mr. Bullock did not perform his part of the settlement, Heartland obtained judgment against him for the settlement amounts and costs.

[20] On March 10, 2014, a further meeting was held at which ACFC presented the Amended Proposal to its unsecured creditors for consideration and voting purposes. In accordance with s. 54(2) of the *BIA*, the requisite majority of creditors approved the proposal, both in dollar amount (98%) and number (13/14). Adrenaline's claim had been filed in the amount of $8 million, consistent with its claim in the Alberta action; however, the Trustee disallowed most of that amount and Adrenaline's claim was valued at only $65,720. Adrenaline was the only creditor to vote against the Amended Proposal. All other creditors, including Heartland, with approximately $3 million in value collectively, voted in favour.

**c) Post-Voting Events**

[21] Adrenaline was unhappy with its claim being valued at $65,720, particularly since it meant that its negative vote was not sufficient to defeat the Amended Proposal.

[22] It filed an appeal of the Trustee's determination of its claim pursuant to s. 135(4) of the *BIA*. That appeal resulted in this Court directing that the Trustee further evaluate Adrenaline's claim based on a more expansive definition of what constituted, or should have constituted, the record before the Trustee. Eventually, on

January 15, 2015, the Trustee valued Adrenaline's claim for voting purposes at $754,720.25.

*[23]* Adrenaline appealed again. On August 17, 2017, Registrar Muir agreed that Adrenaline's claim should be increased to $1,122,720.25 for voting purposes: *Asian Concepts Franchising Corporation (Re)*, 2017 BCSC 1452 at para. 123 [*Asian Concepts*]. This further increase was still not sufficient to cause a defeat of the Amended Proposal, since Adrenaline's claim constituted only 26.7% in value of the voting creditors.

[24] In the meantime, after the voting, Adrenaline was also taking aim at other creditors' claims or the value of those claims, which had resulted in a vote approving the Amended Proposal. This included Heartland's claim.

[25] Unfortunately, as with the determination of Adrenaline's claim, the challenges to these other claims has equally been a drawn-out and litigious process that has significantly delayed the resolution of this proposal proceeding. This process has been marked by considerable disagreements and a fractious relationship that arose between Adrenaline and the Trustee as to both the substance of Adrenaline's objections, and also the procedures necessary to move the issues forward.

[26] The Trustee refused Adrenaline's request for copies of the proofs of claim filed by various creditors, including that of Heartland. The Trustee only provided them after Registrar Muir ordered that production on February 12, 2015.

[27] Once it had reviewed the materials provided by the Trustee with respect to Heartland's claim, Adrenaline wrote to the Trustee pointing out what it considered were discrepancies in that claim. On May 24, 2016, the Trustee disagreed with Adrenaline's assessment of Heartland's claim and provided a detailed justification for allowing Heartland's claim at $1.6 million. I will address the Trustee's response in more detail below.

[28] On July 14, 2017, Registrar Muir directed that Adrenaline write to the holders of the third party claimants, including Heartland, for the purposes of notifying them of

Adrenaline's intention to challenge their claims in court. On July 18, 2017, Adrenaline's counsel did just that. On July 31, 2017, Heartland's principal, Rick Menendez replied, stating that Heartland would not be attending any court hearing.

[29] As directed by Registrar Muir, Adrenaline was to file and serve separate applications relating to its challenge to each third party claim. This application is intended to address the Trustee's acceptance of Heartland's claim at $1.6 million.

[30] As previously indicated by Mr. Menendez, no one appeared for Heartland on this application, despite being served. However, Heartland did file a response to this application, essentially adopting the position of the Trustee.

## HEARTLAND'S CLAIM

[31] In March 2010, Heartland and ACFC executed a franchise agreement by which Heartland was to operate a Wok Box franchise in Mississauga, Ontario. In November 2009, in anticipation of this document being executed, ACFC provided a disclosure statement to Heartland.

[32] The tenant of the restaurant premises was 1185662 Alberta Ltd. ("118"). As I will discuss in more detail below, Heartland executed an indemnity agreement in favour of the landlord, Orlando Corporation ("Orlando"), in respect of 118's obligations under the lease.

[33] Heartland operated the restaurant for about one year, from 2010–2011. The operation was formally abandoned in August 2011. Shortly thereafter, Orlando officially terminated 118's lease in October 2011 and retook the premises.

[34] It is common ground that the procedures leading up to these franchise arrangements, the franchise agreements and the fallout from the franchise's failure, were governed by the *Arthur Wishart Act (Franchise Disclosure), 2000*, S.O. 2000, c. 3 (the "*Wishart Act*"). Although s. 13.6 of Heartland's franchise agreement specified that it was to be governed by and construed in accordance with the laws of British

Columbia, s. 10 of the *Wishart Act* provided that such a choice of law clause was void.

[35] Section 5 of the *Wishart Act* requires a “disclosure document”, such as ACFC purported to give Heartland in this case. Disclosure requirements are governed by ss. 5(4) and (6).

[36] Sections 6 and 7 of the *Wishart Act* are highly relevant to Heartland’s claim:

> **6** (1) A franchisee may rescind the franchise agreement, without penalty or obligation, no later than 60 days after receiving the disclosure document, if the franchisor failed to provide the disclosure document or a statement of material change within the time required by section 5 or if the contents of the disclosure document did not meet the requirements of section 5.
>
> (2) A franchisee may rescind the franchise agreement, without penalty or obligation, no later than two years after entering into the franchise agreement if the franchisor never provided the disclosure document.
>
> (3) Notice of rescission shall be in writing and shall be delivered to the franchisor, personally, by registered mail, by fax or by any other prescribed method, at the franchisor’s address for service or to any other person designated for that purpose in the franchise agreement.
>
> (4) The notice of rescission is effective …
>
> …
>
> (6) The franchisor, or franchisor’s associate, as the case may be, shall, within 60 days of the effective date of the rescission,
>
> > (a) refund to the franchisee any money received from or on behalf of the franchisee, other than money for inventory, supplies or equipment;
> >
> > (b) purchase from the franchisee any inventory that the franchisee had purchased pursuant to the franchise agreement and remaining at the effective date of rescission, at a price equal to the purchase price paid by the franchisee;
> >
> > (c) purchase from the franchisee any supplies and equipment that the franchisee had purchased pursuant to the franchise agreement, at a price equal to the purchase price paid by the franchisee; and
> >
> > (d) compensate the franchisee for any losses that the franchisee incurred in acquiring, setting up and operating the franchise, less the amounts set out in clauses (a) to (c).
>
> **7** (1) If a franchisee suffers a loss because of a misrepresentation contained in the disclosure document or in a statement of a material change or as a result of the franchisor’s failure to comply in any way with section 5, the franchisee has a right of action for damages against,
>
> > (a) the franchisor;

> (b) the franchisor’s agent;
>
> (c) the franchisor’s broker, being a person other than the franchisor, franchisor’s associate, franchisor’s agent or franchisee, who grants, markets or otherwise offers to grant a franchise, or who arranges for the grant of a franchise;
>
> (d) the franchisor’s associate; and
>
> (e) every person who signed the disclosure document or statement of material change.
>
> (2) If a disclosure document or statement of material change contains a misrepresentation, a franchisee who acquired a franchise to which the disclosure document or statement of material change relates shall be deemed to have relied on the misrepresentation.
>
> (3) If a franchisor failed to comply with section 5 with respect to a statement of material change, a franchisee who acquired a franchise to which the material change relates shall be deemed to have relied on the information set out in the disclosure document.
>
> (4) A person is not liable in an action under this section for misrepresentation if the person proves that the franchisee acquired the franchise with knowledge of the misrepresentation or of the material change, as the case may be.
>
> …

[37] In August 2011, Heartland delivered a notice of rescission to ACFC in relation to the franchise agreement.

[38] In March 2012, Heartland commenced an action against ACFC and Messrs. Bender, Eade and Bullock in the Ontario Superior Court of Justice. Heartland asserted that it had not received the required disclosure from ACFC in that the disclosure it had received was “materially deficient.” Heartland therefore claimed the right to rescind the franchise agreement under ss. 6(2) and (3) of the *Wishart Act*. In its amended statement of claim filed in April 2013, Heartland claimed damages, being approximately $1,383,186.77 (under s. 6(6)) and damages for misrepresentation (under s. 7(1)).

[39] On January 7, 2014, after the filing of ACFC’s initial proposal, Heartland filed its first proof of claim in these proceedings in the amount of $2,383,187. The particulars of the two separate claims under the *Wishart Ac*t were set out in Schedule “A”, “Calculation of Claim”, as follows:

a) Part A (s. 6(6)): $1,383,186.77 - these included: (a) out of pocket monies paid to ACFC for the setting up of the franchise; (b); inventory; (c) equipment and supplies; and (d) other "losses" incurred in acquiring, setting up and operating the franchise, which were said to include "operational losses" of $347,500.54 and "lease indemnity costs" of $523,318.04; and

b) Part B (s. 7(1)): damages of $1 million.



[40] On February 27, 2014, Heartland filed a second proof of claim in the amount of $1.6 million. As with its first proof of claim, the same Schedule "A" was attached (indicating total claims of $2.38 million) with no particular clarity about which claims had been deleted or reduced to account for the overall reduction in the amount claimed.

[41] On March 24, 2015, after Adrenaline had reviewed the second proof of claim filed by Heartland, Adrenaline wrote to the Trustee requesting that it expunge Heartland's claim pursuant to s. 135(5) of the *BIA*. At this point, Adrenaline had not received the package of supporting documents provided by Heartland to the Trustee in January 2014, including Heartland's Compensation Brief.

[42] In its letter, Adrenaline's counsel pointed out various apparent discrepancies. These included:

a) the lack of substantiation for the $1 million claim in damages for misrepresentation under the *Wishart Act*, which was said to be a duplication of the s. 6(6)(d) lost profit or operational loss claim;

b) that no credit had been received for the disposition proceeds of the assets which ACFC was required to repurchase from Heartland;

c) the inclusion of "non-cash" items in the s. 6(6) operational loss claim, being depreciation of $35,236.68; and

d) the validity of the claim for lease indemnity costs.

[43] Adrenaline's counsel asserted that there was "no discernable basis to support" the $1.6 million claim. Although Adrenaline referred to "expunging" the claim, it is more than apparent that what was also being sought was a *reduction* of Heartland's claim in relation to the questionable aspects of the claim.



[44] On May 24, 2016, the Trustee's counsel replied to Adrenaline's concerns regarding Heartland's claim. It was only at this point that the Trustee provided Adrenaline with the Compensation Brief previously provided by Heartland back in January 2014. I will deal with the Trustee's analysis and conclusions below in more detail under "Discussion." It will suffice at this time to state that the Trustee was satisfied with the quantification of the claim based on certain "Revised Calculations." The Trustee's counsel advised Adrenaline that it would not be taking any further position on, or expunging, Heartland's second proof of claim.

## STANDARD OF REVIEW

[45] The process by which a trustee examines proofs of claim and either allows or disallows them is set out in s. 135 of the *BIA*:

> 135 (1) The trustee shall examine every proof of claim or proof of security and the grounds therefor and may require further evidence in support of the claim or security.
>
> (1.1) The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.
>
> (2) The trustee may disallow, in whole or in part,
>
> > (a) any claim; …
>
> (3) Where the trustee makes a determination under subsection (1.1) or, pursuant to subsection (2), disallows, in whole or in part, any claim, any right to a priority or any security, the trustee shall forthwith provide, in the prescribed manner, to the person whose claim was subject to a determination under subsection (1.1) or whose claim, right to a priority or security was disallowed under subsection (2), a notice in the prescribed form setting out the reasons for the determination or disallowance.
>
> (4) A determination under subsection (1.1) or a disallowance referred to in subsection (2) is final and conclusive unless, within a thirty day period after the service of the notice referred to in subsection (3) or such further time as the court may on application made within that period allow, the person to

> whom the notice was provided appeals from the trustee's decision to the court in accordance with the General Rules.
>
> (5) The court may expunge or reduce a proof of claim or a proof of security on the application of a creditor or of the debtor if the trustee declines to interfere in the matter.



[46] Section 113 of the *Bankruptcy and Insolvency General Rules*, C.R.C., c. 368, provides that a trustee is required to serve or deliver a notice of disallowance or valuation under s. 135(3) of the *BIA* on the affected person. There is no evidence on this application that the Trustee performed this task although I have no doubt that Heartland understood in some fashion that its claim had been valued and accepted at the "settled" amount.

[47] Adrenaline's application is brought under s. 135(5), which permits the Court to "…expunge or reduce a proof of claim or a proof of security on the application of a creditor ... if the trustee declines to interfere in the matter." The Trustee must have allowed the claim and there must be a request from the creditor to deal with the claim resulting in the trustee declining to "interfere": *Re Light's Travel Service Ltd* (1985), 56 C.B.R. (N.S.) 175 (B.C.S.C.) at 181; *Roberts v. E. Sands & Associates Inc.,* 2013 BCSC 902 at para. 29, rev'd on other grounds 2014 BCCA 122.

[48] The Trustee takes issue with Adrenaline having made any "request" to it to reduce Heartland's claim, as a pre-condition to this application. She submits that there was no issue with the Trustee's conclusion that ACFC was liable to Heartland arising from the disclosure issues under the franchise agreement. In that event, she says that there was simply no basis upon which to "expunge" Heartland's claim, as she interpreted Adrenaline's March 24, 2015 letter as asking her to do.

[49] In my view, this is an overly technical reading of Adrenaline's March 24, 2015 letter requesting that the Trustee address certain issues relating to the Heartland claims. I agree that the word "expunge" was generally used in the letter; however, the letter also refers to various "reductions" of Heartland's liquidated damage claims. Reading the letter in its entirety, Adrenaline was clearly conveying its objections to

certain parts of the claims that would have, if accepted, resulted in reductions or a complete disallowance of certain aspects of the damage claims.

[50] I conclude that Adrenaline has met the necessary requirement to engage s. 135(5). The Trustee allowed Heartland's claim at $1.6 million. Adrenaline then requested that the Trustee disallow certain portions of Heartland's damage claims and the Trustee failed to do so or "interfere."

[51] Adrenaline bears the onus to show, on a balance of probabilities, that Heartland's claims should be reduced: *Purdy (Re)* 1997, 44 B.C.L.R. (3d) 369 at para. 31 (B.C.S.C.); *Roberts* at paras. 31–32.

[52] The Trustee and Adrenaline do not agree on the standard of review to be applied by the Court on this s. 135(5) application and what deference, if any, is to be accorded to the Trustee's decision to allow Heartland's claim.

[53] Firstly, I agree with the Trustee that normally a court should accord a trustee's decision to value a claim with deference. To do otherwise is to ignore a trustee's expertise in what is intended to be an efficient and summary process to resolve such commercial matters. This deference would also normally be afforded to a trustee acting under s. 135(1.1) of the *BIA* in valuing contingent and unliquidated claims.

[54] This approach was confirmed in *Galaxy Sports Inc. (Re)*, 2004 BCCA 284:

> [39] On a consideration of all the "contextual" factors mandated by the "pragmatic and functional" approach, I see no reason to disagree with the long-standing principle enunciated in *Re McCoubrey*, *supra*, which requires the application of a "correctness" standard where compliance with a "mandatory" provision (which I would equate to a question of law or statutory compliance) is involved, <u>and the application of a "reasonableness" standard where the determination of a factual matter or an exercise of true discretion is called for</u>. In the former category, I would place the chair's decision under s. 108 rejecting a proof of claim for voting purposes and the trustee's decision disallowing a proof of claim under ss. 124 and 135(2). <u>In the latter category, I would place the trustee's role in valuing contingent and unliquidated claims under s. 135(1.1).</u> <u>This general approach conforms with the objective, which I see as implicit in the *BIA*, of enabling debtors to have their proposals voted upon expeditiously and permitting creditors to have their rights and claims</u>

> determined in a business-like manner, while at the same time providing a meaningful appeal to a court of law on questions that clearly affect legal rights, engage the relative expertise of judges, and set precedents for other cases.
>
> [Emphasis added.]



[55] Accordingly, assuming that a trustee has properly exercised her discretion in coming to a decision under s. 135(1.1), that decision will ordinarily be approached on a "reasonableness" standard: *Galaxy Sports* at paras. 43–44. For that proposition, the Trustee also refers to *Erdman, Re,* 2006 SKQB 280. In that case, the court similarly confirmed:

> [32] … The trustee, when valuing a contingent or unliquidated claim, must consider all the relevant circumstances and arrive at what the trustee believes is a fair and reasonable valuation: See *Re Wiebe* (1995), 1995 CanLII 7367 (ON SC), 30 C.B.R. 109 (Ont. Gen. Div.). …

[56] Applying administrative law principles to this standard, the question will be whether the process employed by the trustee in coming to a valuation of a contingent or unliquidated claim was justified, transparent and intelligible and whether the decision, based on discretion, falls within possible acceptable outcomes: *Transglobal Communications Group Inc., Re*, 2009 ABQB 195 at para. 73.

[57] However, it will not be sufficient for the Trustee to simply show that she conducted a reasonable process and came to a reasonable decision based on that process. Adrenaline may show that the claim lacked merit or was not properly supported such it should not have been allowed. It is common sense that allowing a claim that lacked merit or had insufficient support could not have been reasonably done by the Trustee using its discretionary powers under the *BIA*: *Marsuba Holdings Ltd, Re*1998*,* 8 C.B.R. (4th) 268 at paras. 14–17 (B.C.S.C.).

[58] Indeed, the Registrar made this same comment in relation to Adrenaline's own appeal as to the value of its claim in *Asian Concepts* where the Trustee had made errors:

> [70] If I am to give deference to the Trustee's decision in that regard, it seems contradictory to then say, that because of the errors in calculation, I should conclude that the valuation would still be reasonable because it is

> greater than the value if one corrects for the admitted errors but assumes that there are no renewals of the MDA.
>
> [71] I accept that deference should be given to the Trustee's decision on the methodology for the valuation, provided it is reasonable. There is, however, nothing in the rationale for deference to the decision of the Trustee that requires me to turn a blind-eye to admitted calculation errors.
>
> [72] In addition, in my view a valuation that is based on incorrect calculations cannot be said to be defensible in respect of the facts, as referred to above from *Transglobal Communications*.



[59] The Trustee and Adrenaline also disagree as to the nature of this application. The Trustee asserts that this is a true appeal and not a *de novo* hearing. As Adrenaline points out, the weight of authority is against the Trustee's position such that the strictures of a true appeal are not applicable.

[60] In *Ted LeRoy Trucking Ltd. (Re)*, 2012 BCCA 511, Justice Lowry, although in *obiter*, specifically considered the proper approach where the application is brought under s. 135(5), such as the case here. He stated:

> [16] This is sufficient to dispose of the appeal but, while nothing appears to turn on it, I do consider s. 135(5) of the *BIA,* which provides that a court may expunge or reduce a proof of claim, effectively provides for applications such as made by the government here to be heard *de novo.* A s. 135(5) application is brought where, as here, a trustee declines to interfere in the matter at issue as opposed to instances where a trustee determines a claim is proven or disallows a claim, which determination or disallowance is, by virtue of s. 134(4), final subject to an appeal. An application under s. 135(5) to expunge or reduce a proof of claim is not an appeal.

[61] In *Roberts* at paras. 33–37, Justice Burnyeat discussed this issue and drew a distinction between appeals from decisions of a trustee under s. 135(4) (such as in *Galaxy Sports*) and those under s. 135(5).

[62] In an application under s. 135(5), a creditor is challenging the decision of the trustee after having had no knowledge of the process and basis upon which the earlier decision was made. In that event, such as here, a creditor is completely in the dark about the process undertaken by the Trustee until disclosure and after the Trustee's decision was made. To restrict the process to only what was before the Trustee would unduly hamper the ability of that challenging creditor to put evidence

before the Court relevant to the claim and its validity. In that event, restricting such a challenge as under a true appeal would be unfair in the extreme.

**<u>THE TRUSTEE'S ASSESSMENT/VALUATION</u>**



[63] The *BIA* anticipates a robust process by which claims will be submitted and then reviewed by the trustee for allowance or disallowance in whole or in part.

[64] Firstly, every creditor must "prove" his or her claim: s. 124(1) of the *BIA*. The creditor bears the onus of establishing its claim. Certainty is not the test; however, the creditor must provide relevant and probative evidence to substantiate the claim: s. 124(4) of the *BIA*; *Mamczasz Electrical Ltd. v. South Beach Homes Ltd.,* 2010 SKQB 182 at paras. 46–47; Lloyd W. Houlden, Geoffrey B. Morawetz & Janis P. Sarra, *The 2017–2018 Annotated Bankruptcy and Insolvency Act* (Toronto: Thomson Reuters, 2017–2018) at G§104, citing *HDYC Holdings Ltd., Re* (1995)*,* 35 C.B.R. (3d) 294 at para. 70 (B.C.S.C.), rev'd on other grounds (1997), 43 B.C.L.R. (3d) 64 (C.A.).

[65] Secondly, the trustee has a duty to examine every proof of claim and the grounds and documentation supporting the proof to determine its validity and, if provable, its value. If a trustee is unsatisfied with the material or evidence provided in support of a claim or the value of a claim, the trustee has both the ability and the right to require further evidence from the creditor. This duty extends to proposals: *In re Toronto Permanent Furniture Showrooms Co.* (1960), 1 C.B.R. (N.S.) 16 (Ont. S.C.) [*Toronto Permanent Furniture*]; *Mamczasz Electrical* at para. 1.

[66] So what did the Trustee do in this case to evaluate Heartland's claim before the voting on March 10, 2014?

[67] The Trustee began communications with Heartland's counsel in November 2013 after Heartland's receipt of the notice of intention to make a proposal. Heartland's counsel advised that they did have a claim of $1,383,186, despite ACFC/Mr. Bender's position in the statement of affairs. On December 31, 2013, the

Trustee advised that Heartland would be required to prove its claim by filing a proof of claim.

[68] On January 7, 2014, Heartland delivered its first proof of claim and voting letter to the Trustee. The Trustee noted that there were no supporting documents. She requested copies.

[69] On January 8, 2014, Heartland's counsel provided Schedule "A" to its proof of claim and a "Compensation Brief" from 2012 that included back-up documentation with respect to the Part A amounts claimed under s. 6(6) of the *Wishart Act*. Later in January 2014, Heartland provided further documentation to the Trustee, as requested, such as the franchise agreement and notice of rescission.

[70] Michelle Madrigga, the Trustee's representative, indicates that she reviewed and investigated Heartland's first proof of claim to determine whether there were documents to support it and whether the heads of damages claimed were appropriate under the *Wishart Act*. After that review, she specifically identified that the unliquidated claims for future profit loss and lease indemnity costs were not supported by documentation.

[71] Based on her later discussions with ACFC's counsel, she understood the ACFC did not dispute liability but that it disagreed with the damages claimed.

[72] It is important to note that no one seriously suggested that ACFC was not liable to Heartland under the *Wishart Act*. ACFC was aware of a previous judgment granted against it by the Alberta Court of Queen's Bench by which the Alberta court determined that ACFC's disclosure was deficient in that case. Accordingly, the issue for the Trustee was, at the beginning, and remains now, a matter of the valuation of Heartland's claim.

[73] Nevertheless, in February 2014, in advance of the vote, Ms. Madrigga understood that negotiations were underway between ACFC and Heartland. On February 26, 2014, she enquired of ACFC's counsel, Mr. Bender and Mr. Eade as to whether the negotiations had been "finalized." On that same date, she was advised by Mr. Eade that information was to be sent to the Trustee that day by which the

Trustee would receive Heartland's revised proof of claim and voting letter, indeed implying that negotiations had been completed.

[74] On February 27, 2014, Heartland's counsel indicated to the Trustee that its claim had been "valued" at $1.6 million. When she received the revised proof of claim in that amount, Ms. Madrigga noted that Schedule "A" was unchanged such that she had no idea which heads of damage had been "amended and agreed to."

[75] This lack of knowledge does not appear to have prompted the Trustee to question any aspect of Heartland's revised claim, particularly as it related to determining the value of that claim for the purpose of the upcoming vote on the Amended Proposal. The evidence indicates that, even after receipt of the revised proof of claim, the Trustee had still not received the documentation to support the profit loss and lease indemnity claims and she made no effort to obtain that documentation.

[76] It was only *after* the voting on March 10, 2014, that, for some inexplicable reason, the Trustee sought further clarification and confirmation of Heartland's claim. On April 4, 2014, Ms. Madrigga requested that ACFC's counsel provide "written confirmation" as to the agreement reached regarding the quantification of Heartland's damage claims.

[77] On April 14, 2014, ACFC's counsel provided his written response. He stated that he was confirming his previous verbal advice as to the settlement. He indicated that ACFC disputed Heartland's claim for damages with respect to the alleged landlord liability (which he estimated at $600,000). However, ACFC's counsel briefly concluded:

> In other respects, ACFC accepted the quantification of the damages established by WB Heartland as recoverable as a statutory claim in [Heartland's Ontario] action.

[78] With ACFC's counsel's April 14, 2014 letter in hand, Ms. Madrigga now states in her affidavit:

> 17. Because of the admission of liability by [ACFC], and with the removal of the disputed lease indemnity costs, the Proposal Trustee was satisfied with

> the quantification of this claim at $1,600,000 and, accordingly, allowed their vote in that amount.
>
> **<u>Conclusion and Summary</u>**
>
> 18. In summary, the valuation of the [Heartland] claim evolved as it was investigated by the Proposal Trustee, with input from Asian Concepts who, as noted, admitted liability, and ultimately settled or compromised for the amount allowed.
>
> 19. In that respect, at no time has any party disputed that Asian Concepts is liable for damages under the *Wishart Act*. The only issue was, therefore, with respect to its valuation, with the specific issues being as to the ability to claim lease costs and quantifying future loss, those being unliquidated claims of a nature that Asian Concepts was best able to provide insight into insofar as to what a reasonable damage valuation would be given their knowledge of the franchise operations and general profitability for them.
>
> …
>
> 22. In summary, based upon the above, when the claim was re-submitted at $1,600,000 (that being approximately 67% of its originally claimed value), with an indication by counsel for [ACFC] that Lease Indemnity Costs of "approximately $600,000" (as noted by [ACFC's] counsel) were largely negotiated away as being in dispute, the Trustee was satisfied that the claim was quantified at an amount that was reasonable having regard to the fact that the disputed items were unliquidated, and that the amount had been fully negotiated and ultimately approved by the debtor, [ACFC], and the costs in any court applications that would have been likely on a disputed claim.

[79] It is unclear whether ACFC's counsel's specific rationale set out in his April 14, 2014 letter factored into the Trustee's decision to accept Heartland's revised claim for voting purposes, since that letter was received *after* the vote. I accept that Ms. Madrigga appears to have received verbal advice from someone before the vote on March 10, 2014, giving some rationale for the $1.6 million valuation by ACFC, although what that advice may have been is unknown.

[80] New evidence as to the rationale for the settlement of Heartland's claim was introduced on this application by ACFC, not Heartland. This evidence comes from Mr. Menendez of Heartland and Mr. Eade of ACFC.

[81] Mr. Menendez now states that in reaching the settled amount, Heartland took into account the "general circumstances," the relative and specific circumstances of the parties and the strength and weaknesses of Heartland's claim, "as [he] understood them." He describes this as a "global assessment." Even Mr. Menendez

recognized that Orlando had not advanced any claim against Heartland under the indemnity agreement and it was unlikely that Heartland would ever be called upon to pay Orlando, given the passage of time. Mr. Menendez says that this assessment was a major factor in justifying a reduction of its claim by approximately $783,000.



[82] Similarly, Mr. Eade’s evidence is that, in February 2014, ACFC and Heartland fully negotiated the claim. ACFC hoped that the claim amount would be reduced since at that time, Heartland was voting against the proposal. He states that various elements of the claim were considered, being the lease indemnity costs (which he considered a weak point), the liquidation costs of equipment, the lost profits claim and litigation costs. Mr. Eade states that ACFC agreed to reduce the claim “on a global basis” to $1.6 million.

[83] Finally, Mr. Eade suggests in his recent evidence that, when the vote was taken, and Heartland voted in favour of the Amended Proposal, there was “no agreement between [ACFC] and Heartland as to how Heartland would vote…”

[84] In my view, Mr. Eade’s suggestion is a completely false portrayal of what happened. The evidence shows that the “settlement” of the claim was directly linked to Heartland voting in favour of the Amended Proposal. On February 26, 2014, Mr. Eade advised the Trustee that Heartland would be filing a revised proof of claim and voting letter prior to the February 27 meeting. Both the second proof of claim and the new voting letter are dated February 27, 2014. Heartland’s counsel forwarded both to the Trustee on that date, and copied ACFC’s counsel. Heartland’s counsel expressly advised both that, if Heartland’s claim was not valued at $1.6 million, Heartland would reconsider its vote and it reserved the right to change its positive vote. By any stretch of the imagination, ACFC had secured the support of Heartland for the Amended Proposal through the negotiations on the claim.

[85] What emerges from this chronology is that the Trustee largely abandoned its role within the proposal process, in relation to the review and assessment of Heartland’s damage claims, in favour of ACFC. In particular:

a) while the Trustee states that she "investigated" this claim, that investigation can only be described as superficial, as including a review of the *Wishart Act* and a document review via the Compensation Brief (which was acknowledged by the Trustee as insufficient in supporting certain claims); and

b) the Trustee refers to ACFC being the one who "…ultimately settled or compromised for the amount allowed." Ms. Madrigga states that ACFC was "best able to provide insight … insofar as to what a reasonable damage valuation would be given their knowledge of the franchise operations and general profitability for them." This is largely confirmed by her later evidence that she relied upon ACFC's advice that it had "…fully negotiated and ultimately approved…" the settled amount.

[86] Ms. Madrigga asserts at para. 20 of her affidavit that the Trustee admitted the claim pursuant to its discretion to compromise and/or settle claims against the estate, pursuant to s. 30(1)(i) of the *BIA*. Nothing could be further from the truth. This claim was compromised by *ACFC*, not the Trustee. Accordingly, I do not consider that this application is an appeal from the Trustee's decision to accept the claim under that provision.

[87] In her affidavit, the Trustee also now asserts that, in addition to considering the Compensation Brief documents, and communications from Heartland and ACFC's counsel as to the settlement, she considered the legal costs to pursue litigation on the issues, including any appeal as to a partial disallowance. However, if is difficult to conceive that the Trustee could have made any such assessment prior to the vote or even after, given that she did not even really know why the claim was settled at $1.6 million beyond very general assertions. She simply had no idea as to the specifics of the issues, beyond the fact that ACFC disputed the Orlando liability claim. Even after receiving ACFC's counsel's letter of April 14, 2014, she had no details as to *why* ACFC disputed Orlando's liability claim.

[88] In these circumstances, the Trustee could have not have had any idea as to what legal process was involved in resolving the issues and any attendant legal costs. There is no indication that, prior to accepting the “settled” claim, the Trustee consulted legal counsel on this matter. For that matter, there is no indication that prior to that time, the Trustee sought any legal advice in her consideration of Heartland’s claims, particularly the profit loss and Orlando’s potential claim under the indemnity agreement.



[89] I have no doubt that, in some circumstances, input from a proposal debtor as to claims advanced against the estate could and should reasonably be considered by a trustee and factored into the valuation of those claims. In most cases, a debtor will have in-depth knowledge of the background of the claims, including circumstances which may support defences to the claim, all of which will be unknown to the Trustee.

[90] However, the duty of the trustee to properly evaluate claims is not abrogated in a proposal process. In *Toronto Permanent Furniture*, the court stated at 21–22:

> It is true that the debtor remains in possession of his property and looks after its administration and his only obligation is to remit to the trustee whatever amount he has arranged to pay his creditors but the scheme of a proposal is and it is so provided by the Form in which proposals are required to be, as well as s. 34(4), that payment in priority to all other claims of all claims directed by the Act to be so paid in the distribution of the property of a bankrupt or a debtor (as the case may be) shall be provided for, so that the trustee in distributing the money received by him from the debtor must have regard to this requirement. <u>The proposal also must provide that payment shall be made on all *provable* claims. In a proposal under The Bankruptcy Act, the debtor making the proposal is, of course, always an insolvent person or a bankrupt and it must be of concern to the creditors that payments to them be made in accordance with the provisions of The Bankruptcy Act with respect to priorities and equal distribution to ordinary creditors who have provable claims</u>. This is so, even if the proposal provides for payment in full of all claims because it cannot be denied that not infrequently a debtor fails to carry out the proposal. <u>Unless, therefore, only those creditors who are entitled to priority and only those creditors who have provable claims are so paid, some of the creditors, at least, will suffer. It would seem therefore necessary that in order to carry out the scheme of the Act with respect to proposals, that the appropriate provisions of s. 94 must be applicable thereto and with great respect I think it is applicable, by virtue of s. 38. This would include the responsibility to see that only provable claims were paid and in accordance with their priorities</u>. This appears to be in accordance with the practice which

> has been followed and is in accordance with comments made in a number of cases.
>
> In the case of *Re McKay* (1922), 2 C.B.R. 462, 52 O.L.R. 466, 3 Can. Abr. 637, the headnote reads in part:
>
> > In composition proceedings taken under s. 13 of the Bankruptcy Act without an assignment or receiving order, the rights and obligations of the debtor and his creditors are to be worked out in substantially the same manner as in cases of assignments and receiving orders.
>
> An appeal was taken from the disallowance by a trustee of certain items in the claim of a creditor. While Orde J. allowed the appeal, the right of a trustee to disallow a claim on a proposal or a composition, as it was then called, was not questioned. In the case of *Re Jacobs* (1922), 3 C.B.R. 419, 23 O.W.N. 118, 3 Can. Abr. 636, the trustee disallowed a proof of a preferred creditor for $300 and the right of the trustee was not only not questioned but the disallowance was upheld. Also in the case of *In re McIntyre* (1922), 2 C.B.R. 396, 3 Can. Abr. 625, McKeown C.J.K.B.D. said at p. 408:
>
> > The approval [by the Court] of this compromise does not involve any pronouncement on the *bona fides* of any claim filed. It is open to the trustee to require the fullest proof to allow or disallow the claim and an appeal can be taken from his decision.
>
> I do not see how it can make any difference whether the trustee has taken possession of the property. It is not a case of administering the property or having management of it, but rather of distributing the moneys of the debtor available to creditors according to the proper priorities and proportions. It may well be that in a proposal the trustee will collaborate more closely with the debtor, but I do not see why he should be less interested in seeing that only provable claims are paid and in accordance with their priorities as provided in the proposal and by the Act. I might add, however, that whereas in *Re Marcotte Inc., supra*, the trustee acted independently of the debtor, there is no evidence that such was so in the case at bar, rather it would appear that the contrary is the fact, namely, that the disallowance was in accordance with the instructions of the debtor.
>
> [Emphasis added.]

[91] In this case, ACFC was out of business, having transferred the vast majority of its assets well before the *BIA* proposal filing. Therefore, it was or should have been questionable just what ACFC was obtaining from this process.

[92] On the face of it, the Amended Proposal appears to be about the "related third parties" funding a pot of money to statutorily "satisfy" the claims of ACFC's creditors, so as to nullify actions by ACFC's creditors against those "related third parties." In doing so, these "related third parties" avoided risk to ACFC's substantial assets that had been transferred to other companies controlled by Mr. Bender, such

as WB Franchising. The Amended Proposal is also, of course, intended to insulate Mr. Bender from claims he was already facing from ACFC's creditors, including Adrenaline. Whether Adrenaline will succeed in opposing the proposal as not being fair and reasonable on this basis remains to be seen: ss. 58-59 of the *BIA*.



[93] When questioned by the Court during submissions, it also became apparent that the ultimate goal may be to "cleanse" ACFC of its creditors' claims so that ACFC's tax losses can be used in some fashion by other entities (for example, WB Franchising, also controlled by Mr. Bender).

[94] I acknowledge that, on the face of things, ACFC and Heartland appeared to be acting at arms length from each other in the negotiations. However, a broader consideration of the entire circumstances raises the prospect that ACFC's and Mr. Bender's motivation toward the Heartland "settlement" was more about securing the cooperation of the single largest creditor against the estate in return for a favourable vote in respect of the Amended Proposal which will benefit him and his companies greatly. That vote in turn was instrumental in winning the vote, particularly since Mr. Bender was voting another of his companies' claim in favour of the Amended Proposal.

[95] Out of fairness, I would also highlight that Heartland's support of the Amended Proposal was likely influenced by the significant reduction of Adrenaline's claim by that point, which would have meant that Heartland would receive the majority of the pooled money funded by the related third parties.

[96] The Trustee's approach (or lack of approach really) is surprising indeed. For a point of contrast, one need only look at the Trustee's rigour applied to its valuation of Adrenaline's unliquidated claim, which was ultimately largely rejected by Registrar Muir in 2017: *Asian Concepts* at paras. 27-32.

[97] All of these circumstances cried out for an *independent* assessment by the Trustee in terms of admitting all or some of Heartland's claims for both voting and distribution purposes. To simply rely on ACFC's assessment without that review

leaves the possibility that ACFC settled Heartland's claims for purposes beyond ensuring that only valid claims are admitted within these proceedings.

[98] It is clear enough that the valuation exercise of Heartland's claim within these proceedings would affect not only ACFC, the debtor (although that is not particularly evident here for the reasons already expressed), but other stakeholders as well. The valuation exercise is intended to be done in a fair and reasonable manner since it affects the claims of all other creditors, not only in terms of the vote, but also distribution. It is the Trustee's role to ensure that all interests are respected within the process, not just those of the debtor or one creditor.

[99] If a trustee simply abdicates or improperly delegates its mandatory statutory duty to review claims and value unliquidated or contingent claims in favour of another entity with perhaps other motivations, the statutory objectives and purposes of the *BIA* proposal process have not been served. I have unfortunately come to the conclusion that this is what happened in this case. Whether the claim was valued at $2.38 million or $1.6 million, the Trustee's mandatory duty was to independently review the claims and if necessary, require support for those claims. This was not done here.

[100] Accordingly, I do not consider that the Trustee has properly exercised her discretion, or exercised it at all, such that any deference is to be afforded to her decision (see similar comment in *Galaxy Sports* at para. 44). The question remains whether certain aspects of Heartland's claim should have been accepted as it was.

**<u>DISCUSSION – HEARTLAND CLAIMS</u>**

[101] The Trustee's counsel's letter to Adrenaline's counsel, dated May 24, 2016, notionally provided a rationale for accepting the $1.6 million "settlement" amount, taking the following position:

a) She "questioned" the quantification of Heartland's revised claim and made enquiries of both Heartland and ACFC since they were "…most knowledgeable as to the strengths and weaknesses of their respective positions and claim valuation." They all agreed that the proper quantification was $1.6 million; and

b) that separate claims advanced under ss. 6(6) and 7 of the *Wishart Act* for lost profits were not duplicative.

[102] The Trustee's letter attached "Revised Calculations" which indicate the following breakdown for the s. 6(6) liquidated claims of $1,289,979.08;

a) s. 6(6)(a) claims: $28,000;

b) s. 6(6)(b) claims: $7,925;

c) s. 6(6)(c) claims: $153,588.37;

d) s. 6(6)(d) claims: $1,100,465.71; these principally included, in addition to other minor adjustments:

i. operational losses accepted at $348,645.42 (slight increase from $347,500). This was supported by Heartland's profit and loss report from January 2010 to January 2012 and general ledger entries for those amounts; and

ii. lease indemnity claim accepted at $480,598.20 based on the Orlando indemnity agreement and a simple calculation of 45 monthly rental payments from September 2011 (after the premises were abandoned) to the end of the five-year indemnity term to May 2015.

[103] In addition, the Trustee indicated that she accepted Heartland's unliquidated damage claim under s. 7 of the *Wishart Act* at $310,020.92, for a total accepted claim of $1.6 million.

[104] On May 24, 2016, the Trustee's counsel stated in her letter to Adrenaline:

> 5. **Overall valuation of the Claim** – Based upon the representations of counsel of [Heartland] and [ACFC], along with the revised Proof of Claim filed

> by [Heartland], the Proposal Trustee is satisfied with this quantification of the claim.
>
> Not only did the Compensation Brief provide supporting documents and a rationale to support liquidated damages under s. 6(6) of the Act in the amount of $1,289,979.08, but a claim for approximately $300,000 for unliquidated damages for future loss of the franchise appeared to be a reasonable amount on its face, particularly given that, as a result of bona fide negotiations involving WB and the Debtor Company, there was an overall reduction of the claim by $783,186.77 that being a 1/3rd reduction in its overall claim (2/3rds reduction in the unliquidated claim).
>
> We also note that, pursuant to ss. 30(1)(i) and 66 of the *Bankruptcy and Insolvency Act,* the Proposal Trustee is entitled to compromise any claim made against the Estate.



[105] Even so, Ms. Madrigga's affidavit sworn on March 22, 2018, filed in opposition to this application, does not refer to her counsel's earlier letter of May 24, 2016, or to the specifics found in that letter, as supporting her acceptance of the "settlement." She simply refers to ACFC's counsel's letter of April 14, 2014, as discussed above, which also does not support the "settlement" with the specific figures found in the May 24, 2016 letter. She does not refer to the "Revised Calculations" which are also referred to in the May 24, 2016 letter. In fact, both ACFC's counsel's April 14, 2014 letter and Ms. Madrigga's affidavit purport to justify the settlement on a completely different basis, namely that there was a "removal of the lease indemnity costs" of approximately $600,000.

[106] In addition, neither Mr. Menendez nor Mr. Eade refer to or justify the "settlement" amount on the basis of any "Revised Calculations"; rather, they now support the settlement only on a "global" basis. Both Mr. Menendez and Mr. Eade also refer to the particular dispute over the lease indemnity costs as justifying the reduction in the claimed amount.

[107] These conflicting and shifting rationales for the ACFC/Heartland settlement raise issues and concerns in and of themselves and do not reflect well upon the Trustee.

[108] I find as a fact that the specific Revised Calculations referred to in the Trustee's letter of May 24, 2016 are the basis upon which ACFC and Heartland

settled Heartland's claim and also, the basis upon which the Trustee accepted those calculations. If one looks at the liquidated damage claim of $1,289,979 (the s. 6(6) claims) in the Revised Calculations, one needs only to add the further very specific number of $310,020 (for the s. 7 damages) to come to the nice round global settlement figure of $1.6 million. I conclude and find as a fact that this was the basis upon which the Trustee valued and accepted Heartland's claims.



[109] Adrenaline's current objections to Heartland's claim are limited to only the lease indemnity costs under s. 6(6)(d) and the lost profit claims under s. 7, as claimable by Heartland against ACFC under the *Wishart Act*. It remains to be determined whether those aspects of Heartland's claims should have been accepted by the Trustee.

**1) Lease Indemnity Costs**

[110] I have already generally referred to Heartland's agreement with ACFC under its franchise agreement. 118 was the tenant at the location where Heartland's franchise business was conducted. Orlando was the landlord.

[111] On April 3, 2010, 118, as tenant, and Orlando, as landlord, entered into a 10-year lease of certain premises in Mississauga, Ontario. In addition, on June 1, 2010, Heartland entered into an indemnity agreement with Orlando, by which Heartland agreed to indemnify Orlando with respect to amounts owing by the tenant (118) under that lease during the first five years of the term. The indemnity agreement provided that it was to be governed and construed in accordance with the law of Ontario.

[112] 118 abandoned the leased premises in August 2011. At that time, rent was in arrears in the amount of $48,204.82. Orlando issued a notice of termination of the lease on October 25, 2011. Thereafter, the leased premises remained vacant until March 1, 2013, when Orlando's new tenant began operations there. This new tenant remained in occupation of the premises until at least June 2017 and possibly beyond.

[113] It is undisputed on this application that Heartland had a claim against ACFC under the *Wishart Act* for any losses arising from the rescission of the franchise agreement, including recovery for claims advanced against Heartland under Orlando's indemnity agreement.

[114] Adrenaline objects to this aspect of Heartland's s. 6(6)(d) claim being accepted in the amount of $480,598. The basis for Adrenaline's objection is that any claim by Orlando under the indemnity agreement signed by ACFC is statute-barred.

[115] To be a provable claim, a claim must be recoverable by legal process. Therefore, a claim may not be advanced if it is statute-barred at the date of bankruptcy or, in the case of a proposal, the date of the initial bankruptcy event. The initial bankruptcy event here was on November 20, 2013, when ACFC filed the notice of intention to make a proposal: *Farm Credit Corporation v. Dunwoody Limited*, 1988 ABCA 216 at para. 7.

[116] Section 4 of the Ontario *Limitations Act*, *2002*, S.O. 2002, c. 24, Sched. B, states that the basic limitation period for Orlando to have advanced a claim against Heartland was two years after the "claim was discovered." Section 5 of that *Act* provides that a claim is discovered on the earlier of:

> **5** (1) A claim is discovered on the earlier of,
>
> (a) the day on which the person with the claim first knew,
>
> (i) that the injury, loss or damage had occurred,
>
> (ii) that the injury, loss or damage was caused by or contributed to by an act or omission,
>
> (iii) that the act or omission was that of the person against whom the claim is made, and
>
> (iv) that, having regard to the nature of the injury, loss or damage, a proceeding would be an appropriate means to seek to remedy it; and
>
> (b) the day on which a reasonable person with the abilities and in the circumstances of the person with the claim first ought to have known of the matters referred to in clause (a).
>
> (2) A person with a claim shall be presumed to have known of the matters referred to in clause (1) (a) on the day the act or omission on which the claim is based took place, unless the contrary is proved.

[117] As previously stated, 118 abandoned the premises in August 2011 and Orlando issued a notice of termination in respect of the lease in October 2011. As such, Orlando would have known of 118's default no later than October 2011 and therefore, would have known then of its right to file legal action against both 118 and Heartland for both past and prospective losses. The premises were leased again in March 2013.



[118] However, Joy Okpara, who is employed in Orlando's legal department, states in her affidavit sworn June 9, 2017:

> 8. Orlando has not commenced any recovery proceedings against the Tenant for damages arising from its breach of the Lease and abandonment of the Leased Premises, nor has it commenced any recovery proceedings against [Heartland] pursuant to the Indemnity Agreement or received any payments thereunder, as at [June 9, 2017].

[119] In the above circumstances, I agree that, since Orlando did not commence any action against Heartland, any claim became statute-barred no later than October 2013, being two years after 118's default and the notice of termination was sent.

[120] In its response to Adrenaline's request that this portion of Heartland's claim be expunged, the Trustee advised that the amounts claimed "relate to [Heartland's] obligation to" the Landlord. Heartland's two proofs of claim included "lease indemnity costs" of $523,318.04. Even so, the Compensation Brief simply referred to 118's monthly estimated lease amount of $10,679.96, which was multiplied by 45 months (September 2011 to the end of term in May 2015), being presumably the remainder of the indemnity period left on the lease. This resulted in a total claim for lease indemnity costs of $480,598.20. Heartland offered no other support for this claim.

[121] However, it is clear that Heartland suffered no loss by reason of 118's default under Orlando's lease. It never paid Orlando under its indemnity obligations and never will by reason of the expiry of the limitation period. This means that Heartland in turn had no valid claim that it could have advanced against ACFC under the *Wishart Act*.

[122] I agree with Adrenaline that the Trustee was in error in admitting this aspect of Heartland's claim in the amount of $480,598 or at all. As a matter of law, it was not a valid claim that could be advanced against ACFC. That aspect of the claim should be entirely expunged.



#### 2) Lost Profits

[123] Heartland's claim, as advanced in its Ontario action and in its proofs of claim, relied solely on its rights under the *Wishart Act*. Heartland made no claim for damages at common law generally.

[124] In relation to the lost profits claim, Heartland's amended statement of claim set out:

a) Para. 1(a): it claimed a declaration that it had validly rescinded the franchise agreement pursuant to the *Wishart Act*;

b) Para. 1(c): it claimed damages of $1 million pursuant to s. 7 of the *Wishart Act* (in addition to the s. 6(6) damages claimed);

c) Para. 17: that ACFC's omissions in its disclosure statement constituted a "misrepresentation" within the meaning of s. 7 of the *Wishart Act*;

d) Para. 18: that as a result, Heartland has "suffered losses including but not limited to the amounts expended on or in connection with the franchise fee, construction costs, and the operational losses incurred by [Heartland] during [its] operation of the Franchise."

[125] Again, there is no dispute that ACFC was liable to Heartland for inadequate disclosure under the *Wishart Act*. ACFC conceded that its disclosure statement given to Heartland was in the same form of disclosure documents given to another franchisee in Alberta which had been found to be incomplete and not in compliance with the *Wishart Act*: *1448244 Alberta Inc. v. Asian Concepts Franchising Corporation,* 2013 ABQB 221.

[126] Turning to the matter of damages, Heartland's principal, Mr. Menendez, describes the s. 7 claim as unliquidated damages and including:

> 11. … future loss of profit and opportunity under the franchise agreement. Such damages were caused by certain misrepresentations made to [Heartland], that were contained in an alleged "franchise disclosure document," that [ACFC] provided to [Heartland] in order to entice [Heartland] to purchase a franchise from [ACFC].

[127] As the Trustee notes, it is not clear whether the s. 7 claim was duplicative of what had already been claimed under s. 6(6)(d). Both of Heartland's proofs of claim simply refer, in Schedule "A", to a damage claim under s. 7 in the amount of $1 million.

[128] Possible duplication was particularly evident from the operational loss claim. The Compensation Brief attached various documents in support of an "operational loss" claim under s. 6(6)(d). This amount was originally claimed in the amount of $347,500 but was later increased to $348,645.42 in the Revised Calculations. As previously noted, this figure was taken from Heartland's profit and loss detail report from January 2010 to January 2012, supported by general ledger entries. Heartland's principal, Mr. Menendez, describes this as a liquidated claim and including "…losses that [Heartland] had incurred in acquiring, setting up and operating its franchised business."

[129] As noted above, in the Trustee's May 24, 2016 response to Adrenaline's request that it review Heartland's claim, the Trustee took the view that s. 7(1) of the *Wishart Act* permits a claim for lost future profit, the value of which was accepted by the Trustee at $310,020.92. In part, the Trustee's counsel stated in her letter:

> Ultimately, it was agreed by all parties that a proper quantification of the claim was $1,600,000, that being $1,289,979.08 under s. 6(6) , <u>and the remaining amount of $310,020.92 under s. 7(1) for future loss of profit and opportunity under the franchise agreement, had it not been rescinded</u>.
>
> ….
>
> Not only did the Compensation Brief provide supporting documents and a rationale to support liquidated damages under s. 6(6) of the Act in the amount of $1,289,979.08, but a <u>claim for approximately $300,000 for unliquidated damages for future loss of the franchise appeared to be a reasonable amount</u>

> on its face, particularly given that, as a result of bona fide negotiations involving WB and the Debtor Company, there was an overall reduction of the claim by $783,186.77 that being a 1/3rd reduction in its overall claim (2/3rds reduction in the unliquidated claim).
>
> [Emphasis added.]



[130] Adrenaline initially argued that, since the franchise agreement was rescinded under s. 6 of the *Wishart Act*, Heartland could not have claimed for future losses under s. 7 as a matter of law. Adrenaline drew a distinction between s. 6(6) damages which seek to put the injured party in a position they would have been in had the misrepresentation had not been made, and to future claims under the agreement.

[131] The Trustee (and impliedly Heartland) argued that the respective remedies of a franchisee under s. 6(6) and 7 of the *Wishart Act* are cumulative and not duplicative. She argues that while s. 6(6) provides for damage claims that are normally seen in rescission cases, s. 7 provides a mechanism to recover statutory damages that are not based on common law principles. This would include the principle that, upon a party electing to rescind a contract, the contract is no longer afoot and it is no longer open to that party to claim the benefit of the rescinded contract in respect of benefits arising under the contract, such as lost future profits: John McCamus, *The Law of Contracts* (Toronto: Irwin Law, 2005) at 337–38; Dominic O'Sullivan, Steven Elliott & Rafal Zakrzewski, *The Law of Rescission* (Oxford, UK: Oxford University Press, 2008 at 297–98).

[132] It is apparent based on the research presented on this application that there are very few Ontario cases interpreting ss. 6(6) and 7 of the *Wishart Act*.

[133] In *1490664 Ontario Limited v. Dig This Garden Retailers Ltd.* 2005, 256 D.L.R. (4th) 451 (Ont. C.A.), the trial court concluded that inadequate disclosure was made in the disclosure statement (para. 19). At para. 28, the court described the remedy under s. 6 as "statutory rescission" which is different than equitable rescission. Further, the court drew a clear distinction in remedies as between s. 6(6) and s. 7:

> [38] As I indicated earlier, the principles of equitable rescission do not apply in a case of statutory rescission. Further, the Act specifically provides for certain payments to be made to the franchisee within sixty days of the effective date of rescission as set out in s. 6(6). In addition, s. 7 clearly provides that if a franchisee suffers a loss as a result of a franchisor's failure to comply *in any way* with s. 5, the franchisee has a right of action for damages. Failure to comply in any way with s. 5 includes a failure to provide the disclosure document that the section requires. In circumstances where a franchisor fails to make the payments required of it under s. 6(6), those damages could include such amounts. As well, if a franchisee suffered any other loss as a result of the franchisor's failure to comply with s. 5, the franchisee may sue for such damages under s. 7.
>
> [Emphasis added.]

[134] In *Salah v. Timothy's Coffees of the World Inc.*, 2010 ONCA 673, the court upheld the trial court's decision (*Salah v. Timothy's Coffees of the World Inc.* 2009, 65 B.L.R. (4th) 235 (Ont. S.C.J.)) to award damages for both breach of contract and breach of the duty of good faith and mental distress. Those damages included past and future losses in respect of the franchise agreement under the *Wishart Act* (paras. 23–24). At trial, the income loss was for a period of 10 years, being the usual and actual term of that franchise: para. 129. Unlike this case, Mr. Salah had not rescinded the franchise agreement.

[135] In *Salah* (Ont. C.A.), at paras. 26–27, the court rejected the contention that an interpretation of the *Wishart Act* restricted damages to compensatory damages only, commenting that the *Wishart Act* is remedial legislation deserving of a broad and generous interpretation. It is important to note, however, that the evidence in *Salah* filed in support of the future damage claim very much supported that claim.

[136] In *1706228 Ontario Ltd. v. Grill It Up Holdings Inc.*, 2011 ONSC 2735, the court awarded only restitutionary damages (not future loss of profits), although that appears to have been based on what was sought at trial: para. 40. The court stated:

> [58] … Upon rescission, the plaintiffs were entitled to be put in the position that they would have been in had they not entered into the agreements. Thus they are entitled to return of the deposits they paid to the defendants and their out-of-pocket expenses associated with the transaction, including their equipment purchases related to the business.... I do not award anything for lost profit: the plaintiffs are seeking a restitutionary remedy, based on rescission, rather than their loss of the profits they expected to earn had the

> transaction closed. In the end, then, the damages for failing to close equal the damages for breach of the *Arthur Wishart Act.*
>
> [Emphasis added.]

[137] *Dig This Garden* and *Salah* were followed in *Burnett Management Inc. v. Cuts Fitness for Men*, 2012 ONSC 3358. There, the franchisees had elected to rescind the agreement. At para. 49, the court agreed that s. 7 damages were available *in addition* to s. 6(6) damages. However, only liquidated damages were awarded.

[138] The final case is *8150184 Canada Corporation v. Rotissieries*, 2014 ONSC 815; aff'd *8150184 Canada Corporation v. Rotisseries Mom's Express (Les Rotisseries Mom's Express Limitée)*, 2016 ONCA 115. The plaintiff franchisees had moved for judgment based on allegations of a breach of s. 3 of the *Wishart Act*, being a duty of fair dealing in relation to a franchise agreement. The s. 6(6) damages claimed were accepted by the court based on a failure to respond to a notice to admit. However, the franchisee also claimed s. 7 damages for misrepresentation and for loss of profit from the time the franchise was intended to be operational from June to October 2012: para. 13. The court directed that this issue proceed to trial.

[139] The later trial with respect to damages was addressed in *8150184 Canada Corporation v. Rotissieries Mom's Express Ltd.*, 2014 ONSC 3256. The court stated:

> [21] Loss of profits is recoverable if an evidentiary basis has been provided sufficient for the court to make an informed determination of the potential loss. (See *Mincom Corona Realty Inc. v. Mincom Realty Systems Inc.*, [2004] O.J. No. 4729 (Ont. C.A.) at paras. 5-6).

In that case, the court accepted as reasonable proof certain *pro forma* calculations as the loss of potential profits but only to October 2012, being the date of rescission by the franchisee (paras. 22, 31(4), Appendix "A").

[140] Accordingly, I agree with the Trustee that s. 7 damages are statutory damages intended to compensate a franchisee for "other loss" or damages that would not be recoverable under s. 6(6). Nevertheless, the Ontario case law is far from clear as to what is included in "other loss" under s. 7—and as to whether this refers to quantifiable further losses arising from the rescission not specifically

identified in s. 6(6), or whether some other head of damages, such as a contingent claim for loss of future profits, may be claimed, and if so, for what period of time.

[141] Even so, accepting *arguendo* for the purposes of this application that claims for loss of future profit may be recoverable under s. 7, it remains the case that a creditor must prove such damages. As stated in *Mincom Corona Realty Inc. v. Mincom Realty Systems Inc.*, [2004] O.J. No. 4729 at para. 6 (Ont. C.A.), the franchisee must provide a "…basis upon which an informed determination of … potential lost profits could be made." Without any such evidence, no claim will have been proven.

[142] As noted above, Heartland itself made no claim for "lost profit", either in its Ontario Action pleadings filed against ACFC or in its two proofs of claim. In accordance with the Trustee's acceptance of the s. 6(6)(d) claim, operational losses (not loss of profits) to January 2012 were taken as proven.

[143] Even accepting that this claim was put forward to ACFC and the Trustee (although that is far from clear), Heartland has *never* provided any evidentiary basis for its $1 million claim for s. 7 "lost profit" damages. ACFC, Heartland and the Trustee do not suggest otherwise.

[144] There was no substantiation for this claim in Heartland's Compensation Brief. As far as I'm aware, there was no substantiation given by Heartland to ACFC as part of the negotiations leading to the "settlement." Most importantly, there is no evidence that the Trustee either requested and/or received any such substantiation in support of this claim. This would have been in relation to the Trustee's consideration as to the proper valuation of this contingent claim. Certainly, even accepting the Trustee's submission that this claim was settled by it pursuant to s. 30 of the *BIA* (which I do not accept), I am not aware that the Trustee even evaluated this aspect of the claim in terms of agreeing to the "settlement" amount negotiated by ACFC.

[145] The Trustee's explanations for her acceptance of this claim are surprising even in the face of a complete absence of any evidentiary basis for this claim. In the

Trustee's counsel's letter of May 24, 2016, she states that the claim for approximately $300,000 for unliquidated damages for future loss of the franchise appeared to be a "reasonable amount on its face." The rationale appears to be that the "reasonableness" arose because of ACFC and Heartland's negotiations that resulted in a significant reduction of the overall claim. This statement was repeated in Ms. Madrigga's affidavit, which only generally referred to the overall claim amount as being "reasonable."

[146] One wonders how indeed the Trustee could have asserted the reasonableness of even the overall settlement without a consideration and understanding of the $1 million loss of profits claim and without having received any materials in support of such a claim. I will repeat that the Trustee seems to have simply relied on the negotiations between ACFC and Heartland in that respect, although what evidence, if any, was provided by Heartland to ACFC in that regard is not known.

[147] In conclusion, the Trustee was not in a position to have accepted Heartland's claim for loss profits, whether at $1 million or even the accepted amount of $310,020.92, without a proper evidentiary basis for doing so. Having done so, the Trustee improperly admitted Heartland's proof of claim as including this type of claim.

## DISSOLUTION OF HEARTLAND

[148] On December 21, 2013, Heartland was dissolved as a corporate entity pursuant to the issuance of a certificate of dissolution under s. 212 of the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 ("*CBCA*"). Section 212(4) of the *CBCA* provides that the "corporation ceases to exist on the date shown in the certificate of dissolution."

[149] As such, Heartland ceased to exist as a corporate entity just one day after ACFC filed its proposal, but before ACFC filed its Amended Proposal on February 14, 2014, and before Heartland filed both proofs of claim and the voting took place on March 10, 2014.

[150] As a result of the dissolution, it is undisputed that Heartland was then not a "person" who could have a provable claim under the *BIA* when it purported to deliver its proofs of claim to the Trustee on January 7, 2014 and February 27, 2014, respectively: ss. 2 "creditor" and "person", 124 of the *BIA*.

[151] At the time of the vote on March 10, 2014, Heartland was not a "person" who had proved its claim and therefore, it was not entitled to vote its claim at that time: s. 109(1) of the *BIA*. In addition, by operation of s. 228(1) of the *CBCA*, any property interest of Heartland would have vested in the Crown upon dissolution.

[152] On March 14, 2018, Adrenaline's counsel wrote to the Trustee, ACFC and Heartland to alert them as to this issue.

[153] On March 23, 2018, in advance of this hearing, Mr. Menendez filed an affidavit indicating that, just days before, he had been alerted to the dissolution. He indicates that this resulted for inadvertence, rather than a deliberate decision on the part of Heartland. He indicated that he had instructed Heartland's counsel to take steps to revive Heartland under the *CBCA*. As of that date of the hearing, Heartland's status was still unclear.

[154] After the hearing, the Trustee provided evidence that, in fact, Heartland was revived on March 22, 2018, just days before the hearing.

[155] In light of the revival, Heartland is now able to proceed as if it had never been dissolved, by reason of s. 209(4) and (5) of the *CBCA*:

> **(4)** Subject to any reasonable terms that may be imposed by the Director, to the rights acquired by any person after its dissolution and to any changes to the internal affairs of the corporation or other body corporate after its dissolution, the revived corporation is, in the same manner and to the same extent as if it had not been dissolved,
>
> > **(a)** restored to its previous position in law, including the restoration of any rights and privileges whether arising before its dissolution or after its dissolution and before its revival; and
> >
> > **(b)** liable for the obligations that it would have had if it had not been dissolved whether they arise before its dissolution or after its dissolution and before its revival.

> **(5)** Any legal action respecting the affairs of a revived corporation taken between the time of its dissolution and its revival is valid and effective.

[156] The combined effect of these provisions is to restore Heartland's assets and "erase" the dissolution and vesting of that property in the Crown: *Saini v. Grand Forks (City)*, 2011 BCSC 320 at para. 23.

[157] As a result of the foregoing, I am satisfied that Heartland's revival has reinstated its status as a "person" for the purpose of participating as a creditor in these proposal proceedings and defending its claim for the purposes of voting and distribution.

## CONCLUSION

[158] I conclude that certain aspects of Heartland's claims were not properly accepted by the Trustee for both voting and distribution purposes.

[159] Adrenaline submits that these admitted amounts should be deducted from the admitted second proof of claim of $1.6 million. I agree. The Trustee's rationale for the accepted claim is set out in its May 24, 2016 and the Revised Calculations indicate that minor adjustments were made to other claims made under s. 6(6)(c) and (d). Accordingly, the only deductions from the admitted amount relate to the lease indemnity claim and the s. 7 damage claim.

[160] Heartland failed to prove any losses under s. 7 of the *Wishart Act* in the amount of $1 million, or even that accepted by the Trustee ($310,020). No claims were properly admitted in that category. My other conclusion results in a reduction of the amounts under the s. 6(6) *Wishart Act* claims totalling $1,289,979, which was accepted by the Trustee, in relation to the lease indemnity claim set out in the Revised Calculations ($480,598).

[161] Accordingly, the total of Heartland's provable claim in this proceeding is $809,382 ($1.6 million less $310,020 and less $480,598).

"Fitzpatrick J."

Court File No.: NB 8881
Estate No.: 092558



IN THE COURT OF QUEEN'S BENCH OF NEW BRUNSWICK

IN BANKRUPTCY & INSOLVENCY

**IN THE MATTER OF** the *Bankruptcy and Insolvency Act*;

**AND IN THE MATTER OF** the Bankruptcy of Thomas Blair Drummie;

BETWEEN **ROYAL BANK OF CANADA** (aka Royal Bank Financial Group)

APPLICANT

AND: **GRANT THORNTON LIMITED** in its capacity as Trustee in Bankruptcy of the Estate of Thomas Blair Drummie

RESPONDENT

AND: **THE SOCIETY OF LLOYDS**

INTERVENOR

**DECISION ON MOTION**

| | |
|---|---|
| Before: | Michael J. Bray, Q.C. Registrar |
| Heard: | October 6, 2003 |
| Decision: | January 23, 2004 |
| Appearances: | Walter D. Vail, Q. C. – Solicitor for the Applicant, Royal Bank of Canada<br>R. Gary Faloon, Q. C. – Solicitor for the Respondent, Grant Thornton Limited<br>Bruce S. Russell – Solicitor for the Respondent, The Society of Lloyds |

## I FACTS

1. Thomas Blair Drummie, Q. C. (hereinafter "the Bankrupt") made an Assignment in bankruptcy on March 29, 2000 in which he listed the applicant as a creditor.
2. The Bankrupt had executed an Agreement on March 23, 1994 by which he hypothecated to the applicant 2,501 shares in Ground Floor Holdings Ltd.
3. In May of 2001 the applicant filed a proof of claim with the respondent claiming a debt of $310,801.90 and listing the hypothecation agreement as security.
4. On July 25, 2001, Vincent L. Duff, acting for the Respondent stated in writing, "…we wish to advise that the documentation in support of your recent claim to security has been reviewed and appears to be in order".
5. By Form 77 dated January 31, 2002, and pursuant to subsection 135(2) of the *Bankruptcy & Insolvency Act* (hereinafter "the Act") the Respondent disallowed the security claim of the applicant because "the security given related to a specific loan in the amount of $150,000.00 and that loan was repaid in full prior to the date of bankruptcy."
6. By Notice of Motion returnable before the Registrar on the 13th day of May 2002, the applicant sought an Order holding that the disallowance by the Trustee of the security that the applicant had alleged on its claim of $310,801.90 was a nullity. The Notice of Motion indicated that reliance would be made upon sections 135, 187 and 192 of the Act.
7. Three oral decisions resulted from the hearing on May 13, 2002. The first allowed the Society of Lloyds to intervene with the status of friend of the court.

In the second decision, the Registrar declined the jurisdiction to hear the appeal because the statutory requirements of subsection 135(4) of the Act had not been observed. The third decision found that the failure to cite section 37 of the Act in the motion was a formal error and permitted an amendment pursuant to sub-section 187(a) to allow counsel to argue the issue of whether a disallowance subsequent to the Trustee's initial determination of security would be null and void.

8. The Registrar's decision concerning jurisdiction based on his finding that the statutory limitations to the appeal period in subsection 135(4) may not be waived by consent, unless a court order is obtained, was taken on appeal first to the Chief Justice of the Court of Queen's Bench and subsequently to the Court of Appeal of New Brunswick (see 2002 NBQB 151 and 2002 NBCA 95 respectively).

9. These appeals having received disposition, this matter is now being resumed to hear the applicant's request that it be permitted to use section 37 of the Act to challenge the Trustee's disallowance and that this decision of disallowance be found to be a nullity.

## II ISSUES

10. Two issues are raised in this motion:

(1) whether a section 37 application is an appropriate vehicle to review a Trustee's disallowance of a security claim under the circumstances, and

(2) whether, having admitted a proof of security under section 135, a Trustee has the authority to subsequently reverse that decision.

**III DECISION**

11. The applicant submits that, although the Act is silent concerning whether or not the determination of a proof of security is final, the court should find it to be final by analogy, using a comparison with subsections 135(1.1) and 135(4) of the Act.

> 135 (1.1) Determination of provable claims - The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.
>
> 135 (4) Determination or disallowance final and conclusive - A determination under subsection (1.1) or a disallowance referred to in subsection (2) is final and conclusive unless, within a thirty day period after the service of the notice referred to in subsection (3) or such further time as the court may on application made within that period allow, the person to whom the notice was provided appeals from the trustee's decision to the court in accordance with the General Rules.

12. It is further submitted by the applicant that, if it is accepted that the Trustee's decision is final, he should be found to be *functus officio* and it should be declared that his only remedy for changing the decision of the Act would be an application to the court to expunge pursuant to subsection 135(5) of the Act.

13. The applicant postulates that, if one accepts that the Trustee is *functus* after allowing the proof of security, the subsequent alleged disallowance would be a nullity and, therefore, the applicant would not be restricted to the provisions of Section 135 in seeking a remedy.

14. Both the respondent and the intervenor argue that the specificity of Section 135 in matters of disallowance of proofs of claim and proofs of security precludes recourse to the more general provisions of Section 37 and that to override the

limitation period in Section 135 by a Section 37 application would be using the latter section to obtain a remedy that is contrary to the Act.

15. Unless the text reveals an inherent contradiction or inconsistency that cannot be avoided without employing a strained and unrealistic construction, a statute should be interpreted in a manner that respects its integrity. In a statute as comprehensive as the *Bankruptcy and Insolvency Act*, a specific provision concerning the procedure to be followed in a particular aspect of the administration of the estate, such as appeals disallowances, must prevail over a general remedy for review of Trustee's decisions. Section 37 cannot be used in place of Section 135 to appeal a disallowance by the Trustee.

16. Although the court has a discretion in granting remedies by way of an application pursuant to a Section 37 application to avoid injustice to any party to the administration of the estate, normally its first inquiry will be whether the Trustee has acted in accordance with his or her obligations under the Act. There is no evidence before the court that the Trustee in this instance conducted himself improperly. Having initially decided that the security claim had appeared to be in order, he later disallowed it based on further information. The Act refers only to the Trustee's disallowance as being final and conclusive. It does so in terms so clear and with such distinct procedures for giving notice of the disallowance and for appeal thereof, that one must imply an exclusion for other decisions by the Trustee.

17. Consideration must be given, nevertheless, to the applicant's submission that, notwithstanding the silence of the Act about any impediment to a change of

decision by the Trustee, the Trustee would be *functus* and that the disallowance should be considered a nullity and, therefore, not a disallowance at all.

18. The term "functus offico" refers to the practice of not allowing a court, or administrative tribunal to amend or reopen formal judgments unless this be permitted by statute or be simply to remedy an error, the correction of which is allowable under "slip rule" provisions. This maintains the integrity of appeal procedures for courts and forms the principle of finality in proceedings before administrative tribunals.

19. It would require a strained interpretation to hold that a trustee in the administration of a bankruptcy estate is acting in the capacity of an administrative tribunal. Neither in the process of determining whether a claim is provable nor in the disallowance of a claim, a priority right or a security, does the Act mandate a hearing procedure. A wide discretion is granted to the Trustee subject to the court's supervision or the right of a creditor to appeal a disallowance pursuant to subsection 135(4) or that of a debtor or creditor to apply to have a proof of claim or proof of security expunged pursuant to subsection 135(5). The nature of the above noted appeal and application is that of a formal reexamination of the facts on the merits which indicates that it is not incumbent upon the court to show deference to the findings of the Trustee and further distinguishes his decision-making role from that of an administrative tribunal.

20. The Act does not make the determination of a provable claim by the Trustee final and conclusive as it does for a disallowance. Had the legislators wished to limit the competence of the Trustee to review a decision under subsection (1.1) of

section 135 of the Act, when further evidence is received, they surely would have done so in terms as clearly as those enacted in subsection (4).

21. I am likewise unpersuaded that the court should expand the provisions of subsection 135(5) to insert a requirement that an application to expunge be required of the Trustee when the language of the text states clearly that it refers to the "application of a creditor or of the debtor, if the trustee declines to interfere in the matter" (emphasis added). The implication is clearly that the Trustee is free to act administratively without court authorization, the court's intervention being triggered only by an application from specified parties.

22. The moving party urges the application of the decision in Ostrander & Co. v. Can. Credit Men's Trust Assn. [1930] 2 D.L.R. 88 (Sask C.A.) to the present instance to support a finding that the Trustee should have made an application to the court to expunge. In Ostrander the Trustee delayed the decision on disallowance for five years from the filing of the claim. The court held that when a trustee delays for such an unreasonable period of time he may be deemed to have admitted the claim, especially if the creditor were prejudiced by the retarded process. The claimant in Ostrander had ceased business and was no longer well placed to defend its claim. The court, however, left it open to the Trustee to make an application to expunge the proof. Although admitting that express rules allowing this process no long appeared in bankruptcy legislation, the court suggested that the term "interfere" as it appeared in s. 127(5) [presently 135(5)] of the Act was wide enough to cover an application to expunge.

> 135(5) Expunge or reduce a proof – The court may expunge or reduce a proof of claim or a proof of security on the application of a creditor or of the debtor, if the trustee declines to interfere in the matter.

23. There are distinguishing factors between the facts of Ostrander and those of the present instance. The lapse of time between the filing of the applicant's proof of claim and the Trustee's disallowance was six months as opposed to five years in Ostrander. Assuming the court to be correct in the latter case in interpreting "interfere" widely enough to permit the Trustee to prevail himself of s. 135(5) in case of necessity, I read the decision as suggesting that the use of this provision is facultative to and not mandatory upon any Trustee who wishes to modify his decision to allow a proof. The circumstances in the cited case were exceptional. There was nothing in the present instance to prevent the filing of an appeal pursuant to s. 135(4) if the applicant believed the Trustee to be in error.

**CONCLUSION**

24. The *Bankruptcy and Insolvency Act* is a comprehensive code developed over an extended period of time and its provisions should be observed unless the court is faced with a situation for which no remedy has been provided or factual circumstances so unique that recourse must be sought from the court's inherent jurisdiction to avoid substantial injustice.

25. The Trustee in the present instance modified his initial decision concerning the applicant's claim based on new information. Nothing in the Act precludes his doing this. The applicant had a remedy pursuant to s. 135(4) if it believed the Trustee's decision to be in error.

26. Having not availed itself of the remedy in accordance with the statutory conditions imposed, the applicant cannot now have recourse to the more general appeal provisions of s. 37 in order to dispense with the said prerequisite conditions.

27. The motion stands dismissed.

28. The question of costs deserves mention, particularly as it relates to the intervenor.

29. Normally there are two types of intervention. There is that in which a corporation or individual applies to intervene as a party in a lawsuit which may affect their economic well-being and in which their interests may not be otherwise protected. A second form of intervention is that of amicus curiae wherein a disinterested party either applies or is requested upon the court's initiative to assist it in considering a point of law that has been overlooked or to avoid a procedural error.

30. It is neither desirable nor appropriate that a creditor have an unfettered right to intervene as a party in a bankruptcy matter unless it has an individual interest which would be in particular jeopardy and the issue involved otherwise might not be raised before the court. This would lead to an unwieldy procedure wherein any creditor could allege that a court review of proof of security would open a right to intervene because some impact might result in the ultimate dividends realized from the estate. As well as unnecessary delay, the legal costs there associated could deplete the estate to no benefit.

31. The intervenor in the present instance framed its motion requesting to be authorized to intervene as an added party or, in the alternative, as a friend of the court for the purpose of addressing the propriety of proceeding under s. 135(4). It

was stated by the court at the outset that the question of subsection 135(4) would be addressed prior to the substantive issues of disallowance, regardless of the outcome of the motion to intervene.

32. For reasons above stated, the intervenor was allowed to address the court not as a party but as amicus curiae. The traditional principle is that an amicus curiae, as a non-party, is not subjected to cost consequences but neither does it benefit thereby.

33. Although these comments might suggest that no order of costs would issue in favour of the intervenor in the present circumstances, it cannot be said that the arguments by counsel for Lloyds were not helpful and as such, a limited order will issue.

34. The applicant shall pay costs to the respondent in the amount of $850.00 and to the intervenor in the amount of $500.00.

Michael J. Bray
Registrar

Court No. 16767 **2010 SKQB 182**
Estate No. 23-1169979 J.C.R.



**IN THE COURT OF QUEEN'S BENCH FOR SASKATCHEWAN**
**IN BANKRUPTCY**
**IN THE MATTER OF THE PROPOSAL OF**
**SOUTH BEACH HOMES LTD.**

**MAMCZASZ ELECTRICAL LTD.**

**Appellant**

**- and –**

**SOUTH BEACH HOMES LTD.**

**Respondent**

**- and –**

**PRICEWATERHOUSE COOPERS INC.**

**Respondent**

Barry Wilcox, for Mamczasz Electrical Ltd., the Appellant
David Gerecke, for Pricewaterhouse Coopers, the Trustee

**May 27, 2010** **L. SCHWANN, Q.C.**

[1] Mamczasz Electrical Ltd. ("M.E. Ltd.", or "the appellant") appeals from the trustee's disallowance of its claim made in a proposal by South Beach Homes Ltd. ("South Beach"). This appeal is brought pursuant to s. 135(4) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*").

## I. Factual Backdrop and Position of the Parties

[2] South Beach was incorporated by the Montreal Lake Cree Nation ("MLCN"), its sole shareholder, as a construction business whose enterprise principally entailed the construction of ready-to-move homes. South Beach encountered financial difficulty and by all accounts ceased operation in January 2008. Several months later a proposal to creditors was filed

pursuant to s. 50 of the *BIA* and M.E. Ltd., although not identified by South Beach as a creditor in its Statement of Affairs, filed a proof of claim. The trustee initially accepted part of the claim but requested supporting evidence on the balance. The trustee subsequently changed its position and the whole of the appellant's claim was disallowed.



[3] The trustee's assessment of the appellant's proof of claim has been complicated if not compromised by actions of the debtor best explained in the trustee's Form 40 report to creditors:

> In or around September 2008 a large portion of the banking records went missing or were destroyed. The Trustee has been able to obtain some records from the financial institutions. It appears that transactions were not properly recorded and it is believed that supporting documentation has likely been destroyed.

[4] As a result, both parties have attempted to reconstruct and augment the record with ancillary sources of information, and in some instances, by drawing inferences from the available information. It is from these supplementary sources and affidavit material the following factual backdrop is gleaned.

[5] In June 2006 South Beach entered into a service contract with Roman Mamczasz, an independent electrical contractor, to provide electrical contracting services for South Beach projects (the "services agreement"). Although not expressly stated, the parties intended this arrangement to serve as a training program for MLCN band members leading to journeyman status as electricians. Both parties accept that the services agreement was assigned to M.E. Ltd. shortly after its execution.

[6] The key features of this agreement were these:

- Roman Mamczasz would provide managerial and general electrical contracting services for the electrical needs of South Beach. In consideration of these services, South Beach agreed to pay him $85,000 per year in equal bi-weekly payments of $3,269.23 (clause 2(a)).
- The contractor was responsible for all expenses incurred and in return was to be reimbursed plus receive a "a mark up of twenty (20%) percent on all gross

invoices for all materials and supplies used (F.O.B site) and the expenses associated with all persons employed by the Contractor" (clause 2(a)).

- Invoicing for markup items was to be submitted every 14 days.
- Unpaid invoices attracted interest at 24% per annum.

[7] M.E. Ltd. filed a proof of claim on May 7, 2009 in the amount of $172,451.97 composed of the following:

| | |
|---|---|
| Managerial services | $ 94,807.67 |
| Goods, wares and services | $ 42,499.99 |
| Interest on services component | $ 27,990.34 |
| Interest on Goods, wares etc | $ 7,153.97 |
| | $172,451.97 |

[8] An amended proof of claim was filed several months later with the bulk of the increase attributable to managerial services. It broke down in the following manner:

| | |
|---|---|
| Managerial services | $124,230.74 |
| Goods, wares and services | $ 42,499.99 |
| Interest on services component | $ 31,980.06 |
| Interest on Goods, wares etc | $ 8,942.46 |
| | $207,653.25 |

[9] The trustee responded to the proof of claim by letter of September 15, 2009 as follows:

> We are prepared to accept and admit the proof of claim at this time for the amount of $133,489.20 based on the following information retrieved from the Contract for Services dated June 2006:
>
> | | |
> |---|---|
> | Managerial Services from December 1, 2007 to February 25, 2009 of 32 biweekly payments of $3,269.23 (Clause 2a) | $104,615.36 |
> | Interest at 24% on Managerial Services from December 1, 2007 to February 25, 2009 (Clause 2b) | 28,873.84 |
> | Total | $133,489.20 |
>
> In order to substantiate any claim for goods, wares and services and interest thereon, further supporting documentation is required.

[10] M.E. Ltd. responded with an affidavit of Roman Mamczasz (September 30, 2009) which attached as exhibits a substantial compilation of invoices from Eecol Electric Corp. ("Eecol") directed to M.E. Ltd. (the "Eecol invoices") covering the period August 30, 2007

until mid-December, 2007. Also attached was a hand made synopsis and a one page sheet entitled 'interest calculations'. In relation to these invoices Roman Mamczasz averred as follows:

> 4. That all of the items and materials and the corresponding charges set out in the invoices attached hereto collectively as Exhibit "A" were delivered to and incorporated into various projects of South Beach Homes Ltd. pursuant to their contract with Mamczasz Electrical Inc.
>
> 5. That the description shown in the upper-right hand corner of the Invoices under "your purchase order number" identifies the particular job of Southbeach Homes Ltd. where the materials were utilized.
>
> [September 2009 Affidavit of Roman Mamczasz,]



[11] I pause here to observe that while some of the invoices identify or use the name 'South Beach', many do not, and instead refer to individuals or other entities including the Montreal Lake Housing, a unit number, the RCMP and so forth. In a subsequent affidavit Roman Mamczasz said this on the issue:

> 16. That the "your purchase order number" notation on the Eecol Electric accounts was not to the name of a project being conducted independently by Mamczasz Electrical but was a notation as to the South Beach Homes Ltd. project on which the materials were being used. South Beach Homes Ltd. had several jobs that they were doing for MLCN and outside organizations such as the RCMP.
>
> 17. That Roman Mamczasz/Mamczasz Electrical, during the time in question, only had one client and that was South Beach Homes Ltd.
>
> 18. That the reasons that some of the Eecol Electric invoices are marked "tools" is because those were tools that were purchased for apprentices working within the program who were members of MLCN and employed by South Beach Homes Ltd. the reason some invoices are marked "shop" is because it gives they were unaware of the specific job this is the notation that was used.
>
> [March 2010 Affidavit of Roman Mamczasz]

[12] Notwithstanding its initial position on the managerial services component of the claim, the entire claim was subsequently disallowed. These reasons were given:

> Information contained in the records of South Beach Homes Ltd. indicates that at the date of the filing of the proposal there was no debt owing to Mamczasz Electric Ltd. In addition there is no evidence provided with the claim to show: that services required under the personal services contract were provided after February, 2007 by either Roman Mamczasz or Mamczasz Electric Ltd.; that there were not material breaches of the claimant's duties under the contract; that the claimant took all reasonable steps to mitigate any losses it may have suffered following the termination of the contract.

> Termination of the contract is supported by the fact that commencing in February 2007 and ending just prior to the discontinuation of the operations of South Beach Homes in January 2008, South Beach Electric (A subsidiary of Montreal Lake Business Ventures) replaced Mamczasz Electric Ltd. as the electrical contractor for the projects that were underway and Mamczasz Electric Ltd./Roman Mamczasz commenced providing services to South Beach Electric as of that date. The effect of this change was to terminate the services contract entered into between Roman Mamczasz/Mamczasz Electric Ltd. and South Beach Homes Ltd. in June 2006. As the claim does not show any amounts owing for services rendered prior to February, 2007 that portion of the claim against South Beach Homes Ltd. arising from the personal services contract and interest thereon is disallowed in its entirety; the sum of $156,210.80.
>
> The invoices provided by Mamczasz Electric Ltd. to support its claim, that $42,499.99 is owed for the provision of materials to South Beach Homes Ltd. are in fact invoices for purchases by Mamczasz Electric Ltd. from Eecol Electric Corp.
>
> No accounts rendered by Mamczasz Electric Ltd. to South Beach Homes Ltd. have been provided to support the claim as filed.
>
> The Eecol Electric accounts are for purchases made by Mamczasz Electric Ltd. commencing in August 2007. This is after the time when South Beach Electric took over as the electrical contractor for South Beach Homes Ltd.
>
> There are no documents provided that show that materials purchased from Eecol Electric were invoiced to South Beach Homes Ltd. by Mamczasz Electric Ltd. There are no documents provided that show that there are outstanding accounts owing by South Beach Homes to Mamczasz Electric Ltd. or that an amount remains outstanding for those accounts. Therefore that portion of the claim that relates to materials supplied to South Beach Homes Ltd. by Mamczasz Electric Ltd. and interest thereon is disallowed in its entirety; the sum of $51,442.45.

[13] The trustee amplified on his reasons and basis for disallowance in a very detailed affidavit filed in this appeal. He began with the debtor’s banking records. For 2006 these records show payments made to Roman Mamczasz and/or M.E. Ltd., after the services agreement was signed, followed by one last, lump sum payment of $50,000. This last payment effectively created a trust account with M.E. Ltd., contemplated by the services agreement, with the appellant given signing authority to draw down on the account.

[14] The payment history was quite different in 2007. Apart from several payments in the early part of the year, most of the payments were made to a new entity called *South Beach Electric*. The trustee subsequently discovered this entity was simply a business name owned by Montreal Lake Business Ventures Ltd. (“MLBV”). The records further show that MLBV,

South Beach Electric and Roman Mamczasz opened an account with the Bank of Montreal, although documentation pertaining to it is dated post January 2008.

[15] From an examination of the remaining South Beach records, the trustee says he was unable to locate any invoices from the appellant for the amounts now claimed. Further, the accounts payable summary for March 2008 (two months after ceasing business) fail to show any amount owing to M.E. Ltd.

[16] In the absence of any invoice or other substantiating documents to establish their claim, “the Trustee had no choice but to disallow the appellant’s Proof of Claim.” [Affidavit of Robert Meldrum, paragraph 8]

[17] The trustee buttressed this conclusion with what he refers to as an ‘inference’ drawn from the fact most of the payments for electrical services after February 2007 were made to South Beach Electric, and not to the appellant. The trustee concluded the services agreement had been terminated and that either South Beach Electric took over the electrical contracting work or stepped between South Beach and M.E. Ltd. as an intermediary. Based on the information before him, and the inference drawn from it, the trustee ultimately concluded no debt was owed to the appellant on the services agreement.

[18] The trustee further observes that as South Beach ceased operation in January 2008, no services could have possibly been provided thereafter.

[19] With regard to the claim for materials and supplies, the trustee’s position is simple: M.E. Ltd. didn’t render any invoices to the debtor; rather the invoices supplied to the trustee were those rendered to M.E. Ltd by Eecol (a third party supplier). The trustee makes these further observations:

- the period covered in the Proof of Claim does not match the vast bulk of the Eecol invoices as most predate that period;

- most of the invoices lack any reference to South Beach, accordingly it was impossible for the trustee to determine if the goods provided to the appellant by Eecol were used in connection with work done on behalf of South Beach;
- it is impossible to discern if any of the 'Montreal Lake' invoices were for South Beach projects or independent projects undertaken by MLCN; and
- several of the invoices were for tools.



[20] The trustee contends that it is highly irregular for a debt to be unsupported by a contemporaneous invoice and that an actual invoice is better proof than an after-the-fact, possibly self-serving affidavit. They further observe that when M.E. Ltd. issued invoices in 2006 and early 2007, those invoices were received and marked 'paid'.

[21] The trustee dismissed the interest claim out of hand based on the wording of the agreement which stipulated that interest would run two days after South Beach received the appellant's invoices. Having received no invoices, the trustee concluded no interest could run and therefore no liability for it arose.

[22] M.E. Ltd. filed a further affidavit in an attempt to address the trustee's arguments. Roman Mamczasz claims that in 2006 and 2007 cheques had been issued by South Beach directly to M.E. Ltd., however, as South Beach's accounting function was in considerable disarray, a new venture – MLBV – was established. That entity was to open sub-accounts, or create 'divisions' for each principal trade with the primary tradesperson given joint signing authority. This operational concept gave rise to *South Beach Electric*, which the appellant claims was purely a notional or artificial division.

> 5. That the idea of setting up the sub-accounts was that of staff of South Beach Homes Ltd. and I was advised that they believed that by making this arrangement, the money for payment of accounts would go into the proper sub-account and the appointed signor of the independent contractor could issue and sign cheques to the contracting entity (in this case Mamczasz Electrical) to pay the outstanding accounts and then only have to obtain the signature of one co-signatory. [March 2010, Affidavit of Roman Mamczasz]

[23] The appellant further observes that South Beach Electric was neither a legal entity nor an electrical contractor capable of obtaining electrical contracting permits in Saskatchewan. In fact all permits for the installation of electrical services on South Beach projects had been

issued to M.E. Ltd. (March 2010 Affidavit of Roman Mamczasz, paragraph 7). Copies of permits covering the period July 2007 to early January 2008 were attached as exhibits to his affidavit and all refer to the work location as ‘South Beach Homes’.

[24] As to the Eecol invoices, Roman Mamczasz urges this Court to accept them as proof of the outstanding debt for materials and supplies on the basis of his September 30th affidavit in which he swore to the fact all materials in the Eecol invoices were supplied on projects for South Beach Homes. This affidavit, he contends, is sufficient proof and no further invoice was necessary, nor for that matter, better proof.

[25] Finally, the appellant urges this Court not to visit the accounting disarray of South Beach upon it. Their persistent state of disarray, possible improper diversion of funds, destruction of records, and the likely co-mingling of accounts with other entities collectively puts M.E. Ltd. in an impossible position to properly prove its claim. These unique set of circumstances should have put the trustee on notice and prompted investigation of the books and records of South Beach Electric. Forcing the appellant to untangle the accounting mess, when it has neither the right of access nor legal powers of the trustee, places it at significant disadvantage.

[26] In spite of the confusing business and accounting arrangements, the appellant contends that it was at all times dealing with South Beach pursuant to the services agreement, and that all of its rights and the corresponding obligations must be viewed from that perspective. The appellant forcefully submits the agreement was never terminated by either side and that it simply expired by effluxion of time in April 2009. There is no evidence of actual termination and the trustee’s conclusion, based solely on inference, is unreasonable in the face of affidavit evidence to the contrary.

[27] Finally, the appellant accepts the trustee's initial allowance of its claim for managerial services plus interest (totaling $ 133,489.20), as set forth in the trustee's letter of September 2009.



## II. Issues

[28] This appeal raises these issues:

1. What is the nature of a s. 135(4) appeal? If an appeal from disallowance is a *de novo* appeal, can the trustee present additional evidence in response to affidavit material filed by the appellant, expand upon or provide background information in relation to its reasons for disallowance?
2. Which party bears the 'onus' of proving the claim?
3. Is the trustee's disallowance a nullity by reason of the fact a portion of the claim was initially admitted?
4. Did the trustee err in disallowing the claim?

## III. Analysis

### *1. The nature of a s. 135 appeal*

[29] The threshold question to any s. 135 appeal concerns the nature and scope of the appeal. Case law is divided on whether a s. 135 appeal should proceed on a *de novo* basis or as a true appeal limited to a review of the record.

[30] The *de novo* approach was adopted and new evidence relative to the claim admitted in the following cases: *Re Eskasoni Fisheries Ltd.* (2000), 16 C.B.R. (4th) 173; *Port Chevrolet Oldsmobile Ltd.*, 2004 BCCA 37, 49 C.B.R. (4th) 146. In contrast, other cases have declined to adopt the *de novo* approach opting instead to treat a s. 135 appeal as a true appeal on the record: *Re Galaxy Sports Inc.*, 2004 BCCA 284, 1 C.B.R. (5th) 20; *Johnson v. Erdman*, 2005 SKQB 515, 18 C.B.R. (5th) 97.

[31] As observed in *Able Automotive Ltd. v. Cameron-Okolita Inc*. (cited as *Re Foreman*) 2009 SKQB 476), more recent decisions have eschewed the rigid approach adopted in both *Galaxy Sports* and *Johnson v. Erdman* in favour of a more flexible, case by case approach.

(see for example: *San Juan Resources, Inc. Re*, 2009 ABQB 55, 52 C.B.R. (5th) 97 and *Lloyd's Non-Marine Underwriters v. J.J. Lacey Insurance Ltd.*, 2008 NLTD 9, 41 C.B.R. (5th) 137; *Business Development Bank of Canada v. Pinder Bueckert & Associates Inc.* , 2009 SKQB 458)



[32] Adopting the approach taken by this Court in *Able Automotive*, I conclude that the fact-sensitive nature of the issues presented in this appeal favours a *de novo* examination of the material. This conclusion is further influenced by the absence of any discernible 'record' and by the plethora of affidavit material filed by both sides upon which reliance was placed.

[33] Having determined this appeal should proceed on a *de novo* basis, is there any concern with the trustee filing further material to buttress or amplify its conclusions? The British Columbia Court of Appeal in *Port Chevrolet*, relying upon the decision in *Eskasoni Fisheries Ltd. Re, supra*, accepted an expansive approach, commenting as follows on the trustee's augmented material filed on appeal:

> I note that the ability of the Court to accept "new" evidence can operate in favour of either party: in *Eskasoni Fisheries Ltd.*, a trustee was permitted to advance a separate and distinct basis for disallowing a claim on the appeal in addition to the basis previously advanced at the meeting. (*Port Chevrolet*, para. 25)

[34] Based on the more recent jurisprudence, I am satisfied this appeal should proceed on a *de novo* basis and have therefore taken into account the affidavit material filed by both sides.

### *2. Which party bears the 'onus' of proving a claim?*

[35] To succeed, the appellant must establish that it has a claim provable in bankruptcy on the day on which the bankrupt became bankrupt. (The provisions of the *Act* pertaining to bankruptcy apply with necessary modification to Division I proposals (s. 66(1)). Section 121 of the *BIA* is the governing section and it provides:

> 121. (1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which

> the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

[36] The scope of 'debt' and 'liability', employed in that provision, has been succinctly summarized in text authorities:

> A debt is a sum due by certain and express agreement, a specified sum of money owing to some person from another, including not only the obligation of a debtor to pay, but the right of a creditor to receive and enforce payment. To be a provable claim, a debt must be due, either at law or in equity, by the bankrupt to the person seeking to prove a claim and must be recoverable by legal process.
>
> The meaning of the word "liability" is broader than that of the word "debt", including almost every character of hazard or responsibility and in particular, as provided in s. 121, includes all obligations to which the bankrupt is subject on the day on which he or she becomes bankrupt. [footnotes omitted] (Honsberger and DaRe, *Bankruptcy in Canada*, 4th ed, (Aurora: Canada Law Book, 2009) at p. 390)

[37] Failure to disclose a claim in its records or in its statement of affairs does not affect the validity of the claim and has been found to be an irrelevant consideration. *Flewitt v. Agravoice Productions Ltd. (Trustee of)* (1986), 61 C.B.R. (N.S) 280.

[38] Inasmuch as s. 121 deals with the substantive right to participate in estate assets, sections 121 and 135, read together, address the method and process employed to determine claims. These sections provide:

> 124. (1) <u>Every creditor shall prove his claim</u>, and a creditor who does not prove his claim is not entitled to share in any distribution that may be made.
> (2) A claim shall be proved by delivering to the trustee a proof of claim in the prescribed form.
> (3) The proof of claim may be made by the creditor himself or by a person authorized by him on behalf of the creditor, and, if made by a person so authorized, it shall state his authority and means of knowledge.
> (4) The proof of claim shall contain or refer to a statement of account showing the particulars of the claim and any counter-claim that the bankrupt may have to the knowledge of the creditor <u>and shall specify the vouchers or other evidence, if any, by which it can be substantiated.</u>
> . . .
> 135.(1) <u>The trustee shall examine every proof of claim or proof of security and the grounds therefor and may require further evidence in support of the claim or security</u>.
> (1.1) The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.
> (2) The trustee may disallow, in whole or in part,
> (a) any claim;

> (b) any right to a priority under the applicable order of priority set out in this Act; or
>
> (c) any security.
>
> (3) Where the trustee makes a determination under subsection (1.1) or, pursuant to subsection (2), disallows, in whole or in part, any claim, any right to a priority or any security, the trustee shall forthwith provide, in the prescribed manner, to the person whose claim was subject to a determination under subsection (1.1) or whose claim, right to a priority or security was disallowed under subsection (2), a notice in the prescribed form setting out the reasons for the determination or disallowance.
>
> (4) A determination under subsection (1.1) or a disallowance referred to in subsection (2) is final and conclusive unless, within a thirty day period after the service of the notice referred to in subsection (3) or such further time as the court may on application made within that period allow, the person to whom the notice was provided appeals from the trustee's decision to the court in accordance with the General Rules.
>
> (5) The court may expunge or reduce a proof of claim or a proof of security on the application of a creditor or of the debtor if the trustee declines to interfere in the matter.
>
> [emphasis added]

[39] It is undisputed that a creditor who wishes to participate and share in estate dividends must prove its claim. (s. 124(1) *BIA*) This process begins with filing a proof of claim in the prescribed form which shows and/or includes:

> … the particulars of the claim and any counter-claim that the bankrupt may have to the knowledge of the creditor and <u>shall specify the vouchers or other evidence, if any, by which it can be substantiated</u>." (s.124(4) *BIA*)

[40] The underlined words in s. 124(4) clearly impose an evidentiary burden on creditors to file sufficient and adequate material to enable the trustee to "make an informed decision as to whether the claim has merit." (Roderick Wood, *Bankruptcy & Insolvency Law*, (Toronto: Irwin Law, 2009) at p. 243) Subsection 135(1) imposes a corresponding duty on trustees to examine every proof of claim and the grounds in support to determine validity (s. 135(1) *BIA*). This duty extends to proposals. (*Re Toronto Permanent Furniture Showrooms Co.* (1960), 1 C.B.R. (N.S.) 16).

[41] Where a trustee is unsatisfied with the material provided in support of a claim, the trustee has both a right and duty to demand further evidence from the creditor. In the exercise of this duty, the trustee may conduct examinations or obtain the production of documents.

(see s. 163 *BIA*; Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada,* 4th ed. looseleaf, vol. 2, p. 5-181)

[42] The parties have elected to frame the issue as one of 'onus'. The trustee contends the onus of proof rests squarely with the claimant based both on the clear wording of s. 124 and as a matter of practical concern. Potential creditors possess the necessary information giving rise to an alleged claim along with the 'vouchers or other evidence' needed to support it.

[43] M.E. Ltd. takes the opposite position because of the unique challenges presented by this debtor. After having asserted a claim and provided what it believed to have been adequate supporting material, the trustee has sufficient material to make an informed choice, they submit. If it does not, then it must exercise its powers of examination to elicit evidence disproving their claim. They suggest this is so because only the trustee has access to the debtor's books and records along with an array of investigative tools which can be used to investigate them. An examination of the financial records of South Beach Electric or MLBV, they suggest, could possibly provide some answers however as a creditor, they don't have the means to access those records.

[44] Decided cases have framed the issue of onus or burden of proof in terms of creditors' duties and sufficiency of response. In *Re Norris* (1988), 67 C.B.R. (N.S.) 246 (Ont. Sup. Ct.) the trustee requested additional material from the creditor (Canada Revenue Agency "CRA") in support of its claim. The CRA in reply provided a copy of the notice of assessment (*Income Tax Act*, R.S.C. 1985, c. 1 (5th supp.)) but nothing more. The trustee found this reply inadequate and disallowed the claim. Although ultimately overturned on appeal on the 'adequacy' issue ((1989), 75 C.B.R. (N.S.) 97 (Ont. C.A.)), the following comments are worth noting:

> In my opinion the proof of claim with a statement of account, vouchers and/or supporting evidence should be sufficient to enable the trustee to make an informed decision as to whether the claim represents a claim which has merit and should be allowed or whether it is a claim unsupported by particulars and supporting material being in the nature of a claim which the trustee should disallow.

[45] The British Columbia Court of Appeal in *Port Chevrole*, *supra*, considered the appeal from the perspective of creditor compliance with s. 124(4) of the *BIA*. Examined factually, the Court found the creditor had failed to specify the vouchers or provide any other probative evidence to support its claim, and in consequence had failed to meet the threshold of 'sufficiency' required by s. 124(4).

[46] Case authority is quite clear: the creditor bears the onus of establishing its claim. It does so by providing vouchers, statement of account or other evidence sufficient to substantiate it. Put another way, the creditor must provide sufficient evidence so as to enable the trustee to make an informed decision on the validity of the proposed claim. The test to be applied when examining proofs of claim has been described as follows:

> In deciding the validity of a claim, *certainty* is not the test. If the method used in calculating the amount of the claim is reasonable <u>and the evidence in support of the claim is relevant and probative, the claim should be admitted.</u> *Re HDYC Holdings Ltd*. (1995), 35 C.B.R. (3d) 294. [Houlden and Morawetz p. 5-181; emphasis added]

[47] If a creditor adduces relevant and probative evidence from which a valid claim can be reasonably inferred, the test has been met and the claim is provable. In the face of that, particularly where a trustee has suspicions, the obligation shifts to the trustee to investigate further. Disallowing a claim based on a hunch or suspicion is not enough.

> The trustee is entitled to have all claims investigated and if, necessary, litigated before he or she can be called to pay….The trustee "is entitled to go behind such forms to get at the truth ….When the trustee is in doubt as to whether a claim should be allowed or disallowed, the trustee may apply to the court for directions.
> [*Bankruptcy In Canada*, p. 409]

[48] In the case at hand, M.E. Ltd. provided the trustee with a copy of the services agreement and interest calculation, which the trustee obviously felt was sufficient substantiation of the creditor's claim for unpaid managerial services because the claim was initially accepted. The trustee subsequently disallowed that part of the claim not because of insufficiency of evidence, but on other grounds. The appeal on this part of the claim, as

discussed more fully later on, turns on whether the trustee erred in concluding the claim was invalid.

[49] The claim for goods and services involves a more fundamental issue as the trustee's disallowance turned on the insufficiency of probative evidence. The issue can be reduced to this: was the information supplied sufficient so as to enable the trustee to make an informed decision? Was it relevant and probative?



***3. Is the trustee's disallowance a nullity by reason of the fact a portion of the claim was initially admitted?***

[50] Before turning to the central issue on appeal, I must first address the issue of whether the trustee is permitted to re-consider all or part of a creditor's claim in circumstances where it was initially allowed.

[51] To recap, following receipt of the appellant's proof of claim, the trustee initially accepted and admitted the managerial services and related interest component of the claim totaling $133,489.20. The formal disallowance subsequently issued on December 10th reversed that position by disallowing the whole of the claim including the previously accepted portion.

[52] This chain of events reflects a clear reversal of position. Whether, having initially admitted the claim, does the trustee have authority to subsequently reverse its decision? There are two cases on point and both decidedly ruled in favour of the trustee. In *Drummie, Re*, 2004 NBQB 35, 49 C.B.R. (4th) 90, Registrar Bray concluded that nothing in the *Act* precluded the trustee from acting on new information with s. 135(4) offering an aggrieved creditor judicial oversight of the trustee's decision. At para. 20 he said:

> 20 The *Act* does not make the determination of a provable claim by the Trustee final and conclusive as it does for a disallowance. Had the legislators wished to limit the competence of the Trustee to review a decision under subsection (1.1) of section 135 of the *Act*, when further evidence is received, they surely would have done so in terms as clearly as those enacted in subsection (4). [see also *Dyrland, Re*, 2008 ABQB 356, 47 C.B.R. (5th) 243 at para. 53]

[53] M.E. Ltd. contends the trustee does not possess an unfettered right of re-consideration, and its power to do so is confined to circumstances where substantial new evidence comes to light. Permitting unfettered reconsideration of claims without any new evidence is improper, they argue. No case law was provided in support.

[54] While this argument has some attraction, I am of the view it cannot succeed in the absence of any evidence of prejudice on the part of the creditor. Had M.E. Ltd. demonstrated reliance on the initial allowance to its detriment, its position would have some strength, however in the absence of such evidence I see no reason to disrupt the existing jurisprudence. In any event, as aptly observed in *Drummie*, the creditor has recourse to the appeal remedy in s. 135(4) if it wishes to challenge the trustee's decision.

**4. *Did the trustee err in disallowing the claim?***

***a) the claim for managerial services***

[55] As the claim rests on the services agreement, I find it helpful to set out the relevant provisions:

> 2(a) The Employer shall pay the Contractor in consideration for providing such services, the sum of Eight-Five Thousand ($85,000.00) Dollars, per annum in lawful Canadian Dollars without deduction, to be paid in equal biweekly payments in the sum of Three Thousand, Two Hundred and Sixty-Nine ($3,269.23) and Twenty-Three Cents plus a markup of Twenty (20%) percent of all gross invoices for all materials and supplies used (F.O.B. site) and the expenses associated with all persons employed by the Contractor.
>
> (b) The Contractor shall submit its invoice for all markup items on the 19th day of June and thereafter every 14 days during the term of this contract. The remuneration set out in a) above shall be paid to the Contractor within Two (2) days of his submission of his invoice to the Employer. Failure to do so will result in interest been payable at the rate of Twenty-Four (24%) percent per annum, payable at the time of payment of the invoice.

[56] As previously noted, the trustee initially allowed this portion of the claim plus interest but subsequently re-considered based not on a lack of substantiation of the evidence but on the following reasons: 1) no obligation to pay arose without an invoice for services rendered; 2) the contract had been terminated in 2007; and 3) as South Beach ceased operation in January 2008, the appellant could not have provided services to South Beach beyond that point in time.



[57] Although the services agreement cannot be described as a model of good drafting, the amount of compensation agreed upon for managerial and general contracting services was expressed clearly and unequivocally, i.e. in exchange for the services provided, you shall be paid $85,000 yearly at the bi-weekly rate of $3,269.23. The 'services', described in clause 1(a) encompassed 'managerial services for the purposes of electrical contracting and staffing'. The agreement was signed in June 2006 and continued in full force and effect for a period of three years up to and including the 30th day of April 2009, unless sooner terminated. (clause 4(a))

[58] The trustee contends South Beach's obligation to pay under the services agreement arose only if and when an invoice was submitted, and without an invoice, no debt exists. I do not agree. The debtor's obligation to pay arises from the wording of the services agreement, which I find to be clear and unqualified.

> Generally speaking the parties to a contract are obliged to perform in accordance with the express and implied terms of the contract. The duty to perform must be carried out precisely and exactly…...The duty to perform may also be qualified or otherwise affected by a provision in the contract under which liability for non-performance may be excluded or limited in some other way. Failing such modifications of contractual duties, whether intrinsic to the contract or resulting from subsequent unilateral or bilateral conduct, the contract must be performed with strict adherence to its language and meaning. (G.H.L. Fridman, *The Law of Contract*, 5th ed. Carswell, p. 531-532.)

[59] The parties expressly put their minds to the services contracted for and the compensation to be paid for it. Payment was not qualified or contingent in any way. Admittedly the wording of clause 2(b) clouds the issue somewhat by inclusion of this

following language: “remuneration *set out in (a) above* shall be paid to the Contractor within Two (2) days of his submission of his invoice to the Employer.” While clause 2(a) embraces both the managerial services and materials and supplies components, I do not interpret this language to mean South Beach’s liability to pay for managerial services was contingent on submission of an invoice. To the extent 2(b) applies to managerial services, if at all, its application is limited to the matter of interest, dealt with more fully below. Accordingly, I conclude that South Beach’s legal obligation under the agreement was not contingent on submission of an invoice and the absence of one does not extinguish its obligation to pay for the services provided.



[60] The second ground - termination of the services agreement - is without merit and cannot stand in the face of more tangible evidence. There is absolutely no evidence to support the trustee’s contention that this agreement had been terminated either by agreement of the parties or otherwise. Roman Mamczasz provided a copy of the services agreement. There is no dispute as to the validity of the agreement or of the debtor’s obligations to pay for the services provided under it. The trustee in fact, takes no issue from date of execution until February 2007.

[61] It was at this point, the trustee argues, the contract was terminated. The trustee bases this conclusion on the fact South Beach Electric became the payee of electrical services, from mid-February 2007 until the end of 2007.

[62] There are several problems with the trustee’s approach. First, there is nothing to support the trustee’s inference that South Beach Electric assumed responsibility for the provision of electrical contracting work. South Beach Electric was simply a business name owned by MLBV. It wasn’t a legal entity, or a ‘person’ for purposes of electrical licensing. As Roman Mamczasz explains, South Beach Electric was simply a ‘division’ created to facilitate the orderly payment of trade accounts. M.E. Ltd., on the other hand, was the entity which obtained required electrical permits from the licensing authority, copies of which were

appended to his March affidavit. Only an electrical contractor can apply for and obtain such permits.



[63] Second, even if payments depict South Beach Electric as the payee for most of 2007, the final two payments that year were in fact made to M.E. Ltd.. This fact further undermines the trustee's theory of contractual termination.

[64] Finally, no evidence was filed to support the trustee's alternate contention that the appellant had been paid for its services by South Beach Electric or that the legal relationship had shifted from the debtor to South Beach Electric. This point is made clear in Roman Mamczasz's affidavit.

> 8. THAT Roman Mamczasz/Mamczasz Electrical always operated totally independently from MLCN/South Beach Homes Ltd., however, MLCN/South Beach Homes Ltd. always handled their business matters incestuously and it was always very difficult or impossible to distinguish the true legal entity with which I was dealing which inevitably made the situation very confusing. However, I only had contractual arrangements with South Beach Homes Ltd. and therefore believe that I was always dealing with that entity. As well as independent projects of South Beach Homes Ltd., its mandate was to act as the contractor for MLCN with respect to all of their building and maintenance requirements and South Beach Homes Ltd. was owned solely by MLCN.
>
> . . .
>
> 17. THAT Roman Mamczasz/Mamczasz Electrical, during the time in question, only had one client and that was South Beach Homes Ltd. [March 2010 Affidavit of Roman Mamczasz]

[65] In contrast, Roman Mamczasz offers a plausible explanation as to why money was paid to South Beach Electric, and how and why it came about. Moving the payables from the debtor to individual sub-accounts or divisions was an arrangement developed by South Beach to ensure proper allocation and timely payment of sub-trades. South Beach Electric was only notional; services continued to be provided by independent contractors. [see March 2010 affidavit of Roman Mamczasz, paras. 2-7]

[66] The answer to the trustee's suspicions may lie in the books and records of South Beach Electric however none of that information was produced on appeal, nor for that matter

was any evidence adduced from the debtor who is in the best position to lend credence to the trustee's theory. The trustee contends that it bears no obligation to investigate further, and they are correct. However where a trustee disallows a claim based on suspicion or inference in the face of otherwise relevant and probative evidence, something more is required.



[67] The last ground of disallowance was based on the contention that no claim can exist for services after January 2008 when South Beach ceased operations. The appellant's initial proof of claim sought recovery of $94,807.67 for the period December 1, 2007 until February 25, 2009, or a period of 449 days. The claim was later amended to extend coverage to April 30, 2009.

[68] No evidence was provided or explanation given for either time frame however, in all likelihood, the amended claim was intended to correspond with the expiry date of the services agreement. That approach, however, is inconsistent with the fact South Beach ceased operations in January 2008 (exact date not provided) and the wording of the services agreement. Clause 2(a) thereof provided:

> 2(a) The Employer shall pay the Contractor <u>in consideration for providing such services</u>, the sum of Eight-Five Thousand Dollars ($85,000) per annum...

[69] In accordance with the wording of the agreement, the debtor's obligation to pay arises when services are provided, and if unpaid, becomes a debt subject to legal enforcement. The unchallenged evidence of the trustee is that South Beach ceased operations in January 2008, which corresponds with the time frames on the Eecol invoices and the electrical contracting permits (with a few exceptions in early January 2008). It stands to reason that as no services could have been provided to South Beach after it ceased to be in business, no obligation to pay arose under the agreement for which a debt can be claimed. The fact the agreement had an unexpired term does not mean the appellant has a right of compensation for the value of the services *it would have provided* had South Beach not ceased operation.

[70] The appellant has a provable claim for managerial services for the period December 1, 2007 until mid January 2008, which I calculate to be $10,624 (1 ½ months x $3,269.23).

***b) Interest for unpaid managerial services***

[71] The right to claim interest for unpaid managerial services is wholly governed by clause 2(b) of the Agreement. It provides:

> 2(b) The Contractor shall submit its invoice for all markup items on the 19th day of June and thereafter every 14 days during the term of this contract. The remuneration set out in a) above shall be paid to the Contractor within Two (2) days of his submission of his invoice to the Employer. Failure to do so will result in interest been payable at the rate of Twenty-Four (24%) percent per annum, payable at the time of payment of the invoice.

[72] The trustee determined interest was contingent on submission of an invoice. I agree. There is no other legal basis to claim interest other than by contract, accordingly the intent of the parties, as expressed in this provision, must govern.

[73] With regard to interest, the parties agreed that payment would be made within two days following submission of an invoice, and "failure to do so will result in interest been payable at the rate of Twenty-Four (24%) percent per annum, payable at the time of payment of the invoice."

[74] The parties expressly provided if and when interest would accrue and the time period for calculating the amount. Their respective rights and obligations turned on submission of an invoice, accordingly, absent an invoice, no liability arose. The trustee was correct in this part of the disallowance.

[75] There is another basis upon which interest on unpaid managerial services can be disallowed and it stems from the opening sentence of clause 2(b). It provides: "The Contractor shall submit its invoice for all <u>mark up items</u> on the 19th day of June and thereafter every 14 days during the term of this contract." Arguably this wording limits the scope of clause 2(a) to 'mark up items', which is in reference to materials and supplies. This

interpretation is consistent with the intent of the parties to pay managerial services every two weeks on an ongoing basis (hence no need to invoice), coupled with the expectation on the part of the appellant to be reimbursed promptly for out of pocket expenses.

***c) the claim for materials and supplies***

[76] Like the claim for managerial services, the appellant's claim under this ground rests on the wording of the services agreement. To repeat, this is what the parties agreed to:

> 2(a) The Employer shall pay the Contractor in consideration for providing such services…….<u>plus a markup of Twenty (20%) percent of all gross invoices for all materials and supplies used (F.O.B. site) and the expenses associated with all persons employed by the Contractor</u>." [emphasis added]

[77] The parties' intent was clear: the appellant was to be reimbursed for materials and supplies and employee expenses, plus 20%, on those expenses incurred in the course of providing electrical contracting services on South Beach projects.

[78] The trustee disallowed this part on insufficient grounds: "no accounts rendered by Mamczasz Electric Ltd. to South Beach Homes Ltd. have been provided to support the claim as filed". [Form 77 Notice of Disallowance] The invoices provided were those rendered by Eecol to the appellant, and not from the appellant to the debtor. In any event, the trustee concluded the claim could not be proven because the Eecol invoices covered a period which was "after the time when South Beach Electric took over as the electrical contractor for South Beach Homes Ltd.". [Notice of Disallowance]

[79] The appellant contends this part of its claim is amply supported by the two affidavits filed by Roman Mamczasz. In particular, in his March 2010 affidavit, he swore to the following:

> 13. That because of extremely confusing methods of payment used by South Beach Homes Ltd., the amount being claimed for "goods, wares and services as per paragraph 6 of the claim and clause 2b) of the contract dated June, 2008 in the sum of $42,499.99 was calculated by totaling the Eecol Electric accounts for which I know were on account of South Beach Homes Ltd. and for which that payment has not been received from South Beach Homes Ltd."

> . . .
> 16. That the "your purchase order number" notation on the Eecol Electric accounts was not to the name of a project being conducted independently by Mamczasz Electrical but was a notation as to the South Beach Homes Ltd. project on which the materials were being used. South Beach Homes Ltd. had several jobs that they were doing for MLCN and outside organizations such as the RCMP.
> . . .
> 18. That for the reason that some of the Eecol Electric invoices are marked "tools" is because those were tools that were purchased for apprentices working within the program who were members of MLCN and employed by South Beach Homes Ltd. the reason some invoices are marked "shop" is because it gives they were unaware of the specific job this is the notation that was used.

[80] The trustee refutes this approach. His practice as a bankruptcy trustee is to require creditors to produce invoices 'or similar back-up documentation' to establish their claim. M.E. Ltd. was unable to do this to the trustee's satisfaction. Paragraph 8 of the trustee's affidavit summarizes the grounds of refusal:

> 8. . . . In the absence of any indication in the records of South Beach that anything was owing to the Appellant, and without any invoices or similar back-up documentation (either in South Beach's records or in the documents received from the Appellant), the Trustee had no choice but to disallow the Appellant's Proof of Claim.

[81] To succeed, the appellant need only produce relevant and probative evidence of its claim. I find the compilation of the Eecol invoices coupled with Roman Mamczasz's averments (set out above) sufficient proof of its claim. The trustee says it is not possible to connect these invoices to work done on South Beach projects, however the evidence given in paragraphs 16-18 of Roman Mamzcasz's affidavit draws a direct link and satisfactorily addresses their concern.

[82] The trustee contends that no weight should be given to these affidavits because they are self-serving and in any event, the services agreement requires invoicing directly from the supplier before liability to pay arises. The agreement required the appellant to "submit *its* invoice for all markup items" every 14 days. (clause 2(b)) Giving effect to the words '*its invoice'* evinces an intention on the part of the parties for M.E. Ltd. to prepare and submit an invoice. However, in the absence of any of their own invoices, as opposed to copies from

their third party supplier, does South Beach have any liability to pay? Is its claim supported by relevant and probative evidence?

[83] For the reasons expressed above, I conclude liability does not hinge on, or is in any manner contingent upon invoicing. South Beach clearly agreed to reimburse for materials, supplies and expenses plus 20%, and this obligation was not contingent or qualified in any way by submission of an invoice. The evidence filed in support is sufficient, relevant and probative, and establishes the appellant's claim.



[84] Furthermore, I find the appellant's description of the debtor's utter state of confusion and disarray with the manner it handled accounts payable, coupled with the fact many of its records are now missing, to be a reasonable answer to the trustee's suspicions on this part of the claim as well. Accordingly, I am prepared to allow this part of the appeal. The appellant's claim for materials and supplies in the amount of $42,499.99 is therefore allowed. Nothing further is added for mark up because the appellant never advanced this part of its claim and in any event abandoned it in argument.

[85] The appellant's claim for interest under this heading cannot succeed for the same reason given above in relation to the managerial services. Unlike the other portions of the claim, South Beach's liability to pay interest was wholly contingent on submission of an invoice, such that in the absence of an invoice, interest does not accrue and cannot be claimed.

## IV. Disposition

[86] The appeal from the trustee's disallowance of the managerial services claim is allowed to the extent of $10,624. The appeal from the trustee's disallowance of the appellant's claim for materials and supplies is also allowed to the extent of $42,499.99. The appeal from the trustee's disallowance of the interest claims is dismissed. An order shall issue to that effect.

[87] As there is divided success, there will be no order as to costs.

DATED at the City of Regina, in the Province of Saskatchewan, this 27th day of May, A.D. 2010.

Registrar in Bankruptcy

# COURT OF APPEAL FOR BRITISH COLUMBIA

Citation: ***New Skeena Forest Products Inc., Re,***
2005 BCCA 192

Date: 20050401
Docket: CA032484

Between:

**In the Matter of the *Companies' Creditors Arrangement Act*,**
**R.S.C. 1985, c. C-36**
**and**
**In the Matter of the *Canada Business Corporations Act*,**
**R.S.C. 1985, c. C-44**
**and**
**In the Matter of the *Company Act*, R.S.B.C. 1996, c. 62, as amended**
**and**
**In the Matter of New Skeena Forest Products Inc.,**
**Orenda Forest Products Ltd., Orenda Logging Ltd. and**
**9753 Acquisition Corp.**

Respondents
(Petitioners)

And

**Kitwanga Lumber Co. Ltd.**

Respondent
(Respondent)

Before: The Honourable Mr. Justice Esson
The Honourable Madam Justice Newbury
The Honourable Mr. Justice Smith

R.J.M. Janes and M.D.B. Paine — Counsel for the Appellant City of Prince Rupert

R.A. Millar — Counsel for the Interim Receiver and Trustee in Bankruptcy Ernst & Young Inc.

P.J. Reardon — Counsel for 646325 B.C. Ltd.

R.D. Leong — Counsel for the Attorney General of Canada

| | |
|---|---|
| D.J. Hatter | Counsel for Her Majesty the Queen in Right of the Province of British Columbia |
| Place and Date of Hearing: | Vancouver, British Columbia<br>February 28, 2005 |
| Written Submissions Received: | March 22, 24, 29 and 30, 2005 |
| Place and Date of Judgment: | Vancouver, British Columbia<br>April 1, 2005 |

**Written Reasons by**:
The Honourable Madam Justice Newbury

**Concurred in by:**
The Honourable Mr. Justice Esson
The Honourable Mr. Justice Smith

**Reasons for Judgment of the Honourable Madam Justice Newbury:**

[1] On August 30, 2004 New Skeena Forest Products Inc. ("New Skeena"), formerly known as Skeena Cellulose Inc., brought to an end its most recent attempt at financial restructuring under the ***Companies' Creditors Arrangement Act*** ("CCAA") by filing an assignment in bankruptcy. The last CCAA proceeding had been initiated in November 2003 when the Supreme Court made an order in the usual terms, staying proceedings against the company, authorizing debtor-in-possession ("DIP") financing to rank ahead of most other charges, appointing a monitor, and granting New Skeena the right to "proceed with an orderly disposition" of its assets in order to facilitate the "downsizing and consolidation of [its] business and operations". But the strenuous efforts made by many creditors and other stakeholders to streamline and restructure New Skeena's business — a mainstay of the economy of northwestern British Columbia — ultimately failed, and the decision was made to move the company into liquidation.

[2] On September 20, 2004, the Supreme Court lifted the stay previously imposed under the CCAA, imposed a new stay under the ***Bankruptcy and Insolvency Act***, and appointed Ernst & Young Inc. as receiver to offer for sale "all or any of the Assets, including any of the properties (whether real, personal or otherwise), rights, assets, businesses, and undertakings of the Company, whether *en bloc* or on a piecemeal basis, as a going concern or otherwise, but subject to the approval of [the Supreme] Court." An auction of many of the remaining assets is scheduled for April of this year.

[3] It is para. 17 of the September order which is significant for purposes of this case. It directed the Receiver to report to the Court concerning the "enforcement" of the so-called "Priority Charges" and the allocation of the sale proceeds of New Skeena's assets proposed to be made by the Receiver among the secured creditors. The order also specified that any proposed allocation could not defeat the priority afforded to any Priority Charges under the Court's previous orders or seek to invoke marshalling or other equitable principles applicable to creditors' remedies. In due course, the Receiver recommended a scheme of allocation of the Priority Charges and it was approved by the Chambers judge below. The discrete question raised by this appeal is whether he erred in so doing, and in particular, whether it was open to him to approve an allocation that may require one key creditor to pay as its share of the Priority Charges an amount greater than its secured charge and indeed greater than what is said to be the true value of the asset against which it holds its security.

[4] This question is complicated by two facts. First, the creditor with which we are concerned is the City of Prince Rupert, appellant in this court. Its security is a statutory tax lien and the enforcement thereof is governed by the ***Local Government Act***, R.S.B.C. 1996, c. 323. Under that Act, the local collector must in September of each year offer for sale by public auction any real estate on which taxes are delinquent. (Evidently, certain obligations under the tax sale provisions of the Act were postponed by special Act of the Legislature in response to the plight of Prince Rupert and other neighbouring municipalities affected by New Skeena's insolvency, but no further special deferments are anticipated.) The upset price at such auction is specified by s. 407(1) and in this case would exceed some

$18,000,000, the amount of the City's unpaid taxes. If no bid is received at least equal to the upset price, s. 407(4) of the Act states that the City "must be declared the purchaser" of the property. Thus it is possible the City will not receive an offer at or above the amount of its claim, and that it will be deemed to be the purchaser of the property. In return it would receive nil proceeds, at least until it succeeds in selling the property at some future time. Obviously, this could take years, and the ***Local Government Act*** preserves for some time the owner's ability to redeem the property: see ss. 414-418. In any event, the City stands to receive only the upset price and interest thereon.



[5] The second complicating factor is that the value of the property over which the City holds its statutory lien is New Skeena's now defunct kraft pulp mill, located on Watson Island. The value of this property is unknown: although in recent years it was assessed for tax purposes at some $8,480,000, an appraisal carried out in January 2004 set its value at only $3,920,000. Now, there are indications that the property may carry a large environmental liability. There is some evidence, which the Chambers judge below did not expressly adopt, that the cost of decommissioning the mill and restoring the property to its original condition might be as much as $100,000,000 — although it seems unlikely any purchaser of the mill site would be willing to do more than restore it to "industrial" standard. Remediation to that standard is expected to cost something less, and the Province has agreed to provide up to $30,000,000 for the latter purpose. However, the possibility of a large liability remains, and to date, no private party has expressed interest in acquiring the property on terms that the Receiver has recommended for acceptance.

[6] Together, these facts are said to place the City in a different position from that of other secured creditors: when the value of their interests falls below the amount of the secured indebtedness, most can simply accept the lesser amount, or even walk away from their secured claim. Indeed, most are lenders who have taken the business risk that their borrower will fail and that their security may prove inadequate to realize their claims. This is not true of the City, however: it is prohibited from accepting less than the statutory upset price, and "must" take the property as its own (subject to the owner's right to redeem) if no offer is received at or above the statutory minimum. This also gives rise to a general 'unfairness' argument that informs the City's other more specific arguments regarding process and jurisdiction.



***Factual Background***

[7] I turn first, however, to the background of the impugned order of December 1, 2004, which adopted the method of cost allocation proposed by the Receiver. I note at the outset that the City, like all other secured creditors, had consented to the granting of "super-priority" for the DIP financing approved by the Court early on in the CCAA proceeding. The initial order of November 19, 2003 granted to one DIP lender, NWBC Timber & Pulp Inc. ("NWBC"), security in an amount up to $2,300,000, "ranking in priority to all creditors of the Petitioners and any other encumbrances, security or security interests now outstanding save and except for the Administration Charge and the Directors' Charge which shall rank in priority to the DIP Charge." Subsequent orders reduced the principal amount of NWBC's priority and approved further borrowing from Northern Savings Credit Union ("NSCU") and granted that lender a charge ranking ahead of all charges (including

NWBC's DIP Charge) other than the Administration Charge. Still further DIP financing, the "Woodbridge DIP Loan", the "MatlinPatterson DIP Charge", and the "Papyrus DIP Charge", was approved on similar terms in the summer of 2004 without any objection being made by the other secured creditors. However, the CCAA stay was, as earlier mentioned, finally lifted on September 20, 2004.



[8] Pursuant to para. 17 of the Order of that date, Messrs. Ernst & Young prepared a report for the Court dated November 19, 2004 (the "Second Report"). The Receiver advised the Court of its progress (or lack thereof) in selling off the New Skeena assets and undertaking as a going concern. Under the heading "The Receiver's Sale Process", the Receiver stated:

> 33. At the commencement of the receivership process, the Receiver was advised by a number of significant secured creditors that they believed that the opportunities to transact with a credible *en bloc*, going concern buyer had been exhausted through what was expressed to be a lengthy and expensive CCAA process, and that they expected the Receiver to conduct a quick sale process with an emphasis on liquidation. The creditors were extremely clear in their communications with the Receiver that the administration, holding and preservation costs associated with the asset realization and receivership administration process were viewed as substantial. Their view was that a lengthy, multi-month asset marketing campaign was unnecessary and to the detriment of their recoveries.
>
> 34. The Receiver recognized the views expressed by these creditors with regard to the length of the sales process and the associated costs, but also recognized that it was important to pursue offers of an *en bloc* or operator nature, including opportunities for acquiring specific mill sites, concurrently with seeking liquidation proposals, given the very significant impact of the New Skeena assets on the economies of the local communities.
>
> 35. The Receiver commissioned an updated asset appraisal of the Company's machinery and equipment from Maynards

> Appraisals Ltd., the firm that conducted the January 2004 appraisal during the CCAA proceedings. No updated appraisal was commissioned for the Company's mill site real estate, as the Receiver considered this to be of a lower cost benefit. Appraisals of the Company's two residential properties situated in Prince Rupert were commissioned, and these properties were listed for sale with a local realtor. [Emphasis added.]



[9] The Receiver's proposal for the allocation of the "Court Ordered Charges" was set out in detail at Appendix F to the Report. The terms "Court Ordered Charges", "Priority Charges" and "CCAA Costs" were all used to refer to the aggregate of the "Administrative Charge" (consisting of the monitor's professional fees and fees for legal services rendered to the monitor and New Skeena), the "DIP Loan Charge" (consisting of amounts advanced by the DIP lenders mentioned above), and the "Directors' Charge" (consisting of amounts for which the directors of New Skeena might have become liable as a result of the insolvency). According to the report, the Administrative Charge amounted to approximately $1,484,000; the DIP Loan Charge was some $3,250,000; and no amount was outstanding in respect of the Directors' Charge.

[10] The Receiver noted that no attempt had been made in the CCAA proceedings to track these Charges "against the various assets of [New Skeena] or the interests of any creditor or creditor group" and that there had been no discussion of the burden each group of assets might be expected to bear in relation to the costs of the CCAA process. The Receiver expressed the view that it was important for the secured creditors to be able to assess their positions reasonably when considering the potential sale of the assets and that "[w]ithout a framework that contemplates

some reasonable expectation as a basis for distributing costs, a realistic assessment of potential sales [would] be very problematic for secured creditors to undertake." This was particularly so with respect to New Skeena's real estate, since it was uncertain when those assets would be sold and, the Receiver stated, it would be "cumbersome to rely on a framework for cost allocation that takes effect only upon the full liquidation of all assets." Further, it would be "neither productive nor accurate" to try to link the CCAA Costs to any specific asset or creditor. Accordingly, the Receiver recommended that:

> 15. As a proxy for the expected values being preserved or enhanced by undertaking the CCAA proceeding, and accordingly incurring the CCAA Costs, <u>an appropriate reference would be appraisals of real estate and equipment at the operating locations of New Skeena</u>. The Monitor commissioned these appraisals in January 2004 as part of the sales efforts at that time. Those appraisals represent information which was current at the time that the CCAA Costs were being incurred, and formed at least some context for the potential value of the restructuring efforts.
>
> 16. The real estate appraisals did not consider potential environmental issues that may be prevalent on a given site, and so do not necessarily represent the best possible indication of value. Not all operating locations were appraised, and the real estate information is therefore incomplete insofar as the major participants in the CCAA process are concerned.
>
> 17. One alternative would be to use the values provided by the BC Municipal Assessment Authority instead of the appraised values (the "Tax Values"). The Tax Values can consist of land only, or can include the improvements on the lands as well. Use of the Tax Values as a value basis has the advantage of being a consistent measure of value, in that each property has a Tax Value for assessment purposes, and has the further advantage of matching expected values against the basis by which the municipal tax obligations are computed.

> 18. When comparing the calculation of improvements for Tax Value purposes with the equipment appraisals performed by Maynards, it is apparent that there is opportunity for overlap between these two categories. There is not a direct method of assessing this potential overlap, or calculating a corrective measure. As well, when comparing the land portion of the Tax Value with the appraised values to the extent both are available, it would appear that the Tax Value of both lands and improvements is higher than the value attributed to the real estate in the appraisal information. Accordingly, it is the Receiver's view that <u>preference should be given to use of the appraised value of the lands, where available, and to use Tax Values for those other properties where necessary</u>.
>
> 19. <u>The Receiver's proposal is to use appraised values as a basis for allocating the CCAA Costs pro rata against those operating assets for which appraisals are available,</u> and in the cases where no land appraisals were commissioned to use the land portion only of the Tax Values, all on an interim basis as described further below. The use of Tax Values shall only apply to land at the operating locations of New Skeena.
>
> 20. Using appraised or assessed values instead of ultimate sale values to allocate costs represents, in some respects, an artificial measure by which to burden participants in the process. By using a measure that is a proxy for ultimate sales value, rather than that sales value itself, <u>the Receiver recognizes that those who believe they may be adversely affected by this basis of allocation may question this proposal</u>. [Emphasis added.]

This method, the Receiver stated, would provide an "independent basis" for dealing with the interests of secured creditors at an early stage of the distribution process. It would avoid "waiting for particular asset sales to occur before allocating costs", and minimize additional disputes "to the extent that actual sales of assets contain price allocations that may be arbitrary, as could occur in multi-asset sales or if secured creditors take assets using their security positions as partial satisfaction of the transaction price." In the Receiver's analysis, the certainty provided by the use of the appraised or assessed values would outweigh "the lack of precision inherent in using a measure other than the actual sales values obtained."

[11] Accordingly, the Receiver recommended that with respect to those operating lands and equipment for which appraisals or assessments were available, an interim allocation of the CCAA Costs in full would be carried out. But notwithstanding the use of the term "interim", no later adjustment would be made to reflect the actual sale of these assets, including the Prince Rupert mill site. In the Receiver's words:

> 26. The Receiver's proposal is to apportion the CCAA Costs pro rata against the equipment and lands appraised in January 2004, on the basis of appraised values or Tax Values, as the case may be, rather than eventual sale proceeds. It is not proposed that the calculation of allocated costs be adjusted subsequently as sales of those assets occur. [Emphasis added.]

[12] Under the heading "Distributions of Sale Proceeds", the Receiver acknowledged the possibility that certain assets could "accumulate a level of allocated costs in excess of their ultimate sales value." In such cases, the Receiver said:

> . . . it is proposed that the shortfall in cost recovery become an additional General Cost, and [be] allocated against the remaining appraised and/or sales values as the case may be.
>
> 40. In the event that a secured creditor seeks to recover the asset against which it holds security, as for example could occur in the instance of a municipality taking title to real property rather than it being sold by the Receiver, then the Receiver would ask that the Court permit such a transaction to be completed only if, and when, the secured creditor provides the Receiver with the cash equivalent of the applicable allocated costs against that asset, as calculated by the Receiver under this proposal. [Emphasis added.]

It is this aspect of the proposal to which the City of Prince Rupert objects.

[13] It does not appear that the recommendations contained in the Second Report were the subject of a court order. Rather, the Chambers judge requested certain additional information, leading to the Receiver's Third Report, dated November 29, 2004. It dealt with various substantive matters and again returned to the subject of cost allocation, on which the Receiver had received further comments from counsel for the concerned municipalities and others. The Receiver noted that certain of the municipalities (including Prince Rupert) had objected to the use of an appraisal that failed to consider any environmental liability attaching to the mill site. Another creditor had objected to the use of asset values generally, suggesting that funds actually generated from the DIP loans be traced to the locations or assets on which such funds had been spent, and that costs be allocated on that basis.

[14] With respect to Prince Rupert's objections, the Receiver responded as follows:

> 52. The assessed value for tax purposes of the Prince Rupert land is $8.48 million, whereas the appraised value used in our cost allocation proposal is $3.92 million. The environmental remediation program currently being funded by the Province has seen almost $19 million of a total funding available of $30 million already expended, and our understanding from discussions with the professional remediation firm is that the completion of this project will render the Watson Island site comparable in condition to other industrial sites in the Province. <u>The use of a value for the Prince Rupert lands is, in the Receiver's view, appropriate in the context of the ongoing remediation and the expectation that this likely will be a site with commercial value in the future</u>, given its physical attributes of rail and water access to facilitate shipping and materials handling opportunities.

> 53. The Receiver understands that any reductions by the Assessment Authority in assessed values, due to the closure of operations, will affect only the industrial improvements values and not the land values, and so the values used in the Receiver's proposal would be unaffected by that development which, in any event, is prospective. [Emphasis added.]



[15] With respect to the proposal that costs be linked to DIP loan expenditures, the Receiver predicted that hardly any costs could be directly tied to the interests of the secured creditors in real estate, which would mean that the cost burden would rest almost entirely on the secured creditors having interests in equipment and other operating assets. In conclusion, the Receiver stated:

> Using a method of allocation that simply traces costs gives no recognition to the underlying basis for the CCAA process and the restructuring effort, which is to preserve and enhance the value of all assets, including the real estate, and in the Receiver's view is therefore inappropriate.
>
> 56. The comments from counsel for the various affected creditors have been considered further by the Receiver, but the Receiver remains of the view that <u>the process set forward in our Receiver's Report #2 provides an appropriate outcome of allocation, taking into account the multiple objectives of early certainty as to the parties' exposure to costs, the relative ability of the affected assets to absorb the allocations (or, alternatively, the various parties' abilities to fund those costs) and the roles played by the various parties during the CCAA and receivership proceedings</u>. [Emphasis added.]

### ***The Order of the Chambers Judge***

[16] The matter came on for hearing before the Chambers judge on December 1, 2004. In his oral reasons, he briefly reviewed the Receiver's proposal as set out in

its Second and Third Reports. With specific reference to Prince Rupert's situation, he reasoned:

> With the exception of Prince Rupert all of the parties here want to have certainty at this stage. Prince Rupert says that the value that is proposed to be used in its case, which is the appraised value of $3.92 million, is unrealistic because it is simply not known whether this property will fetch that amount, or even any amount, given the environmental contamination issues.
>
> At paragraph 52 of his report number three, the Receiver addresses the conservatism in his proposal. The Receiver points out that the assessed value of the land set by Prince Rupert for tax purposes is some $8.48 million; the appraised value used by the Receiver for the purpose of this cost allocation proposal is $3.92 million.
>
> There has been an ongoing remediation effort on the Prince Rupert mill site, which has been funded by the Province. Some $19 million of a total funding available of $30 million has been spent. While there is some issue as to the likely market value of these lands, it is the Receiver's view that, given this remediation which has taken place, and given the remediation which is going to continue, that the appraised value figure is a realistic figure to use for the purposes of his proposal.
>
> The reality is that no method, in these circumstances, is perfect. The only way to achieve perfection, as I said at the outset, is to do nothing until everything has been sold. That clearly would not serve the interests of the parties and it is one that simply does not make sense. [paras. 16-19]

In the result, the Chambers judge concluded that it was in the best interests of all the parties to accept the Receiver's recommendation with respect to the cost allocations. The entered Order provided in this regard:

> 6. the Receiver's proposal:
>
> (a) to allocate the CCAA Costs (as defined in the Report) on a preliminary basis against only those assets consisting of equipment and real property which are identified in the illustrative chart attached to Appendix F to the Report

> (the "Assets"), pro rata based upon the appraised or assessed value of the Assets at January, 2004, provided that such preliminary allocation will be subsequently adjusted based upon:
>
> (i) the actual sale proceeds realized on the future disposition of the <u>remaining assets</u> of the Petitioners which do not have values attributed to them in Appendix F as aforesaid; or
>
> (ii) such other value as may be subsequently attributed to such remaining assets by the Court; and
>
> (b) to allocate the Receivership Costs (as defined in the Report) by:
>
> (i) firstly, applying specific costs directly attributable against specific assets; and
>
> (ii) secondly, applying any specifically allocated costs not fully recoverable from specific assets together with all general receivership costs which cannot be specifically allocated, pro rata against all assets on the same basis as the CCAA Costs;
>
> is hereby approved, provided that the obligations of any affected creditor to pay its portion of the allocated costs in relation to any asset where they hold a first priority position (subject to the prior CCAA Costs and Receivership Costs) is [sic] postponed, pending further application at the time that the Receiver applies for approval to distribute any of the proceeds generated from the sale of any of the Petitioners' assets; [Emphasis added.]

[17] It is worth emphasizing that notwithstanding the reference to "preliminary" allocation in subpara. 6(a) of the Order, the only adjustment contemplated is in respect of sale proceeds received from the "remaining assets" (which I understand consist mainly of intangibles such as forestry licences) and that no adjustment is contemplated in respect of the sale proceeds of the assets with which we are here concerned — those items of equipment and real property referred to in Appendix F

to the Receiver's Second Report. Further, the Order does not specifically incorporate the Receiver's recommendation that if and when a secured creditor seeks to recover an asset on which it holds its security, the Court will permit such a transaction to be completed "only if, and when, the secured creditor provides the Receiver with the cash equivalent of the applicable allocated costs against that asset, as calculated by the Receiver under this proposal." Instead, the Order "postpones" the obligation of any creditor to pay its portion of the allocated costs in respect of any asset on which it holds first priority, pending further application. However, the Chambers judge did approve the entire proposal for cost allocation set out in the Receiver's reports and counsel have all agreed that the Court intended to impose the condition on recovery described at para. 12 above. I will also proceed on that assumption, although it would have been preferable if the Order had been worded to reflect this important aspect of the recommendation.

***On Appeal***

[18] In this court, the City submits that the Chambers judge made two basic errors of law in acceding to the Receiver's recommendation regarding the allocation of CCAA Costs: first, that in exercising his discretion the Chambers judge "ignored" a relevant factor, namely, the actual value of the asset in question; and second, that it did not lie within the jurisdiction or discretion of the Chambers judge to approve an allocation that carried with it the risk that a secured creditor — i.e., the City — would have to pay to the Receiver an amount that exceeds the value of its security interest on the Watson Island property.

[19] Counsel for the City acknowledged that the CCAA, which consists only of 22 sections, gives the court a broad discretion, in the sense that the court must consider a wide variety of competing interests which are likely to vary greatly from case to case. (See S. Waddams, "Judicial Discretion", (2001) 1 ***Cmnwth. L.J.*** 59.) As we observed in the previous *Skeena* appeal (***Clear Creek Contracting Ltd. v. Skeena Cellulose Inc.*** (2003) 13 B.C.L.R. (4th) 236, 2003 BCCA 344), the case law that has developed under the CCAA "fills the gaps" between the provisions of the statute and has been informed by the "broad public policy objectives" thereof:

> There is now a large body of judge-made law which "fills the gaps" between these provisions. Most notably, courts appear to have given full effect to the "broad public policy objectives" of the Act, which in the phrase of a venerable article on the topic (Stanley E. Edwards, "Reorganizations under the Companies' Creditors Arrangement Act", (1947) 25 *Can. Bar Rev.* 587) are to "keep the company going despite insolvency" for the benefit of creditors, shareholders and others who depend on the debtor's continued viability for their economic success. . . .
>
> In accordance with these objectives, Canadian courts have adopted a "standard of liberal construction" that serves the interests of a "broad constituency of investors, creditors and employees" and reflects "diverse societal interests." (See *Re Smoky River Coal Ltd.* (1999) 175 D.L.R. (4th) 703 (Alta. C.A.), at 721-2.) [paras. 34-35]

[20] Consistent with this approach, Canadian courts have now accepted that their discretion may be exercised to permit DIP financing and to grant "super-priority" to DIP lenders, albeit subject to certain restrictions and safeguards: see Michael B. Rotsztain, "Debtor-in-Possession Financing in Canada: Current Law and a Preferred Approach", (2000) 33 Can. Bus. L.J. 283, at 284-87; and ***Re United Used Auto & Truck Parts Ltd.*** (1999) 12 C.B.R. (4th) 144 (B.C.S.C.), aff'd (2000) 16 C.B.R. (4th) 141 (B.C.C.A.), superseding the more restrictive approach taken in

***Robert F. Kowal Investments Ltd. v. Deeder Electric Ltd.*** (1975) 59 D.L.R. (3d) 492, 21 C.B.R. (N.S.) 201 (Ont. C.A.) and ***Lochson Holdings Ltd. v. Eaton Mechanical Inc.*** (1984) 55 B.C.L.R. 54 (B.C.C.A.). Appellate courts also accord a high degree of deference to decisions made by Chambers judges in CCAA matters and will not exercise their own discretion in place of that already exercised by the court below. This court has stated that its powers should be exercised "sparingly" when it is asked to interfere with the exercise of discretion of a CCAA court: see ***Clear Creek***, *supra*, at para. 52, citing ***Re Pacific National Lease Holding Corp.*** (1992) 72 B.C.L.R. (2d) 368, and ***Re Smoky River Coal Ltd.*** (1999) 175 D.L.R. (4th) 703 (Alta. C.A.). In the more general context, I note the statement of Viscount Simon L.C. in ***Charles Osenton & Co. v. Johnston*** [1942] A.C. 130 (H.L.), which was quoted by the majority of the Supreme Court of Canada in ***Friends of the Old Man River Society v. Canada (Minister of Transport)*** [1992] 1 S.C.R. 3, at 76-77. Viscount Simon L.C. stated:

> The law as to the reversal by a court of appeal of an order made by the judge below in the exercise of his discretion is well-established, and any difficulty that arises is due only to the application of well-settled principles in an individual case. The appellate tribunal is not at liberty merely to substitute its own exercise of discretion for the discretion already exercised by the judge. In other words, appellate authorities ought not to reverse the order merely because they would themselves have exercised the original discretion, had it attached to them, in a different way. [at 138]

At the same time, discretionary decisions are not immune from review. As Viscount Simon L.C. stated in the same case:

> But if the appellate tribunal reaches the clear conclusion that there has been a wrongful exercise of discretion in that no weight, or no sufficient

> weight, has been given to relevant considerations such as those urged before us by the appellant, then the reversal of the order on appeal may be justified. [at 138]

(See also ***Harelkin v. University of Regina*** [1979] 2 S.C.R. 561 at 588, where it was said that in refusing to take into consideration a "major element for the determination of the case", the trial judge had failed to exercise his discretion on relevant grounds and thus gave the Court of Appeal "no choice" but to intervene.)



[21] The City contends that the Chambers judge in the case at bar "ignored" or failed to consider a relevant matter — the actual value of the Watson Island property — and proceeded on an irrelevant criterion — whether a previous appraisal had been carried out — in approving the allocation method he did. Mr. Janes referred us to ***Musqueam Indian Band v. Glass*** [2000] 2 S.C.R. 633, where the Supreme Court of Canada held that the Federal Court of Appeal had wrongly interfered with a trial judgment fixing the "value" of a leasehold interest in certain reserve lands. The Court of Appeal had ruled that the value should be determined on the basis of land in fee simple with no reduction for the fact that it was located on a reserve. However, the Supreme Court of Canada restored the trial judgment, Gonthier J. noting for the majority that the Indian band was bound to "accept the realities of the market". (Para. 44.) Similarly, in ***Cowichan Tribes v. Canada*** (2003) 314 N.R. 384, [2003] F.C.J. No. 1919, the Federal Court of Appeal upheld a trial judgment which, in determining the "fair market rental value" of property that was subject to flooding, took that susceptibility into account. Létourneau J.A. for the Court stated that "[i]t defies common sense to think that a prudent and reasonable

developer or tenant would allocate the same value to a land that is partly flooded annually as it would to a land that is not so flooded and that is ready for development or occupation. This is not a question of law: this is a fact of life, a practical reality which . . . the mortgage lenders and the insurers will soon remind you of when they assess the risk they have to assume." (Para. 9.)



[22] In response to the City's submission that the Chambers judge in the case at bar erred in the same manner as the Federal Court of Appeal in ***Glass***, counsel for the Receiver says it is implicit in the Chambers judge's Reasons that he did not accept the "negative value theory" with respect to Watson Island, particularly in light of the fact that the Province has already spent more than $19,000,000 in restoring the mill site. Mr. Millar characterized the evidence of remediation liability of $100,000,000 as "entirely vague" and noted that that estimate had included the cost of decommissioning and closure (dismantling, demolition, removal, transportation, resloping and grading) of the mill site. In his submission, it is unrealistic to think that this will ever be done in the near to middle term, and the Chambers judge must be taken to have been of the opinion that the property did have commercial value by reason of its location, its facilities, and the remediation work.

[23] In my view, these are the kinds of considerations which the Chambers judge (who has heard most if not all of the Chambers applications relating to New Skeena) was especially qualified to make. Moreover, I do not agree that the Chambers judge "ignored" the issue of the true value of the Watson Island property. He specifically referred to this matter at paras. 16-18 of his Reasons (quoted above), but at the end of the day he concluded that "perfection" in terms of matching values with costs, was

outweighed by the need for certainty and expediency. In my view, assuming for the moment that the Court had the jurisdiction to make the order it did, the Chambers judge was entitled to weigh these competing interests and to decide that the interests of all the creditors as a group overshadowed the City's particular objections.

[24] Two other factors raised by the City, however, do in my view cast greater doubt on the Court's exercise of its discretion. First, there is the fact that Prince Rupert's security and the remedies available to it are very different from those of other creditors. As has been seen, if the Watson Island property cannot be sold, the ***Local Government Act*** requires Prince Rupert to take the land, environmental liabilities and all, whether or not it will realize anything after payment of its share of the CCAA Costs. Not surprisingly, there is no case law directly on point, but in ***Re Hunters Trailer & Marine Ltd.*** (2001) 305 A.R. 175, [2001] A.J. No. 1638 (Alta. Q.B.), the Court said it would be unfair to ignore "differences in the type of security held by various creditors and the degree of potential benefit that might be derived by them from CCAA proceedings" in allocating CCAA costs. Thus the Court in ***Hunters*** approved the allocation of a share of CCAA costs to a mortgage lender that was smaller than the shares allocated to other creditors. Wachowich C.J.Q.B. commented:

> The CCAA recognizes that there may be different classes of creditors for purposes of voting on a plan of arrangement or compromise. Would UMC as first and second mortgagee of Hunters' real property have been placed in a different class than the other secured creditors? There is no significant difference in the nature of the debt giving rise to the claim. However, there is a difference in the nature and priority of

> UMC's security, the remedies that were available to it and the extent of its recovery.
>
> Under the circumstances, I conclude, as did the Interim Receiver, that UMC is in a different position than that of the other major secured creditors and it would not be equitable that it be allocated the same proportion of CCAA costs. I agree with the Interim Receiver's proposal that UMC be charged 15 percent of the Monitor's fees and $500.00 of the Monitor's legal fees, the same percentage proposed for its share of the interim receivership costs. I note that UMC also agreed with this proposal.
>
> Under the Interim Receiver's proposal, UMC is not allocated any of the DIP financing costs. The Interim Receiver and UMC take the position that UMC received no benefit from the DIP financing and therefore should not be required to contribute to repayment of these funds.
>
> Not only UMC but all of the secured creditors can point to costs that cannot be attributed to the assets over which they hold security. However, DIP financing was granted to meet the debtor company's urgent needs during the sorting-out period. That was for the benefit, at least the potential benefit, of all creditors. . . .
>
> I am of the view that UMC must bear a proportion of the DIP financing costs. I recognize that any means of calculating that percentage will be arbitrary. A strict accounting on a cost-benefit basis would be impractical. I am prepared to allocate five percent of the DIP financing costs to UMC, in addition to that share of the Monitor's fees and legal expenses identified above. [paras. 20-23 and 26]

[25] My second concern is that the Chambers judge proceeded on the assumption that there were urgent time pressures militating in favour of cost allocations that provided immediate certainty to creditors of what they were likely to be receiving net of the CCAA Costs. Indeed, at para. 3 of his Reasons, the Chambers judge noted that "time is the enemy of enterprise value" and at para. 19 that it would clearly not serve the interests of the parties to "do nothing until everything has been sold". But at this state of New Skeena's existence, the hope of "enterprise value" has had to give way to the reality of liquidation value, all efforts at restructuring the business of

the company as a going concern having failed. As in ***Re Weststar Mining Ltd.*** (1993) 75 B.C.L.R. (2d) 16 (B.C.C.A.), "The battle for the survival of the Company is over, at least for the time being. What remains is merely to determine priorities. . . ." (Para. 58, *per* McEachern C.J.B.C. dissenting, whose judgment was adopted by the Supreme Court of Canada on appeal at [1993] 2 S.C.R. 448.) The Chambers judge was not facing a "now or never" determination. As Mr. Janes noted, he could have elected to recognize the unusual position of the City and await any sale that might occur within a reasonable time. Failing such a sale, he could assign a value based on more up-to-date evidence. In the meantime, interim allocations and distributions could be made. In this regard, I note that para. 4 of the December 1 Order stated:

> 4. The sale proceeds from the sale of each specific asset shall stand in the place and stead of the asset sold and all liens, claims, encumbrances and other interests that are attached to an asset prior to its sale shall attach to the sale proceeds with the same validity, priority and in the same amounts, and subject to the same defences, that existed when the liens, claims, encumbrances and other interests attached to the asset;

As counsel for the Receiver suggested, this provision obviates in large measure any time pressure which might have made a more exact allocation of costs and proceeds impractical. Assets can be sold to the highest bidder free and clear of encumbrances. The charges attach instead to the proceeds held by the Receiver, and interim allocations and distributions can be made subject to final adjustment, all without unduly inconveniencing creditors.

[26] I would prefer, however, not to decide this appeal on the basis that the Chambers judge erred in the exercise of his discretion by failing to give due weight

to the two factors I have described. Again, an appellate court should not interfere with an exercise of discretion in the present context where the question is one of the weight or degree of importance to be given to particular factors, rather than a failure to consider such factors or the correctness, in the legal sense, of the conclusion. Instead, I turn to the more fundamental question of jurisdiction — whether it lay within the Chambers judge's authority to adopt a method of cost allocation that might require the City to pay as its share of CCAA Costs an amount greater than the value of the land over which it holds its tax lien. I note that Mr. Janes and Mr. Millar have confirmed their view that this question relates to the equitable and statutory jurisdiction of the Court under the CCAA rather than under the ***Bankruptcy and Insolvency Act***.

[27] Mr. Janes for the City submitted that the potential imposition of a "personal liability" on the City over and above its interest in the Watson Island property is fundamentally inconsistent with the entire CCAA scheme, which empowers the court to impose stays and compromise creditors' rights but not to impose further financial liabilities on creditors. He characterizes the scheme as providing a "shield, not a sword". In his submission, this principle is implicit in s. 11 of the Act, which permits a court to stay, to restrain and to prohibit various proceedings (see especially, ss. 11(3) and (4)); and it is explicit in s. 11.3, which states:

> 11.3 No order made under section 11 shall have the effect of
>
> (a) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; or

(b) requiring the further advance of money or credit.
[Emphasis added.]

Further, Mr. Janes contends that the orders made during the CCAA proceedings in this case which permitted the DIP loans and granted the "super-priority" to them, all contemplated that the CCAA Costs would be paid out of the proceeds of realization of the assets, not out of additional funds to be advanced by creditors. Certainly there was no explicit reference to the possibility that any secured creditor might have to advance or contribute funds beyond its existing exposure.



[28] Mr. Janes also notes what he calls the "perverse" effect of the cost allocation order in this case: while the unsecured creditors, who were the parties who stood to gain the most from the attempted restructuring of New Skeena, will bear none of the CCAA Costs under the proposed allocation, the City of Prince Rupert will, if the Watson Island property cannot be sold for the statutory "upset price", actually end up worse off. Its unpaid tax debt will go unpaid and it will have to pay something — likely between $1.5 and $2.5 million — in CCAA Costs. This is particularly anomalous when one considers that the Legislature intended to grant municipalities such as the City of Prince Rupert a very high level of priority for its claims for unpaid taxes.

[29] Counsel also notes the caution with which courts have approached the granting of the "extraordinary" remedy of priority for DIP financing, as illustrated by ***United Used Auto***, *supra*, at paras. 21-30 (B.C.S.C.). In that case, Tysoe J. quoted a passage from the judgment of Blair J. in ***Re Royal Oak Mines Inc.*** (1999) 6 C.B.R. (4th) 314 ((Ont. Gen. Div.) and a passage from a judgment of Farley J. in

***Royal Oak Mines Inc.*** (1999) 7 C.B.R. (4th) 293 (Ont. Gen. Div.). Farley J. stated in part:

> Aside from the question of the lienholders who have registered liens which but for the Initial Order granted by Blair J. (but subject to the comeback clause) would have priority over the DIP financing, I see no reason to interfere with this superpriority granted. It would seem to me that Blair J. engaged properly in a balancing act as to the $8.4 million of superpriority DIP financing as authorized. I am in accord with his views as expressed in *Re Skydome Corporation* [(1998), 16 C.B.R. (4th) 118 (Ont. Gen. Div.)], where Blair J. stated [at para. 13]:
>
> > This is not a situation where someone is being compelled to advance further credit. What is happening is that the creditor's security is being weakened to the extent of its reduction in value. It is not the first time in restructuring proceedings where secured creditors - in the exercise of balancing the prejudices between the parties which is inherent in these situations - have been asked to make such a sacrifice. Cases such as *Re Westar Mining Ltd.* (1992), 14 C.B.R. (3d) 88 (B.C.S.C.) are examples of the flexibility which courts bring to situations such as this. See also *Re Lehndorff Gen Partner* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div.); *Olympia & York Developments Limited v. Royal Trustco* (1993), 17 C.B.R. (3d) 1 (Ont. Gen. Div.).
>
> Implicit in his analysis and part of the equation is the reasonably anticipated benefits for all concerned which derive from these sacrifices. [para. 5; emphasis added.]

Tysoe J. in ***United Used Auto*** stated that in his view, "there should be cogent evidence that the benefit of DIP financing clearly outweighs the potential prejudice to the lenders whose security is being subordinated." (Para. 28.) He was not so satisfied in that case and therefore declined to approve the application for a prior charge to secure DIP financing which was before him.

[30] The City emphasizes the underlined sentence in the quotation above from ***Re Skydome Corporation*** and contrasts that with the situation here, where the City

may well be "compelled" to advance further funds from its pocket simply in order to "recover" an asset that will fall into its possession in any event as a matter of law and that has little or no market value at present. (I note parenthetically that no argument was made by the City to the effect that the imposition on the City of the condition reproduced at para. 12 of these Reasons contravenes s. 403(1) of the ***Local Government Act***, which requires that the local collector offer "each parcel of real property on which taxes are delinquent" for sale by public auction on the last Monday in September. See the discussion in ***Clear Creek***, *supra*, at paras. 40-42.)

[31] The Receiver contends on the other hand that the proposed cost allocation is simply a consequence of the original grant of priority to the DIP financing early on in the CCAA process, and that it was "implicit in any priority scenario that where a creditor took title to an asset, it would have to first satisfy the burden of the Charge." In the Receiver's analysis, the question in this case is not whether the Order was made without jurisdiction by virtue of the fact that it imposes a "personal liability" on the City, but rather whether it is appropriate that "if the City takes the property in lieu of taxes, it must as a condition of that taking, discharge or pay any priority charge that affects the property. That the City would have to discharge that liability upon taking title is a most uncontroversial and self-evident proposition. If one takes the benefit of an asset [one] must discharge the burdens associated with it."

[32] Counsel also emphasizes that under the terms of the Order and the Receiver's recommendation, the City would not be required to "ante up" any amount unless it decided to take the property into its own name — i.e., that the City's obligation to pay the share of the CCAA Costs would not apply if the Watson Island

property were sold to a third party without the City having to "recover" it. Further, since the mill was the "primary asset" of New Skeena, the City should, Mr. Millar argues, properly bear a large portion of the costs incurred in trying to sell the business as a going concern — a possibility that had obvious potential benefits for the City and its inhabitants. As for s. 11.3 of the CCAA, Mr. Millar says that it is not aimed at the situation with which we are concerned, but rather is intended to allow creditors the right to require "C.O.D." payment under supply contracts with the insolvent company.



[33] I agree that para. (a) of s. 11.3 was intended for the purpose Mr. Millar describes, but para. (b) appears to have a wider reach that is engaged by the facts of this case, assuming the Chambers judge's order of December 1, 2004 was an order "made under s. 11" of the CCAA. (On this latter point, neither counsel for the City nor the Receiver argued to the contrary.) In my view, the effect of the Order is to require the further advance of money or credit in certain circumstances. Considering the purpose and tenor of the Act, which does generally operate as a "shield, not a sword", I am persuaded that the Chambers judge strayed beyond his authority in acceding to the recommendation of the Receiver that if a secured creditor sought to recover the asset against which it holds security, the creditor should be required as a condition of such transaction to pay to the Receiver in cash the amount of CCAA Costs allocated against that asset. To the extent that a creditor could be required to pay funds in excess of the value of its security interest, such a condition was not, in my view, an inevitable aspect of the granting of DIP priority but

instead was an unusual feature that, in the almost unique circumstances of this case, contravenes s. 11.3(b). I would therefore allow the appeal.



[34] The question then is what order this court should make to permit the sale of New Skeena's assets to proceed as quickly and conveniently as possible, while recognizing the City's unusual situation as a secured creditor. The City sought an order to the effect that the CCAA costs should be allocated on the basis of actual values as and when they are realized, or alternatively, that the Watson Island property be treated in the same way as the "remaining assets" referred to in the Order — i.e., based upon such values as may be attributed by the court. I find the latter alternative more attractive in that it does not affect all the other assets, minimizes the accounting that will be required, and thus retains much of the efficiency of the original order. It will be clear from these Reasons, however, that if and when the time comes for the Court to allocate a value to the Watson Island property for the purposes of allocating the CCAA Costs, the effect of the order cannot be to require that Prince Rupert pay cash from its pocket as a condition of taking the property, the "value" (as determined by the Court) of which is less than the amount required to be paid.

***Costs***

[35] The City sought an order of costs "on a substantial indemnity scale, such costs not to form part of the Receiver's charge against the assets of the bankrupt." I would ask that the City provide us with written submissions of law concerning this

prayer, to be filed within 15 days of the issuance of these Reasons. I would then ask the Receiver to file its written submissions within 10 days of the latter date.

“The Honourable Madam Justice Newbury”

I Agree:

“The Honourable Mr. Justice Esson”

I Agree:

“The Honourable Mr. Justice Smith”

**COURT FILE NO.:** 31-395548
**DATE:** 2004-11-02



**ONTARIO**

**SUPERIOR COURT OF JUSTICE**

| | |
|---|---|
| **B E T W E E N:** | |
| In the Matter of the Bankruptcy of OSFC Holding Limited, a Company Duly Incorporated under the Laws of the Province of Nova Scotia with its Principal Place of Business in the City of Toronto in the Province of Ontario | |
| | Murray B. Page, Q.C., for the Trustee, BDO Dunwoody Limited<br>Geoffrey B. Morawetz for Thorsteinssons<br>Surksha Nayar, for the Minister of National Revenue<br>Kevin O'Hara, for the Ministry of Finance for the Province of Ontario |

**<u>REASONS FOR DECISION</u>**

**<u>Pepall, J.</u>**

<u>Request</u>

[1] BDO Dunwoody Limited, the Trustee in Bankruptcy of OSFC Holding Limited, seeks an order pursuant to section 34 of the *Bankruptcy and Insolvency Act* for advice and directions.

<u>Facts</u>

[2] There are no material facts in dispute. The debtor, OSFC, has two creditors of substance: Canada Customs and Revenue Agency ("CCRA") and the Ontario Ministry of Finance (the

"Ministry"). The claims of these entities are $4,594,464.63 and $1,670.367.94 respectively. There is also another claim of $3,745 in favour of Steel Investments Ltd. The indebtedness of OSFC to the two major creditors arises from adverse tax assessments made in reliance on the General Anti-Avoidance Rule ("GAAR") provisions found in the *Income Tax Act* and the *Corporations Tax Act (Ontario)* respectively. OSFC had been entitled to a tax refund of $3,500,000 but CCRA applied the refund to OSFC's outstanding tax liability. The reassessments were unsuccessfully appealed to the Tax Court and then to the Federal Court of Appeal. OSFC then sought leave to appeal the Federal Court of Appeal decision to the Supreme Court of Canada. The Supreme Court of Canada denied OSFC leave on June 20, 2002.

[3] On February 14, 2002, OSFC filed a proposal in bankruptcy and was subsequently deemed to have made an assignment in bankruptcy. On March 4, 2002, the Trustee disallowed the claims of CCRA and the Ministry on the grounds that, as the Supreme Court of Canada had not rendered its decision, the indebtedness was contingent. The disallowances were appealed to the Registrar in Bankruptcy. After the Supreme Court refused leave to appeal, the Registrar allowed the appeals on consent of the Trustee. Those orders are dated July 4, 2002 (the "Registrar's orders"). CCRA and the Ministry appointed themselves as the two inspectors of the bankrupt's estate.

[4] OSFC had had partners who engaged in a tax scheme similar to that of OSFC. They too were reassessed and were unsuccessful in both the Tax Court and the Federal Court of Appeal. Unlike OSFC, however, their leave to appeal application to the Supreme Court of Canada was granted on June 24, 2004. The appeal is scheduled to be heard on March 7, 2005. According to the affidavit of Mr. M. G. Williams of Thorsteinssons, this appeal and another will be the first GAAR cases heard by the Supreme Court of Canada.

[5] Not surprisingly, the shareholders of OSFC wish a motion to be brought before the Supreme Court for reconsideration of OSFC's original application for leave to appeal and for an extension of time. The essence of the motion is that it would be manifestly unjust if OSFC's partners were able to dispute the reassessments while OSFC could not. The threshold test for reconsideration of an application for leave to appeal is set out in Rule 73 of the Supreme Court of

Canada Rules. It provides that there shall be no reconsideration of an application for leave unless there are exceedingly rare circumstances in the case that warrant consideration by the Court. It is obviously not for this Court to determine the issues that would be before the Supreme Court.

[6] If OSFC's motion and appeal were successful, subject to addressing the Registrar's orders, the claims of the two creditors would be extinguished and the bankrupt's estate would be entitled to receive the tax refund which now amounts to approximately $5,000,000 inclusive of interest.

[7] Thorsteinssons acted for OSFC on its original leave to appeal application. It has made a proposal to the Trustee wherein it would bring an application to the Supreme Court on behalf of the Trustee requesting that that court reconsider OSFC's original leave application. There would be no charge or cost to the bankrupt's estate in the event that any of the proceedings in the Supreme Court were unsuccessful. The Trustee also has advised the Court that Thorsteinssons has agreed to provide the Trustee with an indemnity with respect to any adverse costs awards made and that the Trustee is satisfied with the form and content of that indemnity. While the proposal also addressed payment of legal fees in the event that the reassessments were vacated by the Supreme Court of Canada, I am not giving, nor am I being asked to give, any directions in that regard.

[8] It was apparent to the Trustee that approving the proposal presented by Thorsteinssons would put the inspectors in a conflict of interest as the benefit of a successful appeal would be to the detriment of these two creditors. In these circumstances, the Trustee applied for directions from the Court. No consent to the proposal has been forthcoming from these two creditors in their capacity as inspectors.

[9] Those two creditors take the position that the Trustee should be directed to refuse Thorsteinssons' proposal. They state that if the Trustee proceeded, it would be acting against the interests of creditors. The administration of the affairs of the estate is to be governed according to the direction of the inspectors. Furthermore, the Registrar has already determined that the claims of CCRA and the Ministry are valid.

Discussion

[10] This is a most unusual situation. If any one of the motions or appeal to the Supreme Court of Canada is unsuccessful, the issue becomes moot. On the other hand, if the appeal is successful, subject to setting aside the Registrar's orders, the indebtedness of the two major creditors would be negated and the tax refund would be payable to the estate.

[11] Firstly, there is the issue of the Registrar's orders. Although the Registrar upheld the claims of CCRA and the Ministry, section 187 (5) of the *BIA* provides that every court may review, rescind or vary any order made by it under its bankruptcy jurisdiction. If the Trustee were successful in the Supreme Court of Canada, it would then have to move for relief pursuant to this section. While the decision of *Re Taylor*[1] may be interpreted as possibly favouring the position taken by the two main creditors, relief pursuant to section 187 (5) is discretionary and that issue should not be determined as part of the motion before me.

[12] Secondly, I agree with the Trustee's conclusion that consideration of the proposal would put the inspectors in a conflict of interest and that it was appropriate to request advice and direction from the court.

[13] Thirdly, one must examine the duties of a trustee. As noted by the Trustee in its factum, a trustee is an officer of the court and must act equitably but essentially he represents the interests of the creditors: *Re Roy.*[2] A trustee is under a continuing duty to effect recovery of the assets of the bankrupt: *Re Salloum*[3]. In the normal course, this would extend to recovery of any tax refund. Here recovery would benefit Steel Investments Ltd. but would be to the detriment of CCRA who offset the refund against OSFC's indebtedness. A successful appeal to the Supreme Court would also be to the detriment of the two major creditors as it would leave them exposed to having their claims in OSFC's bankruptcy set aside. A successful appeal would benefit the

[1] [1998] B.C.J No. 837.
[2] [1963] 4 C.B.R. (N.S.) 275.
[3] (1988) 69 C.B.R. (N.S.) 255.

shareholders in that, assuming that the claims of the two major creditors were subsequently set aside, they would be entitled to participate in a distribution of assets after any remaining creditors were paid in full: *Re Thompson Cadillac Mining Corp*.[4]

[14] The role of a shareholder in bankruptcy proceedings is not clearly defined. There are situations where a shareholder of the bankrupt may be permitted to bring a section 37 application for permission to bring an action that a trustee has declined to bring: *Churchill Pulp Mill Ltd. v. Manitoba*.[5] Similarly, a shareholder of a bankrupt company is an "interested person" within the context of a section 119 (2) application to review and revoke decisions and actions of inspectors of the estate: *NSC Corp v. ABN Amro Bank Canada*.[6] The case before me, however, does not engage either of those sections of the *BIA*.

[15] That said, it does seem most inequitable in the circumstances outlined to preclude OSFC from pursuing the requisite motions, and if successful, the appeal. In addition, although the claim is modest, there is at least one creditor, namely Steel Investments Ltd., who might benefit from this course of action. I have concluded that in these circumstances the Trustee should be advised and directed to pursue the proposal presented on the following basis:

> (i) there is to be no charge to the estate of OSFC if any of the motions or the appeal is unsuccessful, and
>
> (ii) before any further proceedings are taken, an indemnity for any adverse costs awards in terms satisfactory to the Trustee is to be provided to the Trustee.

Pepall, J.

**Released:** November 2, 2004

[4] (1943), 24 C.B.R. 274 (S.C.C.).
[5] 24 C.B.R. (N.S.) 116.
[6] (1992) 15 C.B.R. (3d) 301.

**COURT FILE NO.:** 31-395548
**DATE:** 2004-11-02



**ONTARIO**

**SUPERIOR COURT OF JUSTICE**

**B E T W E E N:**

In the Matter of the Bankruptcy of OSFC Holding Limited, A Company Duly Incorporated under the Laws of the Province of Nova Scotia with its Principal Place of Business in the City of Toronto in the Province of Ontario

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**REASONS FOR DECISION**

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**PEPALL J**

**Released:** November 2, 2004

# Court of Queen's Bench of Alberta

**Citation: Re Residential Warranty Company of Canada Inc. (Bankrupt), 2006 ABQB 236**

**Date:** 20060327
**Docket:** 24 112232 and 24 112233
**Registry:** Edmonton



In the Matter of the Bankruptcy of Residential Warranty Company of Canada Inc.
Estate No. 24 112232

and
In the matter of the Bankruptcy of Residential Warranty Insurance Services Ltd.
Estate No. 24 112233

**Corrected judgment:** A corrigendum was issued on April 26, 2006; the corrections have been made to the text and the corrigendum is appended to this judgment.

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**Memorandum of Decision**
**of the**
**Honourable Madam Justice J.E. Topolniski**

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## I. Nature of the Application

[1] This Decision concerns retrospective and prospective funding of a trustee in bankruptcy from assets under administration when all of the assets are subject to a disputed trust claim that is far from being resolved.

[2] Residential Warranty Company of Canada Inc. (RWC) and Residential Warranty Insurance Services Ltd. (RWI) (collectively the Bankrupts) are Alberta companies that operated a home warranty business. They were in the process of winding up when, in late 2004, Deloitte & Touche LLP was appointed their interim receiver (IR) in the context of a minority shareholder's oppression action. On the companies' deemed bankruptcy in May 2005 (Bankruptcies), Deloitte & Touche LLP became their trustee in bankruptcy (Trustee).

[3] The Applicant, Kingsway General Insurance Company (Kingsway), was an insurance underwriter of home warranty policies brokered or administered by the Bankrupts in Alberta and British Columbia. Kingsway filed proofs of claim in the estates pursuant to s. 81 of the

*Bankruptcy and Insolvency Act* (*BIA*)[1] claiming approximately $11,200,000.00 pursuant to contractual, statutory and common law trusts. The Trustee gave notice under s. 81(2) that the trust claim was disputed. It maintains that all or substantially all of the insurance premiums collected by the Bankrupts for insurance policies on which Kingsway is liable have been paid to Kingsway and that the balance of the estate of the Bankrupts is income derived from the operation of their home warranty business. Kingsway has appealed the Trustee's decision (Appeal).

[4] Kingsway's trust claim arises from a series of transactions that are detailed in a broadly drafted Amended Statement of Claim (BC Action) which it filed in the British Columbia Supreme Court in June 2004, prior to the Bankruptcies. The Amended Statement of Claim is comprised of 125 paragraphs over 42 pages and contains allegations of breach of contract, fraud, conversion, breach of trust, breach of fiduciary duty. The Bankrupts, along with certain of their directors, officers, and employees, are named as defendants in the lawsuit.

[5] Kingsway now applies for an order:

1. declaring that the Trustee is not entitled to use the realizations of any assets and property of the Bankrupts for the purpose of paying its fees and expenses, both past and future, pending the hearing of the Appeal and the disposition of the BC Action;

2. directing that the Trustee return all fees paid after notice of its trust claim, subject to deduction for reasonable fees directly attributable to preservation of the alleged trust property;

3. appointing the Trustee as Interim Receiver of the Bankrupts' assets under s. 47.1 of the *BIA* (*BIA* IR) for preservation purposes pending determination of the Appeal and the BC Action; and

4. requiring the Trustee to post security for costs in respect of its defence of the Appeal and the BC Action;

[6] The Trustee's position is that resolution of the Appeal to finally determine the validity of Kingsway's claim is central to administration of the Bankruptcies. The Trustee is concerned about prejudice to other creditors and competing trust claimants if it is unable to respond to the Appeal for lack of funding.

[7] In response to Kingsway's application, the Trustee asks for a retrospective and prospective charge on all of the estate assets under its administration in order to pay its fees and

[1] R.S.C. 1985, c. B-3, as amended and renamed by S.C. 1992, c. 27

disbursements, including legal fees and disbursements. The Canada Revenue Agency (CRA), an unsecured creditor, and a builder, Nucon Developments, support the Trustee's request.

[8] The parties on this application focussed squarely on the issue of Trustee funding. Kingsway did not pursue its request for security for costs and, while mention was made of its request for the appointment of the Trustee as a *BIA* IR in Kingsway's written submissions, no evidence or argument was offered to support the relief requested. In supplemental written submissions, Kingsway argued that 'super-priority' funding for a *BIA* IR under s. 47.2 of the *BIA* is not applicable in a "straight bankruptcy" like this. I took this submission to mean that it had abandoned this arm of its application.



[9] Kingsway has applied for an order transferring the Appeal to the British Columbia Supreme Court (In Bankruptcy) and for an order granting it leave to continue the BC Action "to be heard at the same time as the Appeal, subject to the direction of the Judge of the British Columbia Supreme Court hearing the BC Action". The applications and the Appeal were adjourned at the parties' suggestion. The applications are now set to be heard in mid May. Kingsway wants to await the outcome of its applications before scheduling the Appeal.

[10] As Kingsway's application to have the Court in British Columbia deal with the Appeal has not been decided, my Ruling on the present application presumes that the Appeal will proceed in the ordinary course of events in this Court.

## II. Background

### A. The Bankrupts, the Builders and Kingsway

[11] The Bankrupts brokered and administered residential warranty policies sold in Alberta and British Columbia to builders which were underwritten by Kingsway as the insurer of record. The builders paid for membership in the programs. Each of them also paid money by way of cash deposit or letters of credit as security for repairs covered by the warranty policies. The Bankrupts held the cash deposits in a segregated account. Provided a builder did not owe any money on expiry of the warranty period, the deposit would be repaid to the builder. Letters of credit were treated in a similar fashion.

[12] Relations between Kingsway and the Bankrupts soured to the point where Kingsway terminated its contracts with them in August 2003, alleging that the Bankrupts had sold unauthorized products and had failed to remit certain premiums. The Bankrupts denied the allegations and the fight was on.

[13] In the spring of 2004, Kingsway complained to the British Columbia Financial Institutions Commission (FICOM), British Columbia's insurance regulatory authority, about the Bankrupts' conduct. FICOM investigated the companies and RWI responded by surrendering its

broker's license for three weeks. The Insurance Council of British Columbia subsequently allowed reinstatement of its license on conditions, one of which was that RWI hold approximately $3,100,000.00 in trust with its lawyers for premiums allegedly owed to Kingsway.

[14] Kingsway commenced the BC Action in June 2004, claiming a minimum of $2,108,576.35 plus additional unascertained damages. It started a similar lawsuit in Alberta, but did not prosecute it. About three weeks after the BC Action was commenced, RWC paid $3,092,612.50 to Kingsway, unconditionally.

[15] By the date of the Bankruptcies in May 2005, the defendants to the BC Action had defended and counter-claimed (alleging outstanding commissions, expenses, third party costs, lost income, lost opportunity, and loss of reputation) and Kingsway had demanded document production. Kingsway's forensic accountant apparently calculated the amount that remained owing to Kingsway from the Bankrupts as at June 7, 2005 to be $3,786,606.00. In late June 2005, after receiving certain financial information from the Trustee, Kingsway's forensic accountant determined that $11,292,224.00 (over and above the monies already paid by RWC), plus additional amounts for unliquidated damages, was still owing from the Bankrupts.

[16] Kingsway filed proofs of claim in the Bankruptcies on September 2, 2005 and put the Trustee on notice of its claim and of the position that it was taking with respect to the Trustee's fees and expenses on October 4, 2005.

[17] In late 2005, the police charged the Bankrupts, one of their former directors, and a former employee with fraud, theft, uttering a forged document and drawing a document without authority. An Information was sworn and warrants were held until December 15, 2005. I was not provided with any additional information on this application as to the current status of the criminal proceedings.

**B. The Interim Receiver, The Trustee and Stakeholders**

[18] The order appointing the IR granted the IR a 'super-priority' charge over the companies' assets, giving it priority over all security, charges and encumbrances affecting the assets.

[19] The IR, which is also the Bankrupts' Trustee, complied with the Court's directions to investigate the Bankrupts' affairs, dispose of certain assets and report on numerous concerns, including the BC Action and the builders' deposits. It prepared three reports for the Court. Kingsway contends that the IR's mention of the BC Action in its first report, dated December 21, 2004, constitutes evidence of notice to Deloitte & Touche LLP of Kingsway's trust claim, and that funding for the Trustee from alleged trust assets, which comprise the entire estate of both Bankrupts, should not be allowed after that date. It asserts that funding should not extend beyond October 4, 2005 at the very latest, when its counsel particularized its trust claim and formally put the Trustee on notice of the position which it now advances.

[20] The assets under the Trustee’s administration include bank accounts and claims against various parties, but the vagaries of the Bankrupts’ business and their relationships with others have somewhat complicated the Trustee’s work. Apart from the typical issues arising in any bankruptcy (financial analysis, securing assets, reviewing proofs of claim, reporting to and meeting with creditors and inspectors, and acting as the point person coordinating court matters), the Trustee has instructed litigation and dealt with winding up business operations. It has also addressed enquiries from policyholders and builder claimants about warranties and the refund of deposits relating to 550 properties.

[21] Kingsway has referred some policyholders to the Trustee on denying coverage under various policies and it has jointly instructed some litigation with the Trustee. The Trustee has provided it with financial analyses and other information, including information concerning the Trustee’s findings on premium payments.

[22] The Trustee predicts that its future work will entail continued realization of assets through litigation efforts, including intended litigation against Kingsway to recover $1,500,000.00 in allegedly overdue profit sharing, and resolution of creditor and proprietary claims. In due course, it will wind up the estates, return property rightfully belonging to others, and distribute residual property to the creditors.

[23] There are 627 persons interested in the builders’ deposit fund and letters of credit (Builder Claimants). The builders’ deposit fund is worth approximately $1,000,000.00 while the letters of credit are valued at approximately $5,000,000.00. The Trustee concedes that some of the Builder Claimants have trust claims against the cash builders’ deposits. The method by which builders’ claims are to be proved in the bankruptcy and a claims bar date were set by Order in December 2005. Kingsway has agreed to that process.

[24] Kingsway has participated in case management meetings and applications relating to the claims of the Builder Claimants. It has requested that it be given notice of claims that the Trustee disallows. It also wants to participate in the Trustee’s application for directions as to whether the letters of credit are impressed with a trust and appeals of the disallowance by the Trustee of some builders’ claims. Kingsway maintains that it is entitled to all of the value of the letters of credit, although it has not indicated how these can be considered traceable trust assets. It also claims approximately $300,000.00 of the builders’ cash deposit fund as a result of alleged setoffs owed to it by builders for the cost of repairs. Kingsway takes the position that once the claims of the Builder Claimants who are seeking access to the cash fund have been resolved in these bankruptcy proceedings, the Builder Claimants must “duke it out” with Kingsway in the ordinary courts to determine who is entitled to the funds.

## III. Analysis

## A. Fairness, Practicality and Neutrality

[25] A significant objective of the *BIA* is to ensure that all of the property owned by the bankrupt or in which the bankrupt has a beneficial interest at the date of bankruptcy will, with limited exceptions, vest in the trustee for realization and ratable distribution to creditors. To further this objective, the *BIA* provides for practical, efficient and relatively inexpensive mechanisms for asset recovery, determination of the validity of creditor claims, and distribution of the estate. A fundamental tenet of *BIA* proceedings is that fairness should govern.

[26] The *BIA* expressly preserves the Bankruptcy Court's equitable and ancillary powers.[2] Accordingly, inherent jurisdiction is maintained and available as an important but sparingly used tool. There are two preconditions to the Court exercising its inherent jurisdiction: (1) the *BIA* must be silent on a point or not have dealt with a matter exhaustively; and (2) after balancing competing interests, the benefit of granting the relief must outweigh the relative prejudice to those affected by it. Inherent jurisdiction is available to ensure fairness in the bankruptcy process and fulfilment of the substantive objectives of the *BIA*, including the proper administration and protection of the bankrupt's estate.[3]

[27] Solutions to *BIA* concerns require consideration of the realities of commerce and business efficacy. A strictly legalistic approach is unhelpful in that regard.[4] What is called for is a pragmatic problem-solving approach which is flexible enough to deal with unanticipated problems, often on a case-by-case basis. As astutely noted by Mr. Justice Farley in ***Canada (Minister of Indian Affairs and Northern Development) v. Curragh Inc.***[5]:

> While the *BIA* is generally a very fleshed-out piece of legislation when one compares it to the *CCAA*, it should be observed that s. 47(2)(c): "The court may direct an interim receiver ... to ... (c) take such other action as the court considers advisable" is not in itself a detailed code. It would appear to me that Parliament did not take away any inherent jurisdiction from the court but in fact provided, with these general words, that the court could enlist the services of an interim receiver to do not only what "justice dictates" but also what "practicality demands". It should be recognized that where one is dealing with an insolvency situation one is not dealing with matters which are neatly organised and operating

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[2] s. 183(1)

[3] ***Re Tlustie*** (1923), 3 C.B.R. 654, 23 O.W.N. 622 (S.C.); ***Re Cheerio Toys & Games Ltd.*** [1971] 3 O.R. 721, 15 C.B.R. (N.S.) 77 (H.C.J.); varied [1972] 2 O.R. 845 (C.A.)

[4] ***A. Marquette & Fils Inc. v. Mercure*** , [1977] 1 S.C.R. 547 at 556 (S.C.C.)

[5] (1994), 114 D.L.R. (4th) 176 at 185, 27 C.B.R. (3d) 148 (Ont. Ct. (Gen. Div.))

under predictable discipline. Rather the condition of insolvency usually carries its own internal seeds of chaos, unpredictability and instability.

[28] Neutrality is the necessary mantra of trustees in bankruptcy. They are neither an agent of the creditors nor of the debtor, but rather are administrative officials and officers of the court charged with the responsibility of looking after all parties' interests. Trustees are obliged to comply with the procedures and rules of conduct set out in the *BIA*, the code of ethics in the *BIA General Rules*[6] and with professional codes of conduct, and cannot enter the fray between competing stakeholders.[7] They must present the facts in a dispassionate, non-adversarial manner in matters before the court.[8] Their job is to act as an independent voice of reason and to provide discipline in the oft-chaotic circumstances created on bankruptcy.



## B. Trust Property

[29] Unless otherwise provided by legislation, trustees in bankruptcy have no greater interest in the property they are responsible for administering than the bankrupt does.

[30] The property held by a bankrupt in trust for another is not divisible among the creditors of the bankrupt.[9] However, this does not mean that the res of the trust is not subject to administration by the trustee in bankruptcy. On the contrary, property held by the bankrupt in trust for a third party becomes part of the bankrupt's estate in the possession of the trustee in bankruptcy, who is obliged to administer the property and to deal with it in accordance with the law.[10]

[31] Section 81(2) of the *BIA* governs the actions of a trustee in bankruptcy when presented with a trust claim. Within 15 days of presentation, the trustee in bankruptcy is either to admit the claim or to give notice disputing it, together with the reasons for doing so. There is no intermediate position which may be taken.

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[6] Rules 34-53

[7] ***Re Rassell*** (1999), 177 D.L.R. (4th) 396, 237 A.R. 136, 12 C.B.R. (4th) 316 (C.A.); ***Re Nagy***, [1997] 10 W.W.R. 348, 199 A.R. 146, 45 C.B.R. (3d) 160 (Q.B.); reversed on other grounds [1999] 11 W.W.R. 48, 232 A.R. 399, 13 C.B.R. (4th) 1 (C.A); ***Engles v. Richard Killen & Associates Ltd.*** (2002), 60 O.R. (3rd) 572 at para. 150, 35 C.B.R. (4th) 77(Sup. Ct. Just.)

[8] ***Re Beetown Honey Products Inc***. (2003), 67 O.R. (3d) 511, 46 C.B.R. (4th) 195 (Ont. Sup. Ct. Just.); affirmed (2004), 3 C.B.R. (5th) 204 (Ont. C.A.)

[9] s. 67(1)(a)

[10] ***Ramgotra (Trustee of) v. North American Life Assurance Co.***, [1996] 1 S.C.R. 325, 37 C.B.R. (3d) 141 at para. 61

[32] Section 81(2) reads:

> 81(2) The trustee with whom a proof of claim is filed under subsection (1) shall within fifteen days thereafter or within fifteen days after the first meeting of creditors, whichever is the later, either admit the claim and deliver possession of the property to the claimant or give notice in writing to the claimant that the claim is disputed with his reasons therefor, and, unless the claimant appeals therefrom to the court within fifteen days after the mailing of the notice of dispute, he shall be deemed to have abandoned or relinquished all his right to or interest in the property to the trustee who thereupon may sell or dispose of the property free of any lien, right, title or interest of the claimant.

[33] The Trustee in the present case has performed a quasi-judicial function in assessing and disallowing Kingsway's claim. There is no suggestion that it acted unfairly in doing so or that it has somehow entered into the fray between competing stakeholders. The Trustee has simply done its job.

[34] The Trustee agrees that the Bankrupts had trust obligations to Kingsway for unremitted premiums, but disagrees with Kingsway's assessment that all of the money collected by the Bankrupts from their customers represented premiums. It also questions the merit of Kingsway's constructive trust claim arising from alleged "secret commissions" and breach of fiduciary duty. Tracing will be an issue concerning Kingsway's claim to entitlement to the letters of credit and possibly other aspects of its claim.

[35] The Act is silent about the trustee's responsibilities on an appeal from its rejection of a claim. However, s. 41(4) of the *BIA* provides that an estate is deemed to have been fully administered only when "a trustee's accounts have been approved by the inspectors and taxed by the court and all objections, applications, oppositions, motions and appeals have been settled or disposed of and all dividends have been paid".

[36] In my view, the Trustee is a necessary party to the Appeal, which it is to participate in as an officer of the court, presenting the relevant facts in a dispassionate, non-adversarial manner, leaving the court to decide the matter. The Trustee's responsibility is to ensure that only valid claims to the assets under administration are recognized.

[37] Kingsway has asserted a significant trust claim that might prevail at the end of the day, but at present that claim is merely an assertion - a fact that weighs heavily on this application.

[38] The onus of establishing a trust at the date of bankruptcy will rest with Kingsway and the ordinary law of trust applies in that regard.[11] Kingsway has not yet proved its claim of a valid trust. It has procured an accounting expert's opinion that it relies on, but that opinion is untested. The BC Action was in the early stages when stayed by the Bankruptcies. Other proceedings dealing with the same series of transactions are seemingly over or similarly not far advanced. FICOM's investigation resulted in a three-week licence suspension, but no further action was taken, and the criminal proceeding is in its early stages.

## C. Trustee Funding

[39] In a typical bankruptcy, the trustee is paid from estate assets. Like all insolvency professionals, trustees in bankruptcy are or should be alive to securing payment of their fees, particularly for work in the initial stages of a bankruptcy until the asset base from which they can be paid is assessed. Trustees often look to the petitioning creditor for an indemnity for their fees. Here, the Bankruptcies occurred when proposal deadlines were not met and there is no petitioning creditor. However, other interested parties include the CRA, an unsecured creditor and the Builder Claimants.

[40] Section 39(1) of the *BIA* provides that: "The remuneration of the trustee shall be such as is voted to the trustee by ordinary resolution at any meeting of creditors." However, if remuneration has not been fixed under 39(1), the trustee is entitled under s. 39(2) to insert in his final statement and retain as remuneration, subject to increase or decrease on application to the court, a sum not exceeding seven and one-half per cent of the amount remaining out of the realization of the property of the debtor after the claims of the secured creditors have been paid or satisfied.

[41] Ordinarily, a trustee in bankruptcy will not be funded from trust assets unless it shows that its work was necessary to preserve or otherwise benefit the trust assets,[12] or the work was required for resolution of the trust claim or to sort out beneficiaries.

[42] The first exception developed as a result of the court's exercise of inherent jurisdiction in ordinary trust cases, a topic reviewed in some depth by Sigurdson J. in ***Re Gill*** and Tysoe J. in ***Re***

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[11] s. 81(3); ***Re Kenny*** (1997), 149 D.L.R. (4th) 508, 37 C.B.R. (4th) 291, 1997 CarswellOnt 6031, 34 O.T.C. 321 (Ont. Ct. (Gen. Div.))

[12] ***Re Gill***, (2002) 37 C.B.R. (4th) 257, 2002 BCSC 1401 at para. 23; ***Grant v. Ste. Marie Estate***, (2005) 39 Alta. L.R. (4th) 71, 8 C.B.R. (5th) 81 at paras. 30 and 31, 2005 ABQB 35; ***Re Westar Mining Ltd.*** (1999), 13 C.B.R. (4th) 289, 1999 CarswellBC 2149 (S.C.); ***Re Broome***, (1986) 61 C.B.R. (N.S.) 233 (Ont. S.C.); ***Re CJ Wilkinson Ford Mercury Sales Ltd.*** (1986), 60 C.B.R. (N.S.) 289 (Ont. H.C.J.); ***Re Shirt Man Inc***. (1987), 65 C.B.R. (N.S.) 309, 19 C.C.E.L. 148 (Ont. S.C.); ***Re Genometrics Corp.***, 2005 CarswellSask 790, 2005 SKQB 488; ***Re Frederick McLeod*** (1949), CarswellOnt 88, 29 C.B.R. 163 (S.C.(H.C.J.))

***Eron Mortgage Corp***.[13] The court's inherent jurisdiction in this regard has been exercised sparingly and generally in circumstances where the beneficiary would have had to hire someone else to do the work performed by the trustee.[14] The second exception flows from the trustee in bankruptcy's duty under the *BIA* to approve or disallow of claims.[15]



[43] There is also statutory authority in Alberta which allows for the funding of ordinary trustees. The *Trustee Act*[16] authorizes the court to order compensation for "the trustee's care, pains and trouble and the trustee's time expended in and about the trust estate". This compensation is available regardless of whether the trusteeship arises by construction, implication of law, or express trust.[17] Trustees in bankruptcy can avail themselves of this legislation to the extent that it is not in conflict with the *BIA*.[18]

[44] The Alberta Court of Appeal in ***Re Sproule Estate***[19] considered the intent and scope of s. 44 funding (then s. 39). Mr. Justice Haddad commented that:[20]

> My concept of the term care and management is consistent with the expressions to which I have referred. It connotes to me not only the responsibility of reasonable supervision and vigilance over the preservation or disposition of assets but also

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[13] (1998), 53 B.C.L.R. (3d) 24, 2 C.B.R. (4th) 184 (S.C.)

[14] ***Re Eron Mortgage Corp.***, footnote 14; ***Harris v. Conway***, [1989] 1 Ch. D. 32, [1989] B.C.L.C. 28, [1988] 3 All E.R. 71 (Eng. H.C.); ***Ontario (Securities Commission) v. Consortium Construction Inc.*** (1992), 9 O.R. (3d) 385, 14 C.B.R. (3d) 6 (C.A.); ***Ontario (Registrar of Mortgage Brokers) v. Matrix Financial Corp.*** (1993), 106 D.L.R. (4th) 132 (Ont. C.A.)

[15] ***Re Ridout Real Estate Ltd***. (1957), 36 C.B.R. 111 (Ont. H.C.J.); ***Re NRS Rosewood Real Estate Ltd***., (1992) 9 C.B.R. (3rd) 163 (Ont. Ct. (Gen. Div.)); ***Re Nakashidze (No. 2)***, [1948] O.R. 254, 29 C.B.R. 35 (H.C.J.); ***Re Walter Davidson Ltd***. (1957), 10 D.L.R. (2d) 77, 36 C.B.R. 65 (Ont. H.C.J.)

[16] R.S.A. 2000, c. T-8, s. 44. The Act expressly permits charging of trust assets for the fees of judicial trustees, but otherwise is silent.

[17] *Trustee Act*, footnote 16, s. 1(b)

[18] *BIA*, footnote 1, s. 72(1); see also the discussion concerning operational conflict in ***Multiple Access Ltd. v. McCutcheon***, [1982] 2 S.C.R. 161 at 190: "[T]here is no true repugnancy in the case of merely duplicative provisions since it does not matter which statute is applied; the legislative purpose of Parliament will be fulfilled regardless of which statute is invoked by a remedy-seeker; application of the provincial law does not displace the legislative purpose of Parliament." In my view, the overarching principle to be derived from ***Multiple Access Ltd.*** and later cases is that a provincial enactment must not frustrate the purpose of a federal enactment, whether by making it impossible to comply with the latter or by some other means. Impossibility of dual compliance is sufficient but not the only test for inconsistency.

[19] (1979) 95 D.L.R. (3d) 458, 13 A.R. 420 (C.A.)

[20] ***Re Sproule Estate***, footnote 20, para. 11

> the responsibility of judgment and decision making in the affairs of an estate to resolve problems from time to time arising over and above the usual and regular procedures attendant upon administration.



[45] The Trustee in the present case was obliged to gather in trust property, which vested in the Trustee, but it cannot distribute the res of the trust to creditors. The Trustee therefore has two capacities, one as trustee in bankruptcy and the other as an ordinary trustee arising by implication of law. If Kingsway prevails at the end of the day, the Trustee is entitled to seek compensation for its work "in and about the trust". In my view, the broad scope of compensable work discussed by Mr. Justice Haddad in ***Sproule*** includes identifying which assets, if any, are subject to a trust and, if doubt exists, placing the necessary information before the court for determination of that issue.

[46] There are several notable cases in which trustees in bankruptcy have been denied or given only limited funding from trust assets. ***Re Broome***, ***Re Shirt Man Inc.*** and ***Re Genometrics Corp.*** involved assets impressed with undisputed statutory trusts for employee withholdings. In ***Broome***, as here, the trust claims were to the entirety of the funds gathering in by the trustee.

[47] ***Broome*** concerned employee tax withholdings. Master Bowne described his ruling as:[21]

> …A signal to trustees that where there are trust claims, before undertaking work with a view to realization of assets to benefit trust fund recipients, the trustee would be advised to make arrangements that remunerations would be paid by the administrator of the trust or otherwise.

[48] Master Browne said in *obiter dicta* that even if the funds in the estate exceeded the amount of the trust claims, the expenses and fees which the trustee would be entitled to claim from the estate assets under s. 107 (now s. 136) of the *BIA* would not include indemnity for any work done which did not result in a benefit to the creditors. This aspect of the decision was qualified in ***Re Pugsley***,[22] an appeal of a registrar's taxing order which disallowed legal fees incurred by the trustee in obtaining an opinion on the validity of a trust claim asserted by Revenue Canada under s. 59 of the *Bankruptcy Act*, R.S.C. 1970, c. B-3 (now s. 81 of the *BIA*). Mr. Justice O'Driscoll in that case held that the comment of Master Browne in ***Broome*** should not be extended or expanded to include the assessed costs of legal counsel retained by the trustee to provide such legal services. He did not consider it logical that a trustee would be entitled to pay counsel for the opinion if in the end the proof of claim was adjudged invalid, but not if the claim was upheld, even though technically there was no benefit to the creditors in obtaining the opinion.

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[21] ***Re Broome***, footnote 12, pp. 236 tp 237

[22] (1988), 63 O.R. (2d) 635, 67 C.B.R. (N.S.) 98 (S.C.)

[49] The debtor in ***Re CJ Wilkinson Ford Mercury Sales Ltd.***[23] sought a charge over statutory trust assets, again employee withholdings, to fund his legal counsel. The court denied the application, commenting that it would not allow money owned by one person to be paid over to another person so that he could pay it to yet another person.

[50] ***Grant v. Ste. Marie Estate***[24] involved a summary trial in the ordinary courts, a bankrupt rogue, a finding of a valid express trust and competing claimants. The plaintiff was granted leave to proceed with his lawsuit against the bankrupt. The issue was whether the plaintiff, a victim of the bankrupt defendant's fraud, could trace funds that he had paid to the bankrupt into the hands of the trustee in bankruptcy.

[51] Mr. Justice Slatter found that the bankrupt had used words of trust to reassure the plaintiff. He ruled that the trustee's investigative work was instrumental in precluding improper payouts to others and thereby benefited the plaintiff. Likening the trustee to a *bona fide* purchaser for value without notice, he allowed encroachment on the trust property to pay certain expenses to the extent they related to the trustee's dealings with the traced funds, but only to the date the trustee received notice of the trust claim.

[52] Slatter J. noted that the trustee's fees and expenses relating to general administration of the estate were a legitimate expense of the estate. Where trust funds are used to discharge a debt owed to the recipient of the funds, there is a giving of value and no tracing to the recipient is permitted.[25] Therefore, he reasoned that the trustee's payment of legal expenses and even its own fees prior to receiving notice of the trust precluded the trust claimant from tracing those funds and defeated the beneficiary's interest to that extent. He commented[26] that:

> ... the Trustee is an officer of the Court, and a necessary part of the bankruptcy regime, and the discharge of the estate's obligation to pay the Trustee should also be considered as the giving of value. Before receiving notice of the Plaintiff's claim the Trustee was a bona fide purchaser for value without notice, and the Plaintiff cannot recover the portion of funds used to discharge the legitimate expenses of the estate.

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[23] footnote 12

[24] footnote 12

[25] D.M. Paciocco, "The Remedial Constructive Trust: A Principled Basis for Priorities Over Creditors" (1989), 68 Can. Bar Rev. 315 at 321

[26] footnote 12 at para. 31

[53] ***Re Westar Mining Ltd.***[27] addressed the issue from the opposite perspective. A group of trust claimants sought funding from estate assets to pay legal fees for their application to exclude certain assets from distribution to the creditors. The court held that the legal work did not benefit the bankrupt's estate nor was it necessary for the management and preservation of estate assets. The court was unmoved by the claimants' plea that it would be unfair to them to have to retain counsel when counsel for the trustee, who was paid for by the estate, represented the other creditors.

[54] The court in ***Re Ridout Real Estate Ltd.***[28] charged trust funds that ultimately were held to belong to realty vendors and purchasers, brokers and salespersons with payment of the fees of a trustee in bankruptcy. The only mention of the trustee's work in connection to the trust assets was that he received a deposit and brought an application for directions concerning distribution of the assets. Presumably, this was sufficient to warrant compensation. The case report refers only to trust funds in the trustee's hands. There is no mention made as to whether there were any residual assets in the bankrupt's estate.

[55] In ***Re NRS Rosewood Real Estate Ltd.***,[29]the court awarded the trustee in bankruptcy $25,000.00 in compensation from trust monies as it was satisfied that issues between the stakeholders had to be resolved by the court and it was the trustee's initiative which had caused that to happen. Apparently, there were some residual assets in that case.

[56] Mr. Justice Urquhart in ***Re Nakashidze (No. 2)***[30] allowed the trustee compensation from securities that were not property of the bankrupt, noting that the trustee had undertaken a vast amount of work in sorting out and assembling the securities and claims. However, he reached a contrary conclusion in ***Re Frederick McLeod***,[31] finding that the trustee in bankruptcy was not entitled to compensation from proprietary assets because the proprietary claimant rather than the trustee had "salvaged" the asset. Nevertheless, he did indicate that any work undertaken by the trustee could be taken into account when the estate was wound up in fixing his general compensation.

[57] ***Re Walter Davidson Ltd.***[32] involved a dispute between a secured creditor claiming under a general assignment of book debts, mechanics' lien claimants and unsecured creditors. The court ultimately ruled in favour of the statutory lien claimants, but held that it was the trustee in

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[27] footnote 12

[28] footnote 15

[29] footnote 15

[30] footnote 15

[31] footnote 12

[32] footnote 15

bankruptcy's efforts which had made the money available to the lien claimants and therefore charged the trust assets with payment of the trustee's fees.

[58] Like Kingsway, the miners' lien claimants in ***Canada (Minister of Indian Affairs and Northern Development) v. Curragh Inc.***[33] protested funding of the insolvency professional. Funding in that case was pursuant to a 'super priority' charge granted under s. 47.2 of the *BIA*. In refusing the claimants' application, Mr. Justice Farley described the interim receiver's work as "providing discipline to the proceedings" and noted that the interim receiver had to be capable of exercising its own independent judgment. He commented as follows on the status of the applicants' claims in ***Canada (Minister of Indian Affairs and Northern Development) v. Curragh Inc.***:[34]

> …Secondly, it would seem to me that one should not presume what one is hopeful of establishing (i.e. the MLA claimants have not yet proved the validity and priority of their liens). Thirdly, while it should be recognized that the IR may be funded, there is no assurance that it will "win"; it may "lose" in whole or in part. However, at least there will be the testing of the Royalty Claim for the benefit of all creditors who have a valid claim against ***Curragh***…
>
> ... Simply put, it comes down to a question of cutting through the Gordian Knot: one does not know at this stage whether these opposing MLA claimants have a valid and prior claim. It seems to me that the amount of funding is reasonable in the circumstances and would be modest investment in the process.

[59] The trustee is an integral part of the bankruptcy system. The claims review process is designed to ensure that only proper claimants are entitled to share in the bankrupt's property. The Trustee, at least in this case, is a necessary party to the Appeal. Kingsway should succeed only if it has a legitimate claim and not simply by default. To rule otherwise would be to open the door for possible abuse of the system by rogue claimants filing spurious proprietary claims.

[60] If a charge is granted, Kingsway ultimately may be prejudiced if it proves its claim to the extent asserted, but that prospect remains an "if". The sheer magnitude of its claim is no reason to hold the Trustee and the bankruptcy system at bay pending determination of its validity. Mr. Justice Farley's words in ***Curragh*** resonate … "one should not presume what one is hopeful of establishing".[35]

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[33] [1994] O.J. No. 1917 (Ont. Ct. (Gen. Div.)) (QL)

[34] 1994 CarswellOnt 3853 at paras. 8 and 9 (Ont. Ct. (Gen. Div.))

[35] footnote 34 at para. 8

## D. Charge on the Assets

[61] Kingsway contends that an asserted trust claim valued at more than potential realizations, regardless of its facial merit, forces the trustee in bankruptcy to seek funding for an appeal of its disallowance of the claim from sources other than the assets under administration. It contends that responsibility to fund the Trustee falls on the shoulders of other creditors or claimants, whether by means of direct funding or an assignment under s. 38 of the *BIA*. Given the nature of the claims in these Bankruptcies, I disagree. The validity and priority of the trust claims must be determined. The Trustee is assisting the Court and all of the claimants in coordinating these matters and in providing the necessary information to resolve these issues.

[62] The Trustee is not asking for a retrospective charge over undisputed statutory employee withholdings, as were the (unsuccessful applicant) trustees in bankruptcy in ***Broome***, ***Shirt Man*** and ***Genometrics***. Nor is the Trustee seeking a prospective charge over undisputed statutory employee withholdings like the bankrupt in ***C.J. Wilkinson Ford Mercury Sales***.

[63] Mr. Justice Slatter held in ***Grant*** that the trustee in that case could not use the trust funds after receiving notice of the proprietary plaintiff's claim. It is unclear what position the trustee in that case took concerning the trust claim (offering financial and documentary information to the court does not equate to disputing the claim), what work, if any, it undertook after notice of the trust claim, and whether there were residual assets from which it could be funded. This is not surprising given that the case was not about trustee compensation or the charging of trust assets.

[64] The role of the Trustee here is more akin to that of the trustees described in ***Ridout Real Estate***, ***NRS Rosewood***, ***Nakashidze (No.2)***, ***Walter Davidson Ltd.***, and ***Frederick McLeod***, each of whom was successful in obtaining a retroactive charge over established trust assets for their work in gathering and preserving trust assets or in sorting out the trust claims.

[65] In ***Pugsley***, Mr. Justice O'Driscoll commented that a trustee should be able to pay counsel for their opinion and services in regard to a proof of claim whether the claim eventually is adjudged invalid or not. He reasoned that if the trustee cannot hire and remunerate counsel to process the claims, counsel to a trustee might refuse to do so because of the potential for non-remuneration. In his view, that would put the trustee in a "no win" situation with regard to legal advice and legal services regarding proofs of claim.

[66] ***Sproule*** is also responsive to the "no win" situation identified by Mr. Justice O'Driscoll in ***Pugsley***.

[67] Common sense dictates that trustees in bankruptcy should receive reasonable compensation when they are called on to exercise their judgment and to be real problem solvers in a situation such as the present one. If it were otherwise, trustees would be inclined to shy away from problems and the list of persons willing to take on the role of trustee would dwindle, particularly in situations where there was no personal connection between the potential trustee and the beneficiary or the assets under administration.

### 1. Retrospective Charge

[68] Kingsway's application is denied. The Trustee is entitled to a charge on the assets under administration for its fees and expenses in undertaking work on the estate to date. Presuming success for Kingsway in the end, a significant part of the Trustee's work will have benefited Kingsway, given that its claim is to all of the assets under administration. Furthermore, the Trustee is entitled to compensation for all of its work to date in sorting out Kingsway's claim. The Trustee has offered its assistance to Kingsway in related proceedings concerning proposals made by various directors and officers of the Bankrupts, it has formulated a plan that Kingsway has joined in for resolving claims by Builder Claimants, it has coordinated and attended case management meetings, and it has argued a preliminary arm of Kingsway's jurisdictional application.

[69] I have taken Kingsway's choices regarding process into consideration in determining whether it is appropriate to grant the Trustee a retrospective charge on the contested assets for its fees and disbursements. Kingsway has chosen to make a preliminary application to move the Appeal to British Columbia. It wants to continue the BC Action. While it is entitled to bring these applications, it cannot ignore the logical consequences of doing so. These applications, and others which it has brought in parallel proceedings relating to the proposals made by various officers and directors of the Bankrupts, have and will continue to delay the ultimate decision about the validity of Kingsway's trust claim. Kingsway wants to take advantage of the bankruptcy proceedings to have this Court determine the validity of the claims of the Builder Claimants and whether the letters of credit are impressed by a trust, but to force builders with trust claims against which it alleges a right of setoff to "duke it out" in the ordinary courts. Finally, I observe that Kingsway did not seek an expedited hearing for this or its other applications.

[70] Kingsway's application to stop the Trustee from using assets under its administration to pay its fees and expenses is denied and the Trustee is granted a retrospective charge over the assets under its administration for all of its reasonable fees and disbursements, including legal expenses, concerning the gathering in and preserving of assets in the estate and the general administration of the Bankruptcies, such as investigating Kingsway's trust claim. The charge is granted no matter what the outcome is of the Appeal.

[71] If an appeal court decides that the retrospective charge should be restricted to fees and expenses relating to work undertaken before the Trustee had notice of Kingsway's claim, as in ***Grant***, I offer my finding that reasonable notice did not occur until November 25, 2005. The reasons for my finding in this regard are:

1. The Trustee's work in its capacity as IR was at the Court's behest. Like the insolvency professional in ***Ontario (Registrar of Mortgage Brokers) v.***

***Matrix Financial Corp.***,[36] it is entitled to payment from trust assets for all work done prior to the Bankruptcies.

2. The Trustee, as IR, indicated in its reports to the Court between December 2004 and May 2005 that:

   (i) the BC Action existed;

   (ii) it had a concern about Kingsway's calculation of premiums owing;

   (iii) it was premature to opine on the merits of the BC Action, but once that could be done, a decision would be taken to settle, vigorously defend or purse damages by counter-claim.

3. The allegation of breach of trust in the BC Action is just one of many claims in a broadly cast pleading. The filing of pleadings in a civil action does not mean that the plaintiff will pursue its claim in a bankruptcy.

4. It was not until October 4, 2005 that Kingsway's counsel particularized its trust claim and formally put the Trustee on notice of the position which it now asserts.

5. Kingsway's Notice of Motion was filed November 25, 2005. That is the date on which the clock should run.

**2. Prospective Charge**

[72] ***Gill*** is the only reported bankruptcy case that specifically addresses prospective charges over trust assets. As might be expected, the decision there turned on the unique facts of the case. There were allegations that the bankrupt had been involved in a scheme to hide his interest in certain properties by having them registered in the names of others. The trustee filed 350 caveats to preserve the interests of creditors and potential proprietary claimants. Information about the extent of the trust property and the claimants was uncertain at the date of the application. The trustee sought a retrospective and prospective charge over the yet unascertained trust assets.

[73] Mr. Justice Sigurdson found that the application for a prospective charge was premature, but granted leave to the trustee to reapply on evidence of creditor prejudice. He noted that the trustee's request would ripen when valid trust claims were established and sale proceeds were ready for distribution. He was concerned that affected parties should have notice of the

[36] footnote 14

application, an impossibility at the time of the application given that the trustee did not know who they were.

[74] The facts in ***Gill*** are distinguishable from those in the present case. Unlike the situation in ***Gill***, the Trustee's application here is not wholly premature. It is clear that Kingsway and the Builder Claimants advance trust claims. The value of Kingsway's claim is established. Values of the assets under administration are known, subject to some further collection efforts and potential litigation recoveries from actions against Kingsway. The trust claims have not been substantiated at present. That alone is not sufficient reason to defer the Trustee's application.

[75] ***Eron Mortgage*** was followed in ***Gill*** and therefore merits brief discussion, although the facts in that case also are distinguishable. ***Eron Mortgage*** involved the judicial trusteeship of an insolvent company. A court sanctioned lenders' committee sought a charge over (what appear to be undisputed) trust assets to secure past and future payment of expenses and remuneration. Mr. Justice Tysoe concluded that he could exercise inherent jurisdiction to order the charge, but declined to do so, although he gave leave to the committee to reapply. His rationale for declining the charge was that the evidence was unclear about certain committee functions. He considered that it was premature to say what future efforts, if any, would benefit the trust assets.

[76] In my view, it is clear in the present case that resolution of Kingsway's claim will benefit the trust claimant if it succeeds. Similarly, the creditors are entitled to have Kingsway's claim tested, presuming the Inspectors agree to the Trustee's involvement in the Appeal.

[77] The Trustee's request, however, is not just for a charge over potential trust assets in relation to the Appeal, but for a charge in relation to furthering the general administration of the Bankruptcies, including the Appeal. I understand that the Trustee intends to seek a charge over the assets at issue in the Builder Claimants' matter. However, even excluding that work, the proposed charge encompasses more than the case law presently authorizes for sorting out claims and preserving trust assets. It is a request for a general "super priority" funding order like that available to *BIA* interim receivers under s. 47.2, to judicial receivers, and to debtors in *Companies' Creditors Arrangement Act*[37] proceedings for financing a restructuring (DIP or priming liens).

[78] Except in the context of commercial restructuring cases under the *BIA*,[38] caution must be exercised when considering developments concerning inherent jurisdiction emanating from the *CCAA*. The *BIA* and *CCAA* are very different in degree of specificity and the policy considerations involved. For example, courts in *CCAA* proceedings routinely rationalize financing for commercial restructuring that compromises creditors' traditional interests in the

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[37] R.S.C. 1985, c. C-36

[38] ***Fiber Connections Inc. v. SVCM Capital Ltd***. (2005), 10 C.B.R. (5th) 192, 5 B.L.R. (4th) 271, 2005 CarswellOnt 1963 (Sup. Ct. Just.), leave to appeal to Ont. C.A. granted (2005) 10 C.B.R. (5th) 201.

name of the greater good. There is an overarching policy concern favouring the possibility of a going concern solution and the potential of a long-term upside value for a broad constituency of stakeholders.[39] Arguably, in some cases, super-priority financing and priming charges must be available if restructuring is to be a possibility.



[79] Here, the policy consideration is not to facilitate a potential business survival, but rather to maintain the integrity of the bankruptcy system and to be fair, while recognizing established trusts law.

[80] According to the court in ***Robert F. Kowal Investments Ltd. v. Deeder Electric Ltd***,[40] "super priority" funding for judicial receivers ordinarily is limited to circumstances where either:

1. The receiver's appointment is at the request of or with the consent or approval of the holders of security.

2. The receiver's appointment is to preserve and realize assets for the benefit of all interested parties, including secured creditors.

3. The receiver has expended money for the necessary preservation or improvement of the property.

[81] In my view, a prospective charge can be fashioned which will respect these limitations. Since the assets under administration are bank accounts and chose in action, the Trustee's work for general estate administration can be restricted to matters of some urgency. If the Appeal is dealt with in a timely fashion, significant hardship to the creditors can be avoided and Kingsway can be offered some assurance deductions from the assets over which it is claiming a trust will be minimized. I appreciate, however, that some litigation may be time sensitive. Therefore, the Trustee is granted leave to revisit this restriction on evidence of prejudice to the creditors by delaying litigation.

[82] A prospective charge will be granted on the Trustee filing a report with the Court confirming that the Inspectors in these Bankruptcies have approved the actions which the Trustee proposes to take, including its involvement in the Appeal and all of the preliminary applications filed by Kingsway that may be heard prior to the Appeal. On the filing of that report, the prospective charge will cover the preliminary applications, the Appeal *per se*, and all steps to readying the Appeal for hearing, whether it is a "paper Appeal" or a directed trial of an issue.

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[39] ***Re Royal Oak Mines Inc.*** (1999), 6 C.B.R. (4th) 314 (Ont. Ct. (Gen. Div.)); David B. Light, "Involuntary Subordination of Security Interests to Charges for DIP Financing under the *Companies' Creditors Arrangement Act*," (2005) 30 C.B.R. (4th) 245.

[40] (1975), 21 C.B.R. (N.S.) 201 at 205-206 (Ont. C.A.)

Conservative measures for asset maintenance and preservation also are covered by this prospective charge. However, the Trustee may not pursue new asset realization without leave of the Court or Kingsway's consent.



[83] The Appeal will proceed on an expedited basis after the hearing of Kingsway's preliminary jurisdictional applications. Any application to have the Appeal dealt with by way of a trial of an issue is to be filed within 14 days of these Reasons and made returnable on May 12, 2006. If there is no such application, a case management meeting will be held May 12, 2006 for the purpose of setting deadlines for the exchange of affidavits, cross-examinations on affidavit and the filing of written submissions.

[84] If, as a result of the Appeal, Kingsway establishes a recoverable trust of the magnitude claimed, it will have suffered a loss by virtue of the charge. Nevertheless, that loss will have been incurred, broadly speaking, to benefit the trust in realizing assets and to determine entitlements. If it is held that all of the assets under administration are not impressed with the trust claimed by Kingsway, a hearing is to be held in order to determine out of which funds (i.e. any trust monies owing to Kingsway, any trust monies owing to the Builder Claimants or other parties with a proven trust claim, and the monies to be distributed to creditors), and in what proportion the Trustees' fees and expenses (once approved) are to be taken.

### 3. Builder Claimants

[85] The retrospective and prospective charges which I have granted have the potential to affect the Builder Claimants if they are successful at the end of the day in establishing entitlement to some of the assets under administration. There is no evidence that the Builder Claimants have been given notice of this application. Accordingly, I direct that the Trustee serve the Builder Claimants with notice of my decision. The charges which I am granting will not take effect on any monies claimed by the Builder Claimants until 14 days after the Trustee has filed proof with the Court of service of these Reasons on all of the Builder Claimants. Prior to that time, the Builder Claimants may challenge the charges which I am granting the Trustee over that portion of the assets to which they claim an interest.

### 4. Costs

[86] Costs of this application will be determined following the Appeal. If the Appeal does not proceed for some reason, the parties may return on notice to settle the issue of costs.

**Dated** at the City of Edmonton, Alberta this 24th day of March, 2006.

**J.E. Topolniski**
**J.C.Q.B.A.**

**Appearances:**

Brian Rhodes
Dolden Wallace Folick

John I. McLean
Davis and Company
for Kingsway General Insurance Company

Kent Rowan
Ogilvie LLP
for Deloitte & Touche Inc.

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**Corrigendum of the Memorandum of Decision**
**of**
**The Honourable Madam Justice J.E. Topolniski**

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The third sentence in paragraph 23 was changed from: “Both Kingsway and the Trustee concede that many of the Builder Claimants have trust claims against the cash builders’ deposits.” to read: “The trustee concedes that some of the Builder Claimants have trust claims against the cash builders’ deposits.”

The date May 12, 2005 in lines 3 and 4 in paragraph 83 have been changed to May 12, 2006.

# In the Court of Appeal of Alberta

**Citation: Kingsway General Insurance Company v. Residential Warranty Company of Canada Inc. (Trustee of), 2006 ABCA 293**

**Date:** 20061010
**Docket:** 0603-0093-AC
**Registry:** Edmonton



**Between:**

**Kingsway General Insurance Company**

Appellant
(Applicant)

\- and -

**Deloitte & Touche Inc., Trustee In Bankruptcy of Residential Warranty Company of Canada Inc. and Residential Warranty Insurance Services Ltd.**

Respondent

**Corrected judgment:** A corrigendum was issued on October 18, 2006; the corrections have been made to the text and the corrigendum is appended to this judgment.

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**The Court:**

**The Honourable Mr. Justice Jean Côté**
**The Honourable Madam Justice Marina Paperny**
**The Honourable Madam Justice Doreen Sulyma**

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**Reasons for Judgment Reserved of The Honourable Madam Justice Paperny**
**Concurred in by The Honourable Mr. Justice Côté**
**Concurred in by The Honourable Madam Justice Sulyma**

Appeal from the Decision of
The Honourable Madam Justice J. E. Topolniski
Dated the 24th day of March, 2006
(24 112232; 24 112233)

**Reasons for Judgment of**
**The Honourable Madam Justice Paperny**



## Introduction

[1] This is an appeal from a case management judge, sitting in bankruptcy, granting a charge for trustee's fees against property subject to conflicting, undetermined trust claims.

## Background

[2] The bankruptcy judge reviewed the facts in her reasons: (2006), 21 C.B.R. (5th) 57, 2006 ABQB 236. The following is a summary.

[3] Residential Warranty Company of Canada ("RWC") and Residential Warranty Insurance Services ("RWI") operated a home warranty business in Alberta and British Columbia. The appellant Kingsway General Insurance ("Kingsway") underwrote warranty policies sold by RWI and RWC.

[4] RWI collected insurance premiums on behalf of Kingsway pursuant to a broker agreement. RWC and RWI also received funds from home builders by way of fees for membership in the warranty programs and by way of cash deposits or letters of credit as security for repairs covered by the warranty policies.

[5] RWC and RWI became bankrupt on May 31, 2005. The respondent, Deloitte & Touche, is the trustee in bankruptcy of their estates.

[6] Kingsway filed proofs of claim pursuant to s. 81 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*") asserting that all property in the bankrupt estates is subject to a trust in Kingsway's favour. Unsecured creditors, Canada Revenue Agency and other competing trust claimants (home builders) also claim interests in the property.

[7] Kingsway claims that the entirety of the bankrupts' estates is comprised of premiums which the bankrupts collected on its behalf and therefore is impressed with a trust under the *Insurance Act*, R.S.A. 2000, c. I-3 and corresponding legislation in British Columbia. Section 504 (formerly 124) of the Alberta statute provides that an insurance agent who acts for an insurer in negotiating, renewing or continuing a contract of insurance and who receives insurance premiums from an insured, is deemed to hold the premiums in trust for the insurer. Kingsway submits that these premiums cannot be subject to the charge granted because as trust funds they do not form part of the bankrupts' estates. Kingsway also asserts an express trust by virtue of the broker agreement and a constructive or resulting trust. The broker agreement between Kingsway and RWI provides that "[a]ll money received by the Broker [RWI] on behalf of the Company [Kingsway] less the Broker commission shall be the property of the Company and shall be held...as Trust Funds...".

[8] The trustee disallowed Kingsway's trust claim and notified Kingsway pursuant to s. 81(2) of the *BIA*. The trustee's review of the records indicated to it that all premiums owing had been paid

to Kingsway and that the funds in the estate represent other income from the operation of the business.

[9] Kingsway appealed the trustee's decision to the Court of Queen's Bench, a summary proceeding under s. 81(2) of the *BIA*. That appeal is pending.

[10] Kingsway applied to the bankruptcy judge seeking that Deloitte & Touche be prohibited from accessing any property in the estates for any purpose, including paying its past and future fees and expenses for appearing on the appeal and otherwise, pending the determination of Kingsway's trust claim.

[11] The trustee opposed Kingsway's application and sought a retrospective and prospective charge against all assets under its administration.

[12] The trustee has been administering the estates of RWC and RWI in accordance with the *BIA*, including: conducting financial analysis; securing and retaining possession of property of RWC and RWI; communicating with Kingsway and builders who are also advancing trust claims; establishing and executing a process to deal with builder claims to cash security deposits held by RWC and RWI; communicating with home owners claiming insurance coverage pursuant to policies issued by Kingsway; and administering insurance claims on a limited basis.

[13] The trustee anticipates future costs arising from dealing with the validity and priority of the trust claims of Kingsway and various builders.

[14] The trustee asserts that because Kingsway's trust claims encompass the entirety of the property under the trustee's administration, the ultimate determination of Kingsway's claim is critical to the administration of these bankruptcies. The trustee is concerned about prejudice to other creditors and competing trust claimants if it is unable to respond to Kingsway's appeal of the disallowance due to lack of funding.

**Decision Below**

[15] The case management judge denied Kingsway's application and granted the trustee's application for a retrospective charge. She also granted the trustee's application for a prospective charge, subject to the trustee filing an interim report with the court confirming the inspectors approved the actions proposed by the trustee, including its involvement in the proceedings to determine Kingsway's trust claim. She stipulated that both the retrospective and prospective charges were subject to challenge by builders with trust claims who had not been given notice of the applications before her. She further ordered the trustee to minimize general estate administration, not to pursue further asset realization without Kingsway's consent or the court's approval, and that Kingsway's appeal from the trustee's disallowance proceed on an expedited basis.

**Issues on Appeal**

[16] This appeal raises the following issues:

> 1. Does a bankruptcy judge have jurisdiction to order that a trustee's fees be paid from property that is subject to undetermined trust

claims?

2. If so, does that jurisdiction include the trustee's fees associated with determination of a trust claim?

3. If jurisdiction exists, what factors should a court consider in exercising its discretion to make such orders?

4. If jurisdiction exists, did the case management judge properly exercise the discretion?

**Standard of Review**

[17] The first three issues raise a question of law, subject to the standard of correctness: ***Murphy Oil Co. v. Predator Corp.*** (2005), 384 A.R. 251, 2006 ABCA 69. The fourth issue involves the exercise of discretion of a case management justice and cannot be interfered with in the absence of a palpable or overriding error: ***Northstone Power Corp. v. R.J.K. Power Systems Ltd.*** (2002), 36 C.B.R. (4th) 272, 2002 ABCA 201.

**Discussion**

**1. Jurisdiction to order trustee's fees be paid from property subject to undetermined trust claims**

[18] The *BIA* does not address the ability of a trustee to obtain a charge for its fees on property that is subject to undetermined trust claims. The trustee submits that the jurisdiction to do so is found in the inherent jurisdiction of the bankruptcy court.

[19] Section 183(1) of the *BIA* preserves the inherent jurisdiction of the Court of Queen's Bench of Alberta sitting in bankruptcy, stating in part:

> 183. (1) The following courts are invested with such jurisdiction at law and in equity as will enable them to exercise original, auxiliary and ancilliary jurisdiction in bankruptcy and in other proceedings authorized by this Act during their respective terms, as they are now, or may be hereafter, held, and in vacation and in chambers:
> ...
>
> (d) in the Provinces of New Brunswick and Alberta, the Court of Queen's Bench;...

[20] Inherent jurisdiction is not without limits, however. It cannot be used to negate the unambiguous expression of legislative will and moreover, because it is a special and extraordinary power, should be exercised only sparingly and in a clear case: ***Baxter Student Housing Ltd. v. College Housing Cooperative Ltd.***, [1976] 2 S.C.R. 475 at 480; ***Wasserman Arsenault Ltd. v. Sone*** (2002), 33 C.B.R. (4th)145 (Ont. C.A.). In ***Wasserman***, the trustee applied for an increase in fees in a summary administration bankruptcy. Rule 128 of the *BIA* Rules caps the trustee's fees in summary administration bankruptcies with no permissive or discretionary language. The Ontario

Court of Appeal concluded that inherent jurisdiction could not be used to conflict with that legislative expression.

[21] Further limitations are based on the nature of the *BIA* - it is a detailed and specific statute providing a comprehensive scheme aimed at ensuring the certainty of equitable distribution of a bankrupt's assets among creditors. In this context, there should not be frequent resort to the power. However, inherent jurisdiction has been used where it is necessary to promote the objects of the *BIA*: ***Re Tlustie*** (1923), 3 C.B.R. 654; ***Canada (Minister of Indian Affairs and Northern Development) v. Curragh Inc.*** (1994), 27 C.B.R. (3d) 148 (Ont. S.C.). It has also been used where there is no other alternative available: ***Re Olympia & York Developments Ltd.*** (1997), 18 C.B.R. (4th) 243 (Ont. Gen.Div.); ***Re City Construction Company Ltd.*** (1961), 2 C.B.R. (N.S.) 245 (B.C.C.A.) and to accomplish what justice and practicality require: ***Canada v. Curragh***.

[22] Kingsway asserts that s. 67(1) of the *BIA* prohibits such a charge. That section states:

> 67. (1) The property of a bankrupt divisible among his creditors shall not comprise
> (a) property held by the bankrupt in trust for any other person...

[23] Kingsway relies on s. 67 to assert that property held by a bankrupt in trust for others does not form part of the estate and therefore use of inherent jurisdiction to grant a charge on that property would be contrary to the Act. Section 67 does not mean, however, that trust property does not fall within a trustee's administration. It only addresses the division of the bankrupt's property among the creditors; it does not address what property forms the estate that must be administered by the trustee.

[24] The Supreme Court of Canada addressed this issue in ***Ramgotra (Trustee of) v. North American Life Assurance Co.***, [1996] 1 S.C.R. 325 at para. 61:

> Unlike provisions of the [BIA] such as ss. 71(2), 91 or 68, s. 67(1) tells us nothing about the property-passing stage of bankruptcy. Instead, it relates to the estate-administration stage by defining which property in the estate is available to satisfy the claims of creditors. It effectively constitutes a direction to the trustee regarding the disposition of property...the trustee is barred from dividing two categories of property among creditors: property held by the bankrupt in trust for another person (s. 67(1)(a)), and property rendered exempt from execution or seizure under provincial legislation (s. 67(1)(b)). *While such property becomes part of the bankrupt's estate in the possession of the trustee, the trustee may not exercise his or her estate distribution powers over it by reason of s. 67.*
> (Emphasis added)

[25] In any event, Kingsway's argument in regard to s. 67 rests on the premise that the property is in fact trust property, a proposition that remains undetermined.

[26] Kingsway also asserts that there is no jurisdiction to order that a trustee's fees be paid from property subject to a statutory trust, citing ***P.A.T. Local 1590 v. Broome*** (1986), 61 C.B.R. (N.S.) 233 (Ont. Master) and ***Re C.J. Wilkinson Ford Mercury Sales Ltd.*** (1986), 60 C.B.R. (N.S.) 289 (Ont. S.C.).

[27] In both of those cases, however, the validity of the trusts in question was clear and accepted by the trustee. Further, the question of fees for sorting out their validity was not squarely in issue in either decision. Here, a statutory trust as well as several other trust claims have been asserted but not accepted by the trustee and all remain to be determined by the Court of Queen's Bench.

[28] Kingsway also relies on ***Re Gill*** (2002), 37 C.B.R. (4th) 257, 2002 BCSC 1401 at paras. 29-32 in support of its statutory trust argument. In that case, however, Sigurdson J. recognized the jurisdiction to grant a charge for trustee fees over assets subject to trust claims. He determined on the distinct facts before him not to grant the charge requested.

[29] I therefore accept that inherent jurisdiction exists to grant a charge on property subject to undetermined trust claims.

**2. Permitting trustee costs involved in determining the validity of the trust to be paid out of trust property**

[30] Kingsway objects to the trustee being paid to "defeat" its claim out of what it alleges to be its property. Kingsway's opinion on the merits of its trust claim differs from the trustee's. However, Kingsway does not suggest that the trustee has acted improperly or unfairly in its disallowance of its claim.

[31] I do not characterize the actions of the trustee as an attempt to "defeat" Kingsway's claims. Upon receiving a proof of claim claiming property in possession of the bankrupt, the trustee must respond in one of two ways according to s. 81(2) of the *BIA*. The trustee can either admit the claim and deliver possession of the property to the claimant, or give notice in writing to the claimant that the claim is disputed, indicating the reasons for the dispute. The section provides for an appeal to the Court of Queen's Bench if the trustee disputes the claim. The trustee is not to function as an adversary. Rather, it functions to advise the court of the relevant facts as its officer in a dispassionate manner, in furtherance of its role to administer the estates to completion, leaving the court to decide the matter: see ***Re Beetown Honey Products Inc.*** (2003), 46 C.B.R. (4th) 195 (Ont. S.C.J.), aff'd (2004), 3 C.B.R. (5th) 204 (Ont. C.A.) and *BIA*, s. 41(4). The trustee's conduct to date has been in accordance with requirements of the Act and its participation in the appeal is necessary in this case. Kingsway's claims purport to cover the entire estates of both bankrupts, against which there are competing property claims and unsecured claims.

[32] There is precedent for allowing a trustee to be remunerated from trust property for efforts in sorting out trust claims and distributing the trust *res* to beneficiaries: see for example, ***Re***

***Nakashidze*** (1948), 29 C.B.R. 35 (Ont. S.C.); ***Re Rideout Real Estate Ltd.*** (1957), 36 C.B.R. 111 (Ont. S.C.); ***Re Kern Agencies, Ltd.*** (No. 3) (1932), 13 C.B.R. 333 (Sask. K.B.); ***Re NRS Rosewood Real Estate Ltd.*** (1992), 9 C.B.R. (3d) 163 (Ont. S.C.). In ***NRS Rosewood***, for example, Austin J.



faced the same argument made by Kingsway in this case that the trustee had no entitlement to share in assets which were not the property of the bankrupt. Austin J. concluded that “[a]s the question had to be settled one way or another, and as the Trustee took the initiative, it is only reasonable that some part of the Trustee’s fees be paid out of the property in issue”.

[33] I do not suggest that a trustee will in every case be entitled to be paid from trust property. On the contrary, such an order, based on inherent jurisdiction, must be granted sparingly. The situation before us is unique in many respects:

1. Kingsway asserts a trust on various grounds, none of which are obvious. Kingsway has delayed determination of its claim, resulting in additional work by the trustee;

2. Kingsway’s claim encompasses the entirety of the estate;

3. There are other trust claimants making claims to the same funds;

4. There are significant sums in dispute;

5. This bankruptcy occurred as a result of a failed proposal. Deloitte & Touche went from interim receiver to trustee and the typical guarantee of the trustee’s fees is not in place;

6. There is no other reasonable and more expeditious alternative but to have the trustee participate in the appeal process as part of its administration of these bankruptcies. Most of the other creditors are owed small amounts, aside from a government claim;

7. There is no suggestion that the trustee is acting improperly in disputing the claims; and

8. Kingsway seeks to link the appeal from the trustee’s disallowance with the trial of other unrelated issues.

These circumstances and the centrality of the trust claims to the bankruptcies underscore the necessity of the trustee’s involvement and the payment of its fees from the property subject to the disputed trusts.

[34] Even if Kingsway is ultimately successful in its appeal of the trustee’s disallowance, the trustee has been administering the property and a significant part of its work will likely have benefited Kingsway. The trustee has expended and will continue to expend considerable effort in

sorting out other claims on the property, including the formulation of a plan that Kingsway has joined in for resolving builder claims. It has offered assistance to Kingsway in related proceedings

concerning proposals made by directors and officers of the bankrupts. It has also formulated, coordinated and attended case management meetings throughout the course of its administration.

[35] Kingsway suggests its claim will not go unchallenged if the trustee is not funded to defend the litigation on behalf of the estates; it asserts that one or more of the creditors can pursue the litigation at their own cost pursuant to s. 38 of the *BIA*. However, the litigation is central to these bankruptcies and not merely an action that interests select creditors. The validity and priority of Kingsway's trust claims must be determined and follows from the claims review process mandated by the *BIA*. That process is designed to ensure that only proper claimants share in the bankrupt's property and in these circumstances, the trustee plays an integral part.

[36] Kingsway also submits that the appeal to the Queen's Bench from the trustee's disallowance will be complex, as it intends to bring other solvent parties into the action. Accordingly, Kingsway argues, the *res* of the estates could be frittered away with fees. However, the appeal to the Queen's Bench is intended to be a summary and efficient process to determine the issue relevant to the bankruptcy. To the extent that Kingsway chooses to increase the scope and complexity of the appeal, it must similarly accept the increased costs of the trustee in dealing with that action.

**3. Factors in exercise of discretion**

[37] Generally, inherent jurisdiction should only be exercised where it is necessary to further fairness and efficiency in legal process and to prevent abuse. The following non-exhaustive factors should be considered before invoking inherent jurisdiction here:

> 1. The strength of the trust claim being asserted. The mere assertion of a trust claim is not determinative of the validity of the trust and cannot preclude the trustee from investigating concerns. In some cases, the trust claim may be obvious, as was the case in ***C.J. Wilkinson***, where the claim was based on statutory trusts in favour of employees or tax authorities and the interim receiver conceded their validity. In other circumstances, a trustee will have no choice but to have the issue of the trust determined in order to further the administration of the bankruptcy. In that event, the ultimate beneficiary of the trust may have to shoulder the costs of the determination;
>
> 2. The stage of the proceedings and the effect of such an order on them. For example, the ability of the trustee to make distributions and their amount may depend on the determination of the issue;
>
> 3. The need to maintain the integrity of the bankruptcy process. The equitable distribution of the bankrupt estate must remain at the forefront. The court should recognize the expertise of the trustee in this regard and in effective management of bankruptcy: see ***GMAC*** at para. 50. Also, the court should assess the extent to which the determination is necessary to administer the bankruptcy and discourage academic

or potentially unrewarding litigation;

4. The realistic alternatives in the circumstances. This could include a s. 38 order, deferring a decision or empowering a court to review the decision in the future, for example, after final determination of the claims and the extent of the property available for distribution. The court should consider whether there is an existing guarantee of the trustee's fees, whether the party ultimately determined to be the beneficiary might bear some responsibility for the costs, and whether counsel might be hired on contingency;

5. The impact on the trust claimants and on the trust property as well as on other creditors. The court should examine the breadth of the trust claims, the existence of competing proprietary claims, and whether the trust claims leave any assets in the estate for unsecured creditors in assessing which stakeholder is going to suffer most from the trustee's disputing of the trust claim. In that exercise, the court should assess what part of the estate would ideally bear the burden of costs. It is important to consider whether the determination would proceed by default if the trustee were not fully funded;

6. The anticipated time and costs involved. The court should contemplate whether the proposed determination represents an efficient and effective means of resolving the issue to the benefit of all stakeholders. Consideration should be given to expediting the process;

7. The limits that can be placed on the fees or charge; and

8. The role that the trustee will take in the determination process.

## 4. Exercise of discretion by the case management judge

[38] The case management judge considered the relevant factors and the applicable law. She carefully constructed a limited charge that she viewed as suitable in the circumstances. The order for a prospective charge is subject to the trustee filing a report confirming the bankruptcy inspectors had approved the steps the trustee proposed to take. She delayed the operation of her order to give builder claimants an opportunity to challenge it. She held that if all the property was not ultimately found to be impressed with a trust in Kingsway's favour, that a further hearing be held in order to prorate the trustee's fees between estate and trust assets. Further, she directed that the trustee only address urgent matters of general administration, and that Kingsway's claim be addressed as quickly and efficiently as possible. I see no basis to disturb her exercise of discretion.

[39] One of the fundamental purposes of the *BIA* is to ensure equitable distribution of a bankrupt debtor's assets among the estate's creditors: ***Ramgotra*** at para. 15, citing ***Husky Oil Operations Ltd. v. Minister of National Revenue***, [1995] 3 S.C.R. 453. Determination of the validity of Kingsway's trust claims is central to these bankruptcies. This trustee's participation in that process furthers

appropriate distribution of the assets, whether that be to unsecured creditors in the event all or part of Kingsway's trust claim is rejected by the Court of Queen's Bench, or whether the estate stays out of reach of other creditors as trust property.

[40] The ultimate purpose of the administrative powers granted a trustee under the *BIA* is to manage the estate in order to provide equitable satisfaction of the creditors' claims: ***Ramgotra*** at para. 45. The trustee will be assisting the court and all of the claimants in the bankruptcies in coordinating Kingsway's claims, as well as dealing with the validity and priority of the other trust claims and in providing the necessary information to the Court of Queen's Bench to resolve these issues. For these reasons, it is also just and practical that inherent jurisdiction be used to grant the charge for the trustee's fees.

**Conclusion**

[41] There is inherent jurisdiction to permit trustee's fees to be paid from property that is subject to undetermined trust claims in appropriate circumstances. The case management judge recognized the power must be used sparingly and did not err in exercising jurisdiction in this case. The appeal is therefore dismissed.

Application heard on September 05, 2006

Reasons filed at Edmonton, Alberta
this 10th day of October, 2006

"Paperny J.A."
Paperny J.A.

I concur: "Côté J.A."
Côté J.A.

I concur: "Paperny J.A."
Authorized to sign for: Sulyma J.

**Appearances:**

E.A. Dolden
B.D. Rhodes
for the Appellant

K.A. Rowan
for the Respondent

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**Corrigendum of the Reasons for Judgment of**
**The Honourable Madam Justice Marina Paperny**

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On page 6, [33] & [34] have been joined and now read:"....contrary, such an order, ...."

Court No. 14313 **2010 SKQB 17**
Estate No. 23-883167 J.C.R.

IN THE COURT OF QUEEN'S BENCH
PROVINCE OF SASKATCHEWAN
IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF THE BANKRUPTCY OF

KRISTYN JOELLE INSLEY

**BETWEEN**:

**ROYAL BANK OF CANADA**

**APPLICANT**

**AND:**

**KRISTYN JOELLE INSLEY**

**RESPONDENT**

Jim Kroczynski, for the Royal Bank of Canada
Jeff Lee, for Dr. Insley
Mary Lou Senko, for Canada Student Loans
Marla Adams, for Deloitte & Touche Inc, trustee

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**JUDGMENT** LIAN M. SCHWANN, Q.C.
January 19, 2010 Registrar in Bankruptcy

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[1] The Royal Bank of Canada ("RBC"), the major creditor in Kristyn Insley's bankruptcy, applies to expunge or reduce the proofs of claim of 'CRA – Govt Programs (Non Tax) Acct Maint' and of 'Trustees of Saskatchewan Student Aid Fund' (the

"impugned claims") pursuant to s. 135(5) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"). The application is opposed by Kristyn Insley ("Insley"), Canada Student Loans ("CSL") and the trustee.



***Facts***

[2] Insley assigned into bankruptcy on July 19, 2006. As her discharge was opposed by the RBC, a hearing ensued before me which culminated in my decision of October 26, 2007, reported at 2007 SKQB 383 (the "decision"). Pursuant to that decision, Insley was granted her discharge from bankruptcy conditional upon consenting to judgment in favour of the trustee in the amount of $193,000.

[3] The Statement of Affairs filed at the time of assignment listed in excess of $287,000 of unsecured debt of which $193,000 was owed to RBC for a 'non-government student loan'. RBC had additional claims of $7,577 on a credit card debt along with Royal Bank (government guaranteed) student loans of $7,458 and $7,641 respectively. She also reported a debt owed to 'National Student Loans' in the amount of $69,829.

[4] The Claims Register submitted with the Trustee's Report in March 2007 reveals the following in relation to the impugned claims:

| Unsecured Creditor | Amount of Claim | Amount filed | Admitted |
|---|---|---|---|
| National Student Loans | $69,829 | $55,244 | $55,244 |
| Royal Bank Student Loans | $7,458 | $7,180 | $0.00 |
| Royal Bank Student Loans | $7,641 | $7,357 | $0.00 |

[5] A subsequent Claims Register was prepared in July 2007 for the discharge hearing depicting the following with regard to the claims in issue:

| Unsecured Creditor | Amount of Claim | Amount filed | Admitted |
|---|---|---|---|
| Canada Revenue Agency | unknown | $62,588 | $62,588 |

| | | | |
|---|---|---|---|
| (Account Maintenance Unit) | | | |
| Royal Bank Student Loans | $7,458 | $7,180 | $0.00 |
| Royal Bank Student Loans | $7,641 | $7,357 | $0.00 |



[6] Another Claims Register was prepared in 2009 for dividend distribution purposes with the only meaningful change between this one and the previous one being the inclusion of the 'Trustees of Saskatchewan Student Aid Fund' with a claim filed and admitted in the amount of $7,167. The two RBC student loans continue to be shown on this document however they are now identified as no proof of claim having been filed.

[7] The trustee and CSL explain the discrepancies in amounts and with names of creditors in the following way. The creditor initially described as 'National Student Loan' is Her Majesty the Queen in right of Canada as represented on collections by the 'CRA Account Maintenance Unit'. They filed an initial claim of $55,244 but later enlarged it to $62,588 when $7,344 was added from one of the Royal Bank student loans. Both Royal Bank student loans (as opposed to the non-government student loan of $193,000) were guaranteed by the two levels of government and on Insley's assignment, the RBC was paid out with $7,344 of debt assumed by Canada and the other debt of $7,167 assumed by the Trustees of the Saskatchewan Student Aid Fund.

[8] In September 2009, following extensive correspondence with the trustee, the RBC expressly asked the trustee to disallow (expunge) the impugned claims. The trustee responded in writing as follows: "Please be advised that, Deloitte & Touche Inc., in its capacity as Trustee in Bankruptcy, in accordance with section 135(5) of the *BIA* hereby declines to interfere in this matter".

[9] At the outset of this application counsel for the RBC conceded that proofs of claim for the impugned claims were in fact filed and disclosed by the trustee but sought to have

them expunged on other grounds.

***Position of the Parties:***

***RBC***

[10] RBC advanced three grounds to expunge the impugned claims:

(a) the impugned claims were not filed prior to Insley's discharge or were not disclosed by the trustee at or prior to the discharge hearing;

(b) the impugned claims survive bankruptcy accordingly are required to be paid regardless of any condition imposed upon the bankrupt for discharge including the award of Judgment;

(c) the award of Judgment was not intended to benefit claims which survived bankruptcy or those which were not filed or disclosed prior to the discharge hearing.

[11] The first ground – that the impugned claims were not filed prior to discharge or disclosed by the trustee – was conceded by counsel for RBC once it became aware of the updated Claims Register and the explanation provided by CSL. RBC proceeded to argue that, notwithstanding this concession, the legislative language in s. 135(5) stands on its own and presents to creditors an unqualified right to expunge admitted claims where 'the trustee declines to interfere.'

[12] RBC contends that once the trustee opens the door by an express refusal to interfere with an allowed claim, the Court has the unconstrained discretion to expunge claims. They urge me to do so in these circumstances because the RBC would otherwise receive a much smaller dividend than expected and thereby suffer prejudice, and secondly because my earlier decision implicitly excluded 'government student loans' from sharing in the fruits of the consent judgment.

[13] RBC points to the considerable time and expense expended in opposing Insley's discharge with the net result being a sizeable consent judgment the RBC believed was theirs and theirs alone. The RBC further argues that as the impugned claims survive bankruptcy discharge by virtue of s. 178 of the *BIA*, those creditors have expanded rights and are able to collect both now and in the future. The CSL and Saskatchewan Student Loans would not therefore suffer any prejudice if their claims were expunged, they argue.

[14] Finally, RBC contends that the discharge decision specifically precluded student loan creditors from sharing the fruits of Insley's judgment. The fact this court failed to address sharing by other creditors, they argue, must be interpreted as judicial direction barring sharing of dividends.

***Canada Student Loans***

[15] CSL characterizes RBC's position as an 'ironic' one. The RBC filed two government student loan claims (both slightly in excess of $7,000) which were subsequently fully redeemed by the two levels of government through government guarantees. In short, RBC has been made whole on the full value of those loans – which were clearly before the Court at the time of Insley's discharge hearing - but now advances the position that it would be unfair for the guarantors to share in dividend distribution.

[16] Furthermore, even though the CSL debt survives discharge by operation of s. 178, CSL is entitled to share rateably on distribution of dividends as a function of legislation and there is no law to support the position advanced by RBC. Expunging these claims, particularly at this late stage of estate administration, would constitute a significant change to the law of rateable distribution and an indirect attempt to re-argue Insley's discharge application.

***Insley***

[17] Counsel for Insley begins by pointing out that RBC presented no evidence that the impugned claims did not exist prior to Dr. Insley's discharge hearing or of the claims not otherwise being legitimate. To give effect to RBC's position, he argues, is inconsistent with the plain wording of s. 141 of the *BIA* which clearly provides that all claims – without distinction – are to be paid rateably. There is nothing in the *Act* or case authority to support RBC's proposition that s.178 survivable claims do not share in dividend distribution. Reliance is placed on the Manitoba cases of *Weihs, Re*, 2005 MBQB 108, 12 C.B.R. (5th) 118 and *Stoski Estate (Trustee of) v. Royal Bank*, 2009 MBQB 17, 51 C.B.R. (5th) 40.

[18] Counsel for Insley also points out that RBC will suffer no prejudice simply because student loan creditors are included in the proposed distribution for the simple reason that such approach reflects the scheme of distribution in the *BIA* and is consistent with case authority. In fact, to the extent there is prejudice, it would be borne by Insley if the RBC prevails. Finally, Insley argues that RBC's application amounts to a collateral attack on the discharge decision. If RBC was dissatisfied with that decision, the proper recourse was to appeal.

***Trustee***

[19] Until discharged, the trustee has an ongoing duty to examine and review all claims which are lodged and to admit for dividend, or disallow where appropriate. The rights of creditors with survivable debts do not impact on these duties.

[20] The trustee emphatically maintains that both Canada and Saskatchewan student

loan debts were disclosed in the trustee's reports. The Claims Register is not static; it can and often does change as the estate moves along such as where creditors amend their claim or where they are subsequently withdrawn. In any event, the trustee points out that the date for admittance of claims is the date of distribution, not the date of the bankrupt's discharge. In response to RBC's secondary argument, they submit that the scheme of distribution in s. 136 applies regardless of the rights of s. 178 creditors.



***Issues:***

[21] The issues raised in this application are the following:

(a) What is the test to be applied by a party seeking relief under s. 135(5)?

(b) Are creditors with a s. 178 'surviving' debt entitled to participate and share in distribution of estate dividends?

(c) Did this Court's decision exclude government student loan creditors from sharing in estate dividends?

***(a) the test applied to expunge a claim under s. 135(5) of the BIA***

[22] Section 135 of the *BIA* sets out the provisions for admitting and disallowing claims with ss. 135(4) and (5) governing the procedures on appeal of disallowance and for expunging or reducing any proven claim. It provides:

> 135.(1) The trustee shall examine every proof of claim or proof of security and the grounds therefor and may require further evidence in support of the claim or security.
>
> (1.1) The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.
>
> (2) The trustee may disallow, in whole or in part,
>
> (a) any claim;
>
> (b) any right to a priority under the applicable order of priority set out in this Act; or
>
> (c) any security.

> (3) Where the trustee makes a determination under subsection (1.1) or, pursuant to subsection (2), disallows, in whole or in part, any claim, any right to a priority or any security, the trustee shall forthwith provide, in the prescribed manner, to the person whose claim was subject to a determination under subsection (1.1) or whose claim, right to a priority or security was disallowed under subsection (2), a notice in the prescribed form setting out the reasons for the determination or disallowance.
>
> (4) A determination under subsection (1.1) or a disallowance referred to in subsection (2) is final and conclusive unless, within a thirty day period after the service of the notice referred to in subsection (3) or such further time as the court may on application made within that period allow, the person to whom the notice was provided appeals from the trustee's decision to the court in accordance with the General Rules.
>
> (5) The court may expunge or reduce a proof of claim or a proof of security on the application of a creditor or of the debtor if the trustee declines to interfere in the matter.



[23] I find it helpful to begin by placing the whole of s. 135 in its proper context. This section imposes a statutory obligation on trustees to examine every proof of claim and every security for the purpose of determining if the claim or security, as the case may be, is valid. (Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada*, vol. 2, p. 5-180; *Canadian Imperial Bank of Commerce v. 433616 Ontario Inc*. (1993), 17 C.B.R. (3d) 160). If unsatisfied with the proof of claim or its supporting material, the trustee has not only a right but a corresponding duty to demand sufficient evidence to establish the validity of the claim. The trustee is given many tools under the *BIA* to fulfil this function including, where necessary, examination of parties and requiring production of documents. (Houlden and Morawetz, vol. 2, p. 5-181)

[24] Following examination, the trustee either allows the claim or disallows it in whole or in part. A disallowance is final and conclusive unless appealed by the aggrieved creditor within the time permitted for doing so under s. 135(4). Section 135(5) is the flip side of a disallowance. Where a claim is admitted, s. 135(5) permits creditors or the bankrupt to apply to expunge or reduce the claim *if the trustee declines to interfere in the*

*matter*.

[25] An application to expunge pursuant to s. 135(5) has been characterized by the courts as an *appeal* against allowance. "In effect, the motion under section 135(5) is an appeal by a creditor or the debtor against an allowance by the trustee of a proof of claim or proof of security" (Houlden and Morawetz, vol. 2, p 5-205 (cites omitted); see also s. 192(1)(n) *BIA*).

[26] In *Lamont Hi-Way Service Ltd. v. Bunning*, 2003 ABQB 297, 44 C.B.R. (4th) 91, para. 20 and 21, an application to expunge was described in this fashion:

> Section 135 creates a two sided token. If a trustee disallows a creditor's claim the creditor's only remedy is given by s.-s. (4)……If a trustee allows a claim other creditors and the bankrupt are adversely affected, so s.-s. (5) gives then a right to challenge the trustee's decision. There is little case law on s.-s. (5). Houlden & Morawetz, Bankruptcy & Insolvency Act (The 2002 Annotated) say that 'in effect' a motion under the s.-s. is an appeal by a creditor or the bankrupt of the trustee's disallowance of a claim, p. 551.

[27] *Marsuba Holdings Ltd., Re* (1998), 8 C.B.R. (4th) 268 is another case where a s. 135(5) application was explored. At paragraphs 14 and 15 the learned Master examined the scope of the provision, commenting as follows on the applicable test.

> Counsel for the trustee says the applicant must show that the trustee acted unreasonably or improperly in accepting the proof of loss. Counsel would have it that so long as the trustee acted reasonably, the actual legitimacy of the claim is irrelevant. I respectfully disagree.
>
> Quite apart from questions of natural justice raised by this position….this construction of s. 135(5) is contrary to the tenor of s. 135 as a whole. The first four sub-sections deal with the procedure to be followed where a creditor appeals the *disallowance* of a claim by a trustee, and in such cases the appeal is decided simply on the basis of the legitimacy of the claim. There is no reason at all why different considerations should apply to appeals of a decision by the trustee to allow a claim. The only question should be <u>whether the claim is indeed legitimate</u>.
> [emphasis added]

[28] No further elaboration was offered in *Marsuba* as to what constitutes a "legitimate" claim nor did the Court expand upon whether an appeal under this subsection proceeds on the record or is *de novo* in nature.

[29] Regardless of the nature of a s. 135(5) appeal, the standard of review also remains an open issue unexplored in the referenced cases. This Court summarized the standard of review in the context of appeals from disallowance under s. 135(4) in the following manner: "Where the trustee's decision involves a question of law or the interpretation of a statute, the standard of review is correctness. On the other hand, where the matter under consideration is factual in nature or involves a discretionary element, the standard of review is reasonableness." (*Business Development Bank v. Pinder Bueckert*, 2009 SKQB 458 at para. 24; see also *Eskasoni Fisheries Ltd., Re* (2000), 16 C.B.R. (4th) 173; *Lloyd's Non-Marine Underwriters v. J.J. Lacey Insurance Ltd.*, 2008 NLTD 9; 41 C.B.R. (5th) 137.)

[30] The application before me is one to expunge two claims filed and admitted by the trustee. The onus rests with RBC to establish error on the part of the trustee, or in keeping with the approach taken in *Marsuba*, to establish these were not "legitimate" claims. In my view there is no need to explore the contours of what is or is not a legitimate claim, or other collateral issues arising on appeal (issues not argued by the parties) for the simple reason that RBC abandoned its initial argument that the impugned claims were not filed prior to Insley's discharge or disclosed by the trustee. In any event, no argument was advanced nor evidence presented concerning the underlying validity of the claims or their allowance. There is no suggestion whatsoever that the trustee improperly interpreted the law, ignored crucial facts, exercised its discretion improperly or acted outside of its authority in the course of exercising its function under s. 135. For all of these reasons, RBC's initial argument fails.

(b) ***are section 178 'survivable debts' excluded from sharing in dividends?***

[31] RBC advances this line of argument through the vehicle of a s. 135(5) appeal, accordingly it must be considered within that context. As noted, the RBC does not challenge the validity of the claim but instead attempts to use s. 135(5) to disrupt the trustee's intended scheme of distribution of estate dividends. This argument is premised on the proposition that once the pre-condition to s. 135(5) exists, i.e. the trustee 'declines to interfere in the matter', a creditor possess an unqualified and unconstrained right to challenge the proposed distribution scheme in the face of an otherwise valid and allowed claim.

[32] In *EnerNorth Industries Inc*., *Re*, 2009 ONCA 536, 55 C.B.R. (5$^{th}$) 1the Ontario Court of Appeal examined the scope of an application to expunge under s. 135(5) in the context of a debt arising from a valid and enforceable judgment. That court's observations concerning the purpose of s. 135(5) applications is summarized at para. 38:

> The appellants' argument that they have an 'unqualified right' to challenge Oakwell's proof of claim under section 135(5) is based on the unsupported theory that the *only* precondition to a creditor being entitled to a hearing under s. 135(5) is that the trustee must have declined to interfere in the matter. I do not read the provision in such a restricted manner. [emphasis in original]

[33] Although *EnerNorth* dealt with an attack in bankruptcy proceedings of an otherwise valid and enforceable judgment, the decision, in my view, stands for the broad principle that s. 135(5) does not confer on creditors an unqualified right of challenge to proven claims. Something more is required apart from the trustee merely declining to interfere in the matter.

[34] Neither, in my judgment, should s. 135(5) be used as an entry point to overturn or disrupt other processes or decisions made by the trustee in the course of estate

administration. Section 135(5) constitutes a right of challenge limited to allowed or disallowed claims and should not be viewed more broadly than that. The right to challenge other decisions made by the trustee in the course of estate administration is available through s. 37 of the Act where an aggrieved person seeks court oversight over those decisions.



[35] Even if I am wrong, there is nothing in the Act or in decided cases which supports RBC's position. Section 178(1) carves out a list of eight distinct types of debts which survive bankruptcy and which are not extinguished on the bankrupt's discharge. Debts or obligations in respect of a loan made under the *Canada Student Loans Act*, R.S.C. 1985, c. S-23, the *Canadian Student Financial Assistance Act*, S.S. 1994, c. 28, or an enactment of the province which provides student loans or guarantees of loans is a "survivable debt" if assignment is made within the prescribed time frames. (s. 178(1)(g))

[36] Section 141 makes clear that *subject to any provision of the Act*, all claims proved in a bankruptcy are to be paid rateably. There is nothing in this section, s. 178 or s. 136 (which addresses priorities on distribution) precluding s. 178 surviving creditors from sharing in dividends or in any manner adjusts the concept of rateable distribution prescribed by s. 141. In fact, case law supports the opposite position. Houlden and Morawetz make the following observation at vol. 3, p. 6-230:

> The claims listed in s. 178(1) are properly provable in bankruptcy. <u>Proofs of claim may be filed for them and the creditor can receive a dividend on them</u>: *Trusts & Guarantee Co. v. Brenner* (1932), 13 C.B.R. 518; affirmed in part 15 C.B.R. 112 (S.C.C.); *B. (S.M.A.) v. H. (J.N.)* (1993), 23 C.B.R. (3d) 81, 87 B.C.L.R. (2d) 241, [1994] 4 W.W.R. 281, affirmed (1994) 31 C.B.R. (3d) 302.
> [emphasis added]

[37] The decisions in *Weihs, Re* (para. 7) and *Stoski Estate* (para. 25) confirm this approach.

[38] In the absence of clear legislative direction, or case authority interpreting the effect of s. 178 claims otherwise, I conclude that Insley's government student loan creditors are entitled to share in the dividends intended to be dispersed by the trustee in accordance with s. 136 of the *BIA*. It follows that this basis to expunge these claims also fails.

### *(c) Did the decision in* **Insley, Re** *exclude government student loan creditors from sharing dividends in the bankruptcy estate?*

[39] RBC argues that my failure to squarely address sharing of estate assets with Insley's government student loan creditors was intended to exclude them from distribution of estate dividends.

[40] The mere fact the present line of argument was not addressed in my decision was simply because it was not put in issue at the time of the discharge hearing. The *Act* speaks for itself in relation to the scheme of distribution and in the event of ambiguity or misunderstanding concerning the sharing in dividend distribution, this decision serves to resolve those questions.

### *Conclusion*

[41] RBC's application to expunge the claims of the CRA – Govt Programs (Non Tax) and the Trustees of Saskatchewan Student Aid Fund is dismissed. CSL shall have costs fixed at $500 payable from the estate.

DATED at the City of Regina, in the Province of Saskatchewan, this 19th day of January, 2010.

"Lian Schwann, Q.C."

Registrar in Bankruptcy

# Court of Queen's Bench of Alberta

Citation: Sapient Grid Corp. (Re), 2012 ABQB 357



**Date:** 20120528
**Docket:** BE03 1502756
**Registry:** Edmonton

In the Matter of the Bankruptcy of
Sapient Grid Corp.

Between:

Oil Lift Technology Inc.

Appellant

- and -

Deloitte & Touche Inc.

Respondent

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Memorandum of Decision
of
W. S. Schlosser, Registrar in Bankruptcy

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[1] These are three appeals of the Trustee's disallowance of property claims.

[2] The situation appears complex but, on examination, the basic facts are relatively straightforward and, for the most part, not in dispute. However, there is conflicting evidence on some key issues.

[3] Oil Lift Technology Inc. hired the Bankrupt, Sapient Grid Corp. to produce an oilwell site device that would allow remote monitoring and control of well sites (the "AMOS System"). Sapient undertook the project with the assistance of Harold Kobler and Terry Renneberg. Oil Lift advanced funds to Sapient and a prototype was built.

[4] The prototype went to Australia for testing in the field. It was installed with less than ideal timing or ideal circumstances. The system required input and contribution from a variety of sources, (including Oil Lift) for it to work. Both Kobler and Renneberg wrote some of the computer code for different portions of the application.

[5] There is conflicting evidence about the status of the system at the end of the test. But it is clear that the system was not complete. It required work.

[6] Oil Lift sued Sapient and Terry Renneberg, March 22, 2011. In general terms, the lawsuit is to recover the amounts Oil Lift paid to Sapient. It also seeks unliquidated damages for, *inter alia,* breach of warranty. The action against Renneberg is based in misrepresentation, breach of duty and the tort of interference with contractual relations.

[7] Sapient filed a voluntary assignment in bankruptcy in late May 2011. The AMOS project was never completed.

[8] Oil Lift sought to prove its claim in the bankruptcy. This claim was disallowed by the Trustee. This is the first appeal.

[9] The second appeal has primarily to do with the ownership of the intellectual property comprising the AMOS System. Mr. Renneberg has asserted a claim for this together with a claim for some other physical property. This claim was also disallowed by the Trustee. Mr. Renneberg has appealed.

[10] The Trustee's first disallowance and the appeal of that disallowance resulted in an explosion of evidence. There were six very detailed Affidavits prepared; variously in support of the disallowance, or the appeal, and two cross-examinations on the Affidavits. The cross-examinations themselves exceed one hundred pages.

[11] The Trustee's disallowance of Mr. Renneberg's section 81 property claim prompted two further Affidavits.

[12] Mr. Kobler asserted a property claim in January of this year which was also disallowed by the Trustee. The disallowance prompted a further detailed Affidavit on appeal.

[13] In the interim, Mr. Kobler sought access to documents in the bankruptcy and the Trustee applied to sell the Bankrupt's hard assets, which was opposed and a qualified Order was granted.

[14] The lawsuit underlying the first disallowance has now grown to include a Counterclaim and Third Party proceedings. Given this additional evidence, the three appeals now before me are quite different from the claims initially presented to the Trustee.



[15] There are three legal questions arising from the Trustee's disallowances and these late developments:

(1) The standard of review to be applied to a Trustee's disallowance;

(2) Whether an appeal from a Trustee's disallowance is *de novo,* and whether new materials can be considered;

(3) If the appeals are allowed, the options open to a Registrar to bring these matters to a conclusion.

<u>Standard of Review</u>

[16] Subsections 135(1) and (1.1), which deal with proof of claims and provable contingent or unliquidated claims, are mandatory in terms of the Trustee's duties and obligations. The decided cases tell us that the standard of review of a Trustee's rejection of a claim is "correctness". The standard of review of a Trustee's *valuation* of a contingent or unliquidated claim is "reasonableness". ***Re Transglobal Communication Group Inc.,*** 2009 ABQB 194 at para. 74, per Yamauchi, J.

[17] Here, all of the claims were rejected, so the starting point for the review of the Trustee's disallowance is correctness.

[18] The threshold for establishing the existence of a contingent or unliquidated claim is low. In general terms, there must be an 'air of reality' to the claim. The claim must not be too remote or speculative. The existence of the claim need not be established on a balance of probabilities to the ordinary civil standard.

> ***Re Confederation Treasury Services Ltd.*** (1997) 43 CBR (3d) 4 (Ont. CA);
> ***Re Experienced Equipment Sales and Rentals*** (2011) ABQB 641, per Belzil, J.
> ***National Bank of Canada v. Merit Energy Ltd.*** (2001) ABQB 583, per LoVecchio, J.

[19] The Oil Lift Statement of Claim discloses a cause of action. It is not too remote or speculative. It is not necessary to resort to further materials or evidence to see that the claim passes the low initial threshold. Accordingly, the appeal of the disallowance of the Oil Lift's claim is allowed. Valuation, however, is another matter and will be discussed below.

<u>Section 81 Claims</u>

[20] Both Kobler and Renneberg have advanced section 81 claims. Section 81 provides that the person claiming property in possession of the Bankrupt should provide a sufficiently particularized Proof of Claim

(subsection 81(1), (2)). Section 81(3) puts the onus on the claimant to establish their property claim. (***Re Melnitzer,*** (1991) 9 CBR (3d) 30, 87 DLR (4th) 696).

[21] The starting point for intellectual property claims is the federal *Copyright Act*, R.S.C. 1985, C-42. The author (of a computer program) is the owner of the program in issue (section 13(1)), unless ownership is displaced by employment, or agreement. ***Massie and Renwick Limited v. Underwriters Survey Bureau Limited et al***, [1940] SCR 218. (There is a similar provision with respect to author's manuscripts in section 83 of the *Bankruptcy and Insolvency Act*).

***[22]*** In this case, the evidence does not disclose any clear *agreement* displacing ownership.

[23] That leaves employment. Among many decided cases on the topic, ***671122 Ontario Ltd. v. Sagas Industries Canada Inc.,*** 2001 SCC 59 and, more recently (for example), ***Alberta Permit Pro v. Booth***, 2007 ABQB 562, per Reid, J. at paras. 129-147, set out the considerations for determining whether a person is an employee. The tests in those cases are not satisfied on the evidence before me. The gist of the evidence in the present case is that Renneberg and Kobler were more like joint venturers with the Bankrupt, than employees.

[24] It is also not for the claimant to *disprove* potential exceptions to ownership. On balance, the evidence does not demonstrate that one of the exceptions should apply. Applying the standard of correctness to the section 81 claims, the appeals of the Trustee's disallowances of the property claims are also allowed.

## Fresh Evidence on Appeal

[25] The uncontroverted evidence is that there was a contract between Oil Lift and the Bankrupt, although the contract was not formalized, and some of the terms are in dispute. There is no doubt that the contract was partly performed.

[26] We do not know the value of the existing equipment, or the value of the technology in its present state of development. However, it appears that the primary value, if any, is in the intellectual property rather than the hardware itself.

[27] In the simplest terms, the evidence discloses that there was a contract and a breach. If the contract was to provide a workable, saleable product, the Bankrupt's efforts plainly fell short of the mark. However, the technology was to be developed with the participation of the claimant, Oil Lift, and overall responsibility for the deficiencies in the prototype is not entirely clear cut. The division of responsibility remains to be determined.

[28] Sapient received a substantial amount of money from Oil Lift for the development of the AMOS system. Exactly how much is in issue and is not clearly demonstrated. There are further issues about whether these contributions were refundable or whether they were investment-type expenses intended to be used for the development of the final product. There are also issues about the extent to which a working final product was warranted by the Bankrupt.

[29] The role of a Trustee with respect to the determination of an unliquidated or contingent claim under section 135 of the *Bankruptcy and Insolvency Act* is, two fold. First of all the Trustee has to decide whether the claim is not too remote or speculative. Once the claim passes this test, the next step is to value it.



[30] The authorities determining what evidence should be considered on appeal are mixed. Some cases say that appeals are *de novo* and fresh evidence can be considered on appeal as a matter of course.

> ***Re Eskasoni Fisheries Ltd.,*** (2000) 16 CBR (4th) 173 (NSSC);
> ***Re Alberta Permit Pro,*** (2011) ABQB 141;
> ***Re Experience Equipment Sales and Rentals***, 2001 ABQB 641.

[31] Other cases hold that appeals from a Trustee are 'true appeals'. They are essentially appeals on the record that was before the Trustee.

> ***Re Galaxy Sports Inc.,*** 2004 BCCA 284.

[32] A hybrid line exists as well:

> ***Re San Juan Resources Inc.,*** 2009 ABQB 55 (Prowse, R.);
> ***Re Transglobal Communications Group Inc.***, 2009 ABQB 195 (at para. 49-50, per Yamauchi, J.;
> ***Re South Beach Homes Ltd.,*** 2010 SKQB 182, per Schwann, R;

[33] The hybrid approach is that an appeal is on the record but it can be *de novo*, involving fresh evidence, where the interests of justice require it. (This was also the fall back position in the ***Alberta Permit Pro*** case).

[34] The *Bankruptcy and Insolvency Act* is sometimes said to be a "businessman's statute'. All that means is that the Act should be administered in a practical and accessible way. Rigid formalism should be rejected and a pragmatic approach should be preferred. However, a claimant should be encouraged to put their best foot forward with their proof of claim. Automatically accepting fresh evidence on appeal would encourage a careless approach to initial proofs. It would also have the effect of transferring the obligations imposed upon the Trustee under section 135 of the Act, to the Court. Accordingly, some explanation ought to be given about why the material now before a Registrar was not initially before the Trustee.

[35] This case is striking in that only a faction of the materials now before the court were before the Trustee when the claims were initially considered. However, despite the ever expanding evidence, there was enough before the Trustee to demonstrate that Oil Lift's contingent, unliquidated claim was not too remote or speculative. There was also, in my view, not enough to demonstrate that ownership of the intellectual property had been displaced from its authors.

[36] The bulk of the evidence *now* before this court demonstrates, unequivocally, that there are live issues in the underlying lawsuit advanced by Oil Lift. Only one party to that lawsuit is bankrupt. The evidence clearly

demonstrates that any damages claimed in the claim (or the counterclaim) are not now capable of assessment on this evidence, or in this forum. Most of the evidence generated after the initial disallowance demonstrates that the claim is in no state to be valued even with the benefit of the additional evidence.



## Options

[37] A Registrar's powers are determined by section 192 of the *Bankruptcy and Insolvency Act*. Among the powers set out in section 192 are the powers to hear and determine appeals from the decisions of a Trustee (section 192(1)(n))and to hear and determine any matter, with the consent of the parties (section 192 (1)(j)). The Registrar may also refer a matter to a Judge for disposition (section 192(6)). (There is a parallel provision in section 13 of the *Court of Queen's Bench Act* permitting a Master to refer a matter to a Judge).

[38] Some of the options open to a Registrar on an appeal from a Trustee's disallowance, in addition to agreeing with the Trustee and upholding the Trustee's determination, would be:

(1) to allow the appeal and assess the claim,
(2) to allow the appeal and refer it back to the Trustee for a determination,
(3) to allow the appeal and permit a revised Proof (***Sinnathurai (Trustee of) v. Sabapathipillai***, 2010 69 CBR (5th) 287 (Ont SCJ));

All of which would be consistent with the Registrar's consideration of new evidence following a disallowance.

[39] Another option would be to allow the appeal and direct a trial. The authorities appear to be divided on this point. A trial was directed in: ***Re Masson,*** (1992) 17 CBR (3d) 230, 136 AR 349 (pursuant to sections 2 and 187(8) of the *BIA)*; ***Re Phillips***, (1994) 27 CBR (3d) 126 (Funduk, Registrar); ***Re Page***, 2006 ABQB 430 (Waller, Registrar). Registrar Prowse in the ***San Juan*** case directed a *Summary Trial*.

[40] Doubt appears to be cast upon the option of directing a trial by ***Re Stuart and Sutterby*** (1930) 11 CBR 279 (Ont SC Aff'd) (1931) 12 CBR 267 (CA). This decision was followed by the Manitoba Court of Queen's Bench in ***Re Hunger***, 2008 NBQB 193 and ***Kalinchuk (Trustee of) v Martinussen*** (2000) 17 CBR (4th) 238. In my view, the Ontario Court of Appeal decision may raise an issue about the power of a Registrar to *hear* a trial but I agree with the decisions of the Alberta Registrars noted above. Even if a Registrar does not have a power to try an issue, directing that a matter go to trial, if not within the Registrar's powers, under section 2 and 187 of the *BIA,* would certainly be justified by section 192(6), which permits the Registrar to refer a matter to a Judge. I have some difficulty with the idea that a Registrar could only refer a matter to a Judge for a determination about *whether* a trial should be directed. (Note: ***The 2012 Annotated Bankruptcy and Insolvency Act,*** Houlden et al (at I§27, I§53)). An interpretation that favours a more complex and less expedient administration of the Act is not to be preferred

[41] Deciding whether something can be decided summarily, or whether it should go to trial is one of the most familiar and natural parts of a Masters jurisdiction. It is only logical here that the Registrar should exercise a similar power.

[42] In this case, there is conflicting evidence, issues of credibility, questions of apportionment of responsibility, and there will likely be expert testimony. It appears to be tailor-made for a trial. This would not be an appropriate circumstance to send it back to the Trustee, even with the new material, to attempt to value the claim. Accordingly, the valuation of the claim should proceed to trial. It would be appropriate to have the claims and cross claims of the non-insolvent parties determined at the same time. If necessary an Order can be made pursuant to section 69.4, allowing Oil Lift's action to proceed. This may be the most expeditious way of dealing with these issues.



Heard on the 13th day of October, 2011, 10th day of November, 2011, and 9th day of February, 2012.

**Dated** at the City of Edmonton, Alberta this 28th day of May, 2012.

W. S. Schlosser
Registrar in Bankruptcy

**Appearances:**

Karen Fellowes
Davis LLP
for the Appellant

B. Beggs
Deloitte & Touche Inc.
Trustee in Bankruptcy

R. Nickerson
Nickerson Roberts Holinski & Mercer
for Harry Renneberg

H. Kobler
Claimant

Ken Pawlyna
Office of the Superintendent of Bankruptcy

COURT OF APPEAL FOR ONTARIO

CITATION: Summit Glen Waterloo/2000 Developments Inc. (Re), 2016 ONCA 405
DATE: 20160530
DOCKET: C58356



Cronk, Pepall and Lauwers JJ.A.

In the Matter of the Bankruptcy of Summit Glen Waterloo/2000 Developments Inc., of the City of Toronto, in the Province of Ontario

Patrick Shea and Brent Arnold, for the appellant/respondent by way of cross-appeal, A. Farber & Partners Inc., as Trustee in Bankruptcy of Annopol Holdings Ltd. and Summit Glen Group of Companies Inc.

Maurice J. Neirinck and Michael McQuade, for the respondents Morris Goldfinger and 1830994 Ontario Ltd. and for the appellant by way of cross-appeal, 1830994 Ontario Ltd.

Heard: October 14 and 15, 2015

On appeal from the judgment of Justice David M. Brown of the Superior Court of Justice, dated February 3, 2014, with reasons reported at 2014 ONSC 756, 9 C.B.R. (6th) 86.

**Pepall J.A.:**

## Introduction

[1] This is the third of three companion appeals, the other appeals bearing file numbers C57879 and C57898. This court's decisions in the three appeals are being released contemporaneously. The background to the three appeals is described in detail in this court's reasons in C57879.

[2] On December 1, 2008, Summit Glen Waterloo/2000 Developments Inc. ("SG Waterloo") was placed under receivership and on June 28, 2010, it was adjudged bankrupt. A. Farber & Partners Inc. ("Farber"), in its capacity as Trustee in bankruptcy of both Annopol Holdings Ltd. ("Annopol") and Summit Glen Group of Companies Inc. ("SG Group"), asserted claims against SG Waterloo, as did Montor Business Corporation ("Montor"), Dr. Morris Goldfinger, and 1830994 Ontario Ltd. ("183"), a company controlled by Goldfinger. These claims were to be heard by the Registrar in Bankruptcy but the trial judge decided that they should be heard in a hybrid trial, together with the subject matter of Court File Nos. C57898 and C57879. Farber now appeals from the trial judge's disallowance of certain claims it advanced in SG Waterloo's bankruptcy. 183 cross-appeals from the trial judge's disallowance of its claim in SG Waterloo's bankruptcy.



[3] For the reasons that follow, I would allow Farber's appeal in part and would dismiss 183's cross-appeal.

## A. Annopol's Claim in SG Waterloo's Bankruptcy

### (i) Background

[4] The first part of this appeal concerns the trial judge's partial disallowance of certain claims advanced by Farber in its capacity as Annopol's Trustee in bankruptcy in the SG Waterloo bankruptcy.

[5] Annopol had lent money to SG Waterloo and filed a proof of claim in SG Waterloo's bankruptcy proceedings. Accordingly, the trial judge had to determine what amount SG Waterloo owed to Annopol as of June 28, 2010, the date of SG Waterloo's bankruptcy.

[6] Annopol originally filed its proof of claim for $519,600, which had been paid in small instalments from June 2000 to December 2008, rather than in a lump sum. Farber was later able to retrieve documents that conclusively established that the amount advanced was actually $557,600. It also filed a report to that effect. $100,000 of this amount was secured and the remaining $457,600 was unsecured.

[7] The trial judge described Annopol as having filed a proof of claim for an unsecured amount of $420,000 and a secured amount of $100,000, for a total of $520,000. Accordingly, he allowed the unsecured claim in the amount of $420,000, rather than $457,600. He also awarded interest calculated at 5% per annum from December 4, 2008, which was the date of the final recorded advance from Annopol to SG Waterloo.

### (ii) Farber's Submissions on Appeal

[8] Farber opposes the trial judge's decision on two grounds. First, it submits that the trial judge erred in awarding Annopol $420,000 instead of $457,600. Farber argues that there is no explanation as to why Annopol's claim for

$457,600 was not allowed given the trial judge's finding that it had loaned $457,600 to SG Waterloo.

[9] Second, Farber submits that the trial judge erred in ordering interest on the entire sum from December 4, 2008 – the date of Annopol's last proven advance. It submits that interest should run from the dates of the individual advances. Farber acknowledges that the trial judge's decision was discretionary, but argues that he had to exercise his discretion with regard to the evidence and proper considerations. On this point, Farber asserts that the trial judge gave no explanation for his selection of December 4, 2008 as the interest commencement date and the only available evidence on the issue of interest did not support his decision.

**(iii) Analysis**

[10] The record clearly supports Farber's position that the correct quantum of the unsecured debt is $457,600. Moreover, Goldfinger does not seriously object to the fact that the $420,000 finding was in error.

[11] I would therefore allow this portion of Farber's appeal, in its capacity as Annopol's Trustee in bankruptcy, and vary the February 3, 2014 judgment to allow Annopol's unsecured claim against SG Waterloo at $457,600.

[12] Turning to the ground of appeal relating to the calculation of interest on the unsecured claim, the evidence on interest payable was limited. Unlike the

secured claim, there was no documentary evidence governing the calculation of interest with respect to the unsecured claim. That said, Annopol did make multiple advances between 2000 and 2008 to SG Waterloo.



[13] Interest compensates for the use or retention by one person of a sum of money belonging to another which accrues day by day: see *Garland v. Consumers' Gas Co.*, [1998] 3 S.C.R. 112, at para. 27. It follows that in the absence of evidence to the contrary, interest should accrue from the date of each individual advance, not from the date of the last advance.

[14] I would therefore also allow Farber's appeal with respect to interest and vary the February 3, 2014 judgment so that interest is calculated by the parties from the date of each advance by Annopol to SG Waterloo.

## B. SG Group's Claims in SG Waterloo's Bankruptcy

### (i) Background

[15] The second part of Farber's appeal is made in its capacity as Trustee in bankruptcy of SG Group in the SG Waterloo bankruptcy. Farber appeals the trial judge's partial disallowance of certain claims advanced by Farber and his interest award.

[16] SG Waterloo owned development property located at 105 University Avenue in Waterloo, Ontario. Farber claimed that SG Group had made payments

to a number of third parties on behalf of SG Waterloo and that therefore SG Waterloo was unjustly enriched to SG Group's detriment.

[17] First, Farber asserted that SG Group had paid $346,029.13 to Joe Somfay Architects on behalf of SG Waterloo and filed a proof of claim including that amount. In support of that portion of its claim, Farber simply filed a summary of invoices, credit notes and payments that had been prepared by Somfay. In his reasons dated October 28, 2013, the trial judge concluded that Farber had filed insufficient particulars of these alleged payments. He accordingly provided Farber with an opportunity to file additional evidence of payment.

[18] In his reasons dated February 3, 2014, having received and reviewed Farber's additional evidence, the trial judge allowed $236,249 of SG Group's claim, but disallowed the remaining $109,780.13 due to inadequate evidence.

[19] He also rejected the interpretation, urged upon him by Farber, of an August 7, 2002 letter from Somfay, allegedly reflecting a payment of $108,531. He concluded that the letter did not reflect confirmation of receipt of the amount of $108,531. Rather, it represented an offer of a discount in that amount. In addition, the trial judge reasoned that if Somfay had received payment of $108,531 prior to the August 7, 2002 letter, it was difficult to understand why invoices from 2000 would continue to be outstanding at that time. The trial judge

also observed that Farber had been given more time to file additional evidence and that it could have filed an affidavit from Somfay but failed to do so.

[20] Second, Farber asserted that SG Group paid operating expenses of $104,855 for SG Waterloo's 105 University Avenue property and, as a result, SG Waterloo was unjustly enriched to the detriment of SG Group.

[21] Before the trial judge, Farber successfully established that SG Group had paid some of SG Waterloo's operating costs. However, while it produced invoices totalling $104,855 rendered for work done at 105 University Avenue, it could not locate any evidence establishing that these amounts had been paid. Farber urged the trial judge to draw an inference that these additional amounts had been paid, but the trial judge declined to do so. He was not satisfied with the sufficiency of the evidence and explained that SG Waterloo went into bankruptcy in part because of its inability to pay all its obligations. In rejecting the claim, he acknowledged that Farber found the Summit Glen companies' books and records in a state of disarray and noted that Farber was not responsible for the absence of the required evidence. However he rejected Farber's additional claim of $104,855.

[22] Third, Farber claimed interest on the total amount of $625,368.88, which is the sum that the trial judge ordered in SG Group's favour.

[23] The trial judge held that, because Farber's claim on behalf of SG Group sounded in unjust enrichment and was not based on a loan agreement, s. 3 of the *Interest Act*, R.S.C. 1985, c. I-15, did not apply. He therefore awarded interest on the sum of $625,368.88 in accordance with the prejudgment interest provisions of the *Courts of Justice Act*, R.S.O. 1990, c. C.43.

[24] He ordered the interest to be payable from June 28, 2010 – the date of SG Waterloo's bankruptcy. The trial judge reasoned that interest should be calculated from the date of bankruptcy, which was the date upon which the deprivation underpinning the cause of action for unjust enrichment occurred.

**(ii) Farber's Submissions on Appeal**

[25] Farber submits that the trial judge erred in law in requiring that it establish with certainty that SG Group paid the sum of $109,780.13 to Somfay and $104,855 to SG Waterloo's other suppliers. It submits that this was too high a threshold. It argues that the trial judge ignored concessions made by Goldfinger, failed to properly consider the lack of documentary evidence available to Farber, including records outside of Farber's control, and failed to give proper weight to the evidence. In particular, it submits that the trial judge erred by misinterpreting the August 2002 letter from Somfay and by concluding that invoices from 2000 continued to be outstanding in 2002.

[26] Farber also argues that the trial judge erred in calculating interest on the basis of the *Courts of Justice Act*, rather than the *Interest Act*. However, Farber concedes that the trial judge erred in concluding that interest ran from the date of SG Waterloo's bankruptcy. Indeed, Farber did not seek such interest. Although it initially submitted that interest should be awarded from December 1, 2008 (the date SG Waterloo's receiver was appointed) to June 28, 2010 (the date of SG Waterloo's bankruptcy), in oral argument, Farber did not press this point.



**(iii) Analysis**

[27] I do not accept Farber's submissions relating to the Somfay and operating cost claims. First, the trial judge did not apply a standard of certainty. Starting at para. 35 of his October 28, 2013 reasons, he reviewed the law applicable to proof of claims.

[28] The trial judge cited *South Beach Homes Ltd. (Re)*, 2010 SKQB 182, 357 Sask.R. 82 – the same decision Farber relies on as establishing the test to admit a claim. At para. 46 of *South Beach*, the court expressly noted that certainty is not the test. Then, in the trial judge's February 3, 2014 reasons, he applied the test he had already articulated in his earlier reasons.

[29] The trial judge applied the correct test, but he was not persuaded that it was met either with respect to the sum of $109,780.13 or the sum of $104,855. He expressly considered Goldfinger's position, the state of the documentary

record and, in the case of the Somfay payments, the terms of the August 2002 letter. His findings of fact, which supported his conclusion, are both within the province of a trial judge and, based on the record, reasonable.

[30] I see no error in the trial judge's denial of these two claims advanced by SG Group. Accordingly, I would also dismiss this part of Farber's appeal.

[31] As for Farber's submission that the trial judge erred in concluding that the *Interest Act* was inapplicable, I see no basis on which to disturb the trial judge's conclusion. Farber had advanced a claim for unjust enrichment and, in any event, the trial judge rejected its contention that the amount paid by SG Group for SG Waterloo's benefit constituted a contingent loan. The trial judge's determination that interest was properly payable under the provisions of the *Courts of Justice Act* rather than the *Interest Act* was reasonable. I would dismiss this part of the appeal.

[32] Lastly, I agree with Farber's concession that interest does not run after the date of bankruptcy. As I have already said, Farber did not press the argument that interest ran from the date of the receivership.

[33] In the circumstances, I would therefore allow the appeal in part so as to allow interest up to December 1, 2008, the date of SG Waterloo's receivership.

## C. Cross-Appeal: 183's Claim in SG Waterloo's Bankruptcy

[34] In the companion appeal (C57898), I concluded that the release signed in 2009 was designed to result in finality and to release any future claim Goldfinger, and by extension 183, had against SG Waterloo. Accordingly, I further concluded that 183 had given up any claim to the proceeds from the sale of 105 University Avenue. That includes both the principal claim, dealt with in the companion appeal, as well as the expenses associated with the principal claim, the subject of this cross-appeal.

[35] Accordingly, I would dismiss the cross-appeal.

## Disposition

[36] In summary, I would:

(1) allow Farber's appeal in its capacity as Trustee in bankruptcy of Annopol and amend paragraph 1 of the February 3, 2014 judgment to replace the sum of $420,000 with the sum of $457,600 with interest calculated from the date of each individual advance;

(2) dismiss Farber's appeal in its capacity as Trustee in bankruptcy of SG Group with respect to the $109,780.13 Somfay expense claim and the $104,855 operating expense claim;

(3) allow Farber's appeal in its capacity as Trustee in bankruptcy of SG Group and amend paragraph 2 of the February 3, 2014 judgment to replace the words "from June 28, 2010" with the words "to the date of December 1, 2008"; and

(4) dismiss the cross-appeal of 183.

[37] As agreed by the parties, I would order Farber to pay Goldfinger $3,000 in respect of the costs of the appeal, and 183 to pay Farber $5,000 in costs concerning the cross-appeal, both inclusive of disbursements and applicable taxes.

Released:

“MAY 30 2016” “S.E. Pepall J.A.”

“EAC” “I agree E.A. Cronk J.A.”

“I agree P. Lauwers J.A.”

**Bankruptcy and Insolvency Law of Canada, 4th Edition § 1:8**

**Bankruptcy and Insolvency Law of Canada, 4th Edition**
The Honourable Mr. Justice Lloyd W. Houlden, Mr. Justice Geoffrey B. Morawetz, Dr. Janis P. Sarra

**Part I. The Bankruptcy and Insolvency Act**

**Chapter 1. General; Short Title (S. 1)**

**II. Short Title (S. 1)**

## § 1:8. Interpretation of Bankruptcy and Insolvency Legislation

The Supreme Court of Canada has held that the starting point for statutory interpretation in Canada is Driedger's definitive formulation in *Construction of Statutes* (2nd ed. 1982) at p. 87:

> Today there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act and the intention of Parliament.

Barrie Public Utilities v. Canadian Cable Television Assn. (2003), 2003 CarswellNat 1226, 2003 CarswellNat 1268, 2003 SCC 28, [2003] 1 S.C.R. 476.

English and French versions of the *BIA* are equally authoritative. Where the meaning of the words in one version are broader than the meaning in the other version, the court must strive to find a meaning that is shared by both versions: Schreiber v. Canada (Attorney General) (2001), 2001 CarswellOnt 385, 52 O.R. (3d) 577, 152 C.C.C. (3d) 205, 196 D.L.R. (4th) 281 (C.A.).

The Act should not be interpreted in an overly narrow, legalistic manner: A. Marquette & Fils Inc. v. Mercure, [1977] 1 S.C.R. 547, 65 D.L.R. (3d) 136, 10 N.R. 239; Re Olympia & York Developments Ltd. (1997), 1997 CarswellOnt 657, 45 C.B.R. (3d) 85, 143 D.L.R. (4th) 536 (Ont. Gen. Div.); Sun Life Assurance Co. of Canada v. Revenue Canada (Taxation), 1997 CarswellAlta 254, 45 C.B.R. (3d) 1, 47 Alta. L.R. (3d) 296, [1997] 5 W.W.R. 159, 144 D.L.R. (4th) 653 (C.A.); Re County Trucking Ltd. (1999), 1999 CarswellNS 231, 10 C.B.R. (4th) 124 (N.S. S.C.). It should be given a reasonable interpretation that supports the framework of the legislation; an absurd result should be avoided: Re Handelman (1997), 1997 CarswellOnt 2891, 48 C.B.R. (3d) 29 (Ont. Gen. Div.).

 

The Act puts day-to-day administration into the hands of trustees in bankruptcy and inspectors as business people and professionals; it is intended that the administration should be practical not legalistic, and the Act should be interpreted to give effect to this intent: Re Rassell (1999), 1999 CarswellAlta 718, 12 C.B.R. (4th) 316, 177 D.L.R. (4th) 396, 71 Alta. L.R. (3d) 85, 237 A.R. 136, 197 W.A.C. 136 (C.A.).

The sections of a statute must be interpreted so that they are in harmony and are not inconsistent, if such an interpretation is possible: Re Goldin (2002), 2002 CarswellOnt 2037, 34 C.B.R. (4th) 196 (Ont. S.C.J.), appeal dismissed (2003), 229 D.L.R. (4th) 736, 2003 CarswellOnt 2626, 174 O.A.C. 117 (Ont. C.A.).

Where a statutory provision is expressed to be "subject to" another statutory provision, the latter provision (the master provision) prevails over the former (the subject provision) if there is any conflict between them: Re A Debtor (No. 22 of 1993), [1994] 1 W.L.R. 47 (Ch.D.); Warran Whillans Enterprises Inc. (Trustee of) v. Gazzola (1989), 75 C.B.R. (N.S.) 151, 1989 CarswellBC 354, 38 B.C.L.R. (2d) 27, 4 R.P.R. (2d) 153, [1989] 5 W.W.R. 740, 60 D.L.R. (4th) 590 (*sub nom. Thome Ernst & Whinney Inc. v. Gazzola*); Canadian Imperial Bank of Commerce v. Canotek Development Corp. (1993), 13 O.R. (3d) 411, 1993 CarswellOnt 1045 (Gen. Div.), reversed on other grounds but affirmed on this ground (1997), 35 O.R. (3d) 247, 48 C.B.R. (3d) 161, 1997 CarswellOnt 3216, 152 D.L.R. (4th) 261 (C.A.).

Where two interpretations of the Act are equally possible, the court should select the interpretation that favours equality among creditors, possessing the same characteristics, rather than the one that favours a particular group of creditors: Re Can. Tabulating Card Co., 17 C.B.R. (N.S.) 248, [1972] 3 O.R. 648, 1972 CarswellOnt 83, 29 D.L.R. (3d) 156; Re Olympia & York Developments Ltd. (1997), 143 D.L.R. (4th) 536, 1997 CarswellOnt 657, 45 C.B.R. (3d) 85 (Ont. Gen. Div.).

A judge is not required to follow the decision of the courts of another province on the interpretation of a federal statute unless he or she is persuaded of the correctness of the decision: Sigurdson v. Reid (1979), 32 C.B.R. (N.S.) 170, 17 B.C.L.R. 117, reversed on other grounds (1980), 37 C.B.R. (N.S.) 146, 26 B.C.L.R. 336, 118 D.L.R. (3d) 555 (B.C. C.A.). Likewise, an appellate court is not obliged to follow the decisions of an appellate court of another province. Such decisions act only as persuasive authority: Reznick v. Zitzerman (1994), 28 C.B.R. (3d) 234, 1994 CarswellMan 18 (Man. C.A.). However, the *Bankruptcy and Insolvency Act* is a federal statute and should, therefore, as far as possible, be interpreted consistently in each of the provinces and territories in Canada: Re County Trucking Ltd. (1999), 10 C.B.R. (4th) 124, 1999 CarswellNS 231 (N.S. S.C.).

In order to obtain uniformity of practice in bankruptcy matters in all of the provinces, a literal following of the letter of the Act should not be adopted where the intent of the Act is clear: Re Drysdale Estate, 19 C.B.R. 324, [1938] 3 W.W.R. 57, 53 B.C.R. 155 (B.C. S.C.).

 

A statute has full operation on the whole day it comes into force, whatever the hour of the day that sanction was given to it. The fact that certain events took place at an hour prior to the hour when the statute was passed into law is therefore of no relevance: Re Plywood Distributors Inc. (1966), 10 C.B.R. (N.S.) 22 (Que. S.C.).

If an amending Act alters the language of the principal Act, the alteration must be taken to have been made deliberately: Langille v. T.D. Bank (1981), 43 N.S.R. (2d) 608, 37 C.B.R. (N.S.) 35, 81 A.P.R. 608, affirmed 40 C.B.R. (N.S.) 113, 50 N.S.R. (2d) 217, 98 A.P.R. 217, 131 D.L.R. (3d) 571, 40 N.R. 67 (S.C.C).

When there is a bankruptcy, the rules established by the *Bankruptcy and Insolvency Act* will govern except where other legislation clearly creates an exception to those rules. The burden of proof that such an exception is created rests on the party who asserts its existence; and, if there is any doubt, the substance of the legislation, not the form, will govern and the doubt will be resolved against the person asserting it: Re Nolisair International Inc. (1966), 44 C.B.R. (3d) 112, 1996 CarswellQue 599, [1996] R.J.Q. 776 (C.S.).

Although there is a general rule that the legislative history of an enactment is not admissible in the interpretation of a statute, legislative history can be helpful in particular circumstances. In Reed v. Franco (1980), 35 C.B.R. (N.S.) 149, 1980 CarswellQue 54, [1980] C.S. 391 (Que. S.C.), appeal dismissed (1983), 49 C.B.R. (N.S.) 21, 1983 CarswellQue 41 (Que. C.A.); U.F.C.W., Local 617P v. Royal Dressed Meats Inc. (Trustee of) (1989), 76 C.B.R. (N.S.) 79, 1989 CarswellOnt 180, 37 C.P.C. (2d) 154 (Ont. S.C.).

The substantive rights of creditors are determined in accordance with the provisions of the *Bankruptcy and Insolvency Act* as it stood at the date of bankruptcy: Albert v. Canada (Human Resources Development) (2002), 39 C.B.R. (4th) 1, 2002 CarswellNB 478, 2002 NBQB 400 (N.B.Q.B.).

Where a section of the *Bankruptcy and Insolvency Act* is revoked or repealed and a new section substituted, the rights of creditors in a bankrupt estate that is in the course of administration, are to be determined so far as substantive rights are concerned in accordance with the former section, and so far as procedural rights are concerned in accordance with the new section: Re Mahon (1935), 16 C.B.R. 132, 1934 CarswellNS 3, [1935] 1 D.L.R. 416 (N.S. S.C.); Transamerica Commercial Finance Corp., Canada v. Imperial T.V. & Stereo Centre Ltd. (Receiver of) (1993), 22 C.B.R. (3d) 297, 1993 CarswellAlta 429, 13 Alta. L.R. (3d) 99, [1994] 1 W.W.R. 506 (Q.B.). Unless there is a clear intention that an amendment to the *Bankruptcy and Insolvency Act* shall operate retrospectively, manifested by express words or arising by necessary and direct implication, a substantive amendment should be viewed as operating prospectively only: Bank of Nova Scotia v. Plastic & Allied Building Products Ltd. (1992), 15 C.B.R. (3d) 161, 1992 CarswellOnt 191, [1993] O.J. No. 2655 (Ont. Gen. Div. [Commerical List]).

 

Unless the text reveals a contradiction or inconsistency that cannot be avoided without employing a strained and unrealistic construction, the *BIA* should be interpreted in a manner that respects its integrity. A specific provision concerning the procedure to be followed in a particular aspect of the administration of an estate, such as s. 135, which provides for appeals from disallowance of claims by a trustee, prevail over a general section, such as s. 37, which provides for the review of trustee's decisions: Re Drummie (2004), 49 C.B.R. (4th) 90, 2004 CarswellNB 17, 2004 NBQB 35 (N.B. Q.B.).

Mere verbal inaccuracies or errors in the use of words, numbers, grammar, punctuation or spelling will be corrected by the court whenever necessary to carry out the intention of Parliament as gathered from the entire *Bankruptcy and Insolvency Act.* Hence if a section of the Act refers to another section by the wrong number and if the legislative intent is clear, the court will correct the error: Re Ferguson, 16 C.B.R. 261, 1935 CarswellOnt 83, [1935] O.R. 223, [1935] 2 D.L.R. 473 (S.C.).

The amendments to the *Bankruptcy and Insolvency Act* in 1992 brought it more into line with the United States *Bankruptcy Code.* American jurisprudence and authorities in bankruptcy matters are, therefore, of assistance in interpreting the *Bankruptcy and Insolvency Act:* Re A. & F. Baillargeon Express Inc. (1993), 27 C.B.R. (3d) 36, 1993 CarswellQue 49 (Que. S.C.).

For a discussion of the principles of statutory interpretation to be applied where the provisions of two statutes appear to be in conflict, see "Case Commentary on *Re Solid Resources Ltd.*" by Jamie Feehely, 40 C.B.R. (4th) 238.

See also Michael J. Bray and Micheline Gleixner, "Differing Climates of Bankruptcy: A Question of Latitude?", in J. Sarra, ed., Annual Review of Insolvency Law, 2011 (Toronto: Carswell, 2012) 281–312; Stephanie Ben-Ishai and Saul Schwartz, "Debtor Assistance and Debt Advice: The Role of the Canadian Credit Counselling Industry" and Jerry Buckland, "A Commentary on the Canadian Task Force on Financial Literacy's Recommendations", in J. Sarra, ed., Annual Review of Insolvency Law, 2011 (Toronto: Carswell, 2012) 351–408; Janis Sarra, "At What Cost? Access to Consumer Credit in a Post-Financial Crisis Canada", Annual Review of Insolvency Law, 2011 (Toronto: Carswell, 2012) 409–478; Paul Goodman and Anna Lund, "Concerns of Insolvency Professionals—Small and Medium Size Enterprises", in J. Sarra, ed., Annual Review of Insolvency Law, 2011 (Toronto: Carswell, 2012) 191–206.



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ESSENTIALS OF CANADIAN LAW

# BANKRUPTCY AND INSOLVENCY LAW

SECOND EDITION

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place the administrative apparatus of the restructuring process. The danger was that considerable costs could be incurred before creditors were notified and afforded the opportunity to object. The second was that the judge hearing the application was faced with a complex document with very little time to review its provisions to ensure that they were not excessive or unusual in comparison with orders normally granted in similar circumstances.

Justice Blair expressed concern over these matters in *Re Royal Oak Mines Inc.*[74] He was of the opinion that the provisions contained in the initial order should be limited to those that are "reasonably necessary for the continued operation of the debtor company during a brief but realistic period of time, on an urgency basis."[75] This principle of minimizing the scope and effect of the order is captured in the idea that the order should be limited to what is necessary to "keep the lights on" until the creditors have had an opportunity to consider their position and prepare their response.

One response to these problems has been the creation of template *CCAA* initial orders in Ontario, Quebec, Alberta, British Columbia, and Saskatchewan. These are intended to provide guidance to counsel and to promote the standardization of *CCAA* provisions.

## 5) The Role of the Appellate Courts

The real-time nature of restructuring proceedings also has significant implications in respect of the role of the appellate courts in reviewing the decisions of the supervising court. Because the restructuring proceedings are ongoing, an appeal has the potential to delay them and thereby endanger their success. The appellate courts have responded to this problem in two ways. First, they have expedited the appeal process in order to minimize the delay associated with the appeal. Secondly, they have expressed a reluctance to interfere with the exercise of discretion by the supervising court. The appellate courts have recognized that the supervising judge is in the best position to balance the competing factors at play in the restructuring proceedings.[76]

In determining whether to grant leave to appeal, there must be serious and arguable grounds that are of real and significant interest to the parties. In making this determination, the appellate court will consider the following four factors: (1) whether the point on appeal is of signifi-

74 *Ibid.*

75 *Ibid* at para 21.

76 *Re Doman Industries Ltd* (2004), 2 CBR (5th) 141 (BCCA).

cance to the practice; (2) whether the point raised is of significance to the action itself; (3) whether the appeal is *prima facie* meritorious or frivolous; and (4) whether the appeal will unduly hinder the progress of the action.[77]

Appellate courts are generally unwilling to intervene where the controversy concerns the weight or degree of importance to be given to particular factors. They have taken the view that the supervising judge makes discretionary decisions in a constantly changing environment and therefore these decisions should be afforded a high degree of deference.[78] However, they are prepared to intervene if the supervising court has failed to apply correct principles.[79]

An appellate court may also refuse to allow an appeal to be heard on the ground that the matter is moot because no merit, substance, or prospective benefit will accrue to the appellant.[80] This may be invoked where it is impossible to "unscramble the egg" because DIP financing has already been extended and used to pay suppliers and employees[81] or if essential elements of the plan have been implemented and are now irreversible.[82]

## D. THE ROLE OF THE CREDITORS

### 1) Creditor Bargaining, Litigation, and Approval

The creditors play a less direct role in the governance of business during the restructuring proceedings. Their proceedings and remedies are stayed until such time as they vote on the plan. Yet, despite an absence of a direct governance role, the creditors can strongly influence the direction of the restructuring through bargaining, through the use of actual or threatened litigation, and through voting on the plan. In extreme cases, creditors may bring application to terminate the restructuring proceedings or to lift the stay of proceedings. They may also attempt to block some action proposed by the debtor company, such as a disclaimer of a contract or a sale of assets outside the ordinary course of business. Finally, the creditors may threaten to vote against the plan if their concerns are not met.

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77 *Re Canadian Airlines Corp* (2000), 20 CBR (4th) 46 (Alta CA).
78 *Canada v Temple City Housing Inc*, 2008 ABCA 1.
79 *Re New Skeena Forest Products Inc* (2005), 9 CBR (5th) 278 (BCCA).
80 *Re Canadian Airlines Corp*, above note 77.
81 *Canada v Temple City Housing Inc*, above note 78.
82 *Re Canadian Airlines Corp*, above note 77.

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27 — It All Began With Galaxy: Appeals and Trials De Novo in Insolvency Revisited

## It All Began With Galaxy: Appeals and Trials De Novo in Insolvency Revisited

*Louise Lalonde* [*]

### I. — Introduction

There are perhaps few areas in bankruptcy in recent years that have given rise to as many conflicting decisions as appeals from trustees' decisions in matters involving disallowance of creditors' claims and particularly the issues of whether such appeals are "true" appeals or appeals *de novo*, and thus, whether evidence, fresh or new, should be admitted, and what is the applicable standard of review.

Yet it seems that not so long ago it was taken for granted by many that if a trustee disallowed a proof of claim, the creditor could appeal to the court sitting in bankruptcy (either the registrar or the judge thereof) and that the case would proceed on a *de novo* basis and that both the creditor and the trustee generally had the right to adduce *viva voce* evidence and any documentary or other evidence required. [2] Neither party was limited to the proof of claim filed and the evidence submitted by the creditor to the trustee, or any other evidence relied upon by the latter, and the proceedings were generally considered "adversarial", although today the trustee is sometimes viewed as being "neutral" as an administrative official. While the trustee's decision was deserving of respect, the court did not grant any particular deference to the trustee's decision and was free to substitute its own discretion.

Today, the trustee is viewed as a decision-maker, even considered by some as rendering "quasi-judicial decisions", [3] as in administrative law matters, who must be afforded deference. Accordingly, the appeal is considered to be a "true" appeal, on the record, where no fresh evidence may be adduced as a matter of course. The creditor in essence is bound by the information provided to the trustee, although the evidence before the court hearing the appeal may possibly extend to other information reviewed by the trustee. The right to adduce new evidence, in principle, should meet the usual criteria for the admission of fresh evidence on an appeal, with many decisions applying the criteria set forth in *R v Palmer* [4] ("*Palmer* criteria") and in particular that the evidence will not be admitted if by due diligence it could have been adduced at trial, in this case, before the trustee's determination.

What happened to get us to this point? Well, it all apparently began with the British Columbia Court of Appeal's decision in *Re Galaxy Sports Inc*, [5] where in a thoughtful analysis, the Court held that in its view the hearing of an appeal under s. 135(4) of the *Bankruptcy and Insolvency Act (BIA)* [6] from disallowance of claims by the trustees is not intended to be a trial *de novo* but a true appeal. The Court further held that the applicable standard of review is a correctness standard when dealing with the trustee's decision disallowing a proof of claim and a reasonableness standard where the determination involves valuing contingent and unliquidated claims pursuant to s. 135(1.1) of the *BIA*.

As to the nature of the appeal, the Court's determination was based primarily on three grounds. One of the grounds was based on the law of British Columbia, where according to the Court of Appeal it is clear that unless the statute that provides for an appeal also states that it is to take the form of a trial *de novo*, the appeal will be an ordinary appeal. Another ground was based upon a contextual analysis of the *BIA* framework and purpose of the legislation, the Court stating that if fresh evidence were to be adduced in the court hearing the appeal as a matter of course, much would be lost in the way of efficiency in the operation that the trustee, within the timeframe specified in the provisions, shall either admit the claim and deliver possession of the property to the claimant or send a notice to the claimant that the claim is disputed, with the trustee's reasons for disputing it. It further provides that unless the claimant appeals the trustee's decision to the court within 15 days after the sending of the notice of dispute, the claimant is deemed to have abandoned or relinquished all his or her right to or interest in the property to the trustee who may then sell or dispose of the property free of any right, title or interest of the claimant.

***iii. — Section 108 meeting of creditors***

Regarding the right to vote at meetings of creditors, s. 108 of the *BIA* provides that the chair of any meeting of creditors has the power to admit or reject a proof of claim for the purpose of voting but the decision is subject to appeal to the court. Subsection 108(3) of the *BIA* further provides that where the chair is in doubt as to whether a proof of claim should be admitted or rejected, he shall mark the proof as objected to and allow the creditor to vote, subject to the vote being declared invalid in the event of the objection being sustained.

***iv. — Section 135 determinations, disallowances and applications to expunge***

Section 135 of the *BIA* sets forth the process for the admission and disallowance of proofs of claim and proof of security. It provides that the trustee shall examine the proof of claim or proof of security and the grounds therefore and may require further evidence in support of the claim or security. The trustee shall also determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it. Thereafter, the claim will be deemed a proved claim to the amount of its valuation (s. 135(1.1) of the *BIA*). Prior to the 1997 amendments, s. 121(2) of the *BIA* provided that it was the court that determined whether a contingent or unliquidated claim was a provable claim and, if provable, valued it. In 1997, the provision was amended and now provides that this determination will be made by the trustee.

Subsection 135(2) of the *BIA* deals with the right of the trustee to disallow any claim or any right to priority or security in whole or in part. Prior to the 1992 amendments, the trustee was not entitled to dispute the validity of the security by way of a notice of disallowance, but had to proceed by way of a direct proceeding. Subsection 135(3) of the *BIA* provides a requirement for the trustee to give notice where the trustee 1) makes a determination under subsection (1.1) (as to whether a contingent or unliquidated claim is a provable claim and if a provable claim, the value thereof); or 2) pursuant to subsection (2), disallows in whole or in part, any claim, the right to a priority or any security. Subsection 135(3) of the *BIA* requires that the trustee provide in the prescribed form a notice to the claimant setting out the reasons for the determination or the disallowance. Subsection 135(4) of the BIA provides the following with respect the disallowance or determination:

> A determination under subsection (1.1) or a disallowance referred to in subsection (2) is final and conclusive unless, within a thirty day period after the service of the notice referred to in subsection (3) or such further time as the court may on application made within that period allow, the person to whom the notice was provided appeals from the trustee's decision to the court in accordance with the General Rules.

Finally, subsection 135(5) of the *BIA* provides that the court may expunge or reduce a proof of claim or a proof of security on the application of a creditor or of the debtor if the trustee declines to interfere in the matter. Historically, this provision has been viewed as "appeal" from admissions of proofs of claim by the trustee. Indeed, s. 135(4) deals with the creditor's remedy where it is dissatisfied with the disallowance of its claim, whereas s. 135(5) deals with the situation where other creditors are dissatisfied with either the failure of the trustee to make a decision with respect to the proof of claim of another creditor or, more often, with the decision of the trustee to admit a claim.

***v. — Outline of the review***

The bankruptcy case law review will be divided into three parts: the first part deals with authorities prior to *Galaxy*, the second deals with the *Galaxy* decision, and the third with the authorities subsequent to *Galaxy*. The first and third parts are further divided based upon whether the decisions adopt or follow the true appeal line of cases or the *de novo* line, and the third part contains an additional division where the decisions follow a "hybrid" line. [38] While generally these categories are clear, some of the cases could have been placed in another, depending on the perspective of the person making the determination. For

 

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| .IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF<br>YG LIMITED PARTNERSHIP AND YSL RESIDENCES INC.<br>OF THE CITY OF TORONTO, IN THE PROVINCE OF ONTARIO | Court File No.: BK-21-02734090-0031<br>Court of Appeal No. COA-22-CV-0451 |

**Court of Appeal for Ontario**

IN THE MATTER OF THE BANKRPUTCY AND INSOLVENCY ACT, R.S.C. 1985, C. B-3 AS AMENDED

**BOOK OF AUTHORITIES OF THE PROPOSAL TRUSTEE**


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