Court File No. 31-2303814
Estate No. 31-2303814

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

IN BANKRUPTCY AND INSOLVENCY

IN THE MATTER OF THE PROPOSAL OF 1482241 ONTARIO LIMITED, OF THE CITY OF TORONTO, IN THE PROVINCE OF ONTARIO

BRIEF OF AUTHORITIES OF THE PROPOSAL TRUSTEE
(motion returnable March 28, 2018)

Date: March 22, 2018

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TAB 1

1993 CarswellOnt 614
Ontario Court of Appeal

Mastercraft Properties Ltd. v. EL EF Investments Inc.

1993 CarswellOnt 614, [1993] O.J. No. 1704, 103 D.L.R. (4th) 759, 14 O.R. (3d) 519, 32 R.P.R. (2d) 312, 41 A.C.W.S. (3d) 886, 64 O.A.C. 308

MASTERCRAFT PROPERTIES LIMITED, MEGA DEVELOPMENT CORPORATION and SEPAM LIMITED, carrying on business as the CONSERVATORY PARTNERSHIP v. EL EF INVESTMENTS INC.

Re Mortgages Act, R.S.O. 1980, Chapter 296, Section 11, as amended from time to time; Re Interest Act, R.S.C. 1985, Chapter I-15

PEACE VALLEY RANCH LIMITED v. COCONUT GROVE MANAGEMENT & DEVELOPMENT CORP., THE HELMSLEY MANAGEMENT & DEVELOPMENT CORP., 767648 ONTARIO LIMITED and 630662 ONTARIO LIMITED

Lacourcière, McKinlay and Austin JJ.A.

Heard: January 20, 1993
Judgment: July 20, 1993
Docket: Docs. CA C9811 and C11163

Counsel: *Nina Perfetto*, for appellants Mastercraft Properties Limited, Mega Development Corporation and Sepam Limited, carrying on business as the Conservatory Partnership.
Sherman W. Hans, Q.C., for appellants Coconut Grove Management & Development Corp., The Helmsley Management & Development Corp., 767648 Ontario Limited and 630662 Ontario Limited.
Michael Rankin, for respondent EL EF Investments Inc.
J. James Wardlaw, for respondent Peace Valley Ranch Limited.

Subject: Property; Corporate and Commercial
Related Abridgment Classifications
Real property
VII Mortgages
VII.6 Interest
VII.6.e Penalty or increased interest on default
Real property
VII Mortgages
VII.6 Interest
VII.6.h Miscellaneous
Headnote
Mortgages --- Interest
Mortgages --- Interest — Penalty or increased interest on default
Mortgages — Interest — Bonuses — Mortgage covenants providing for bonus payments of three months' interest on default — Covenants not contravening s. 8 of Interest Act — Bonus not constituting fine, penalty or rate of interest — Interest Act, R.S.C. 1985, c. I-18, s. 8.

Mortgages — Payment and discharge of mortgage — Payment during default — Section 16 of Mortgages Act constituting valid provincial legislation — Section 16 not being in conflict with s. 8 of Interest Act — Interest Act, R.S.C. 1985, c. I-18, s. 8 — Mortgages Act, R.S.O. 1980, c. 296, s. 16.

Two mortgages contained similar covenants on the part of the mortgagors. The covenants provided that, following default under the mortgages, the mortgagors could not require that the mortgagees accept payment of the principal outstanding without first giving three months' previous notice in writing or paying a bonus in lieu thereof. Contradictory decisions were rendered in the lower court rulings where, in the first action, the covenant was held enforceable while, in the second action, the covenant was found to be unenforceable pursuant to s. 8 of the *Interest Act* (Can.). At issue on the appeals was whether s. 8 of the *Interest Act*, which prohibits the payment of a fine, penalty or rate of interest on arrears of principal or interest which increases the charge on the arrears beyond the rate of interest payable under the mortgage, precludes the enforcement of the covenants in each case. Also at issue was whether s. 16 of the *Mortgages Act* (Ont.) is in conflict with s. 8 of the *Interest Act*.

Held:

The appeal in the first action was dismissed and that in the second action was allowed.

The covenants were valid and enforceable, and s. 16 of the *Mortgages Act* was constitutionally valid.

To contravene s. 8 of the *Interest Act*, a mortgage provision must both stipulate for a fine, penalty or rate of interest and have the prohibited effect of increasing the interest rate. In the subject covenants, the payment in question was referred to as a "bonus," which is not expressly prohibited by s. 8. The "bonus" was not an amount being paid in punishment for a breach of the mortgage agreement, but constituted a payment required for the privilege of paying mortgage arrears without the necessity of giving the three months' notice. Had the covenants required the payment of interest during the notice period plus an additional amount equivalent to three months' interest, then this would clearly have been contrary to s. 8. The "bonus" also did not constitute a "rate of interest" charged on "arrears of principal and interest."

Section 16 of the *Mortgages Act* provides a mortgagor with the right, when in default of payment of principal, to repay the principal upon the giving of three months' notice to the mortgagee of his intention to pay. The provision also protects the mortgagor from any further payment of interest except to the date of payment. Section 16 of the provincial statute does not conflict with s. 8 of the *Interest Act*; both enactments are constitutionally valid.

Table of Authorities

Cases considered:

Adams Properties Ltd. v. Sherwood Estates Ltd. (1976), 144 D.L.R. (3d) 562 (B.C. C.A.) — *applied*

Glinert v. Kosztowniak, [1972] 2 O.R. 284, 25 D.L.R. (3d) 390 (Master) — *referred to*

Gullett v. Income Trust Co. (1985), 37 R.P.R. 123, 11 O.A.C. 178 (C.A.) — *applied*

Parkhill v. Moher (1977), 17 O.R. (2d) 543, 80 D.L.R. (3d) 754, 3 R.P.R. 26, 1977 CarswellOnt 432 (Ont. H.C.) — referred to

Schwartz v. Williams (1915), 35 O.L.R. 33, 27 D.L.R. 733 (H.C.) — *referred to*

Tapio v. Kajander (1964), [1965] 1 O.R. 431, 48 D.L.R. (2d) 302 (Dist. Ct.) — *referred to*

Tomell Investments Ltd. v. East Marstock Lands Ltd. (1977), [1978] 1 S.C.R. 974, 2 R.P.R. 69, 16 N.R. 139, 77 D.L.R. (3d) 145, affirming Ont. C.A. [unreported], affirming (1975), 8 O.R. (2d) 396, 58 D.L.R. (3d) 172 (H.C.) — *distinguished*

459745 Ontario Ltd. v. Wideview Holdings Ltd. (1987), 44 R.P.R. 97, 59 O.R. (2d) 361, 37 D.L.R. (4th) 765 (H.C.) — *referred to*

Statutes considered:

Interest Act, R.S.C. 1970, c. I-18 [R.S.C. 1985, c. I-15] —

s. 8 [R.S.C. 1985, c. I-15, s. 8]

Interest Act, R.S.C. 1985, c. I-15 —

s. 8

s. 8(1)

s. 10

Mortgages Act, R.S.O. 1980, c. 296 [R.S.O. 1990, c. M.40] —

s. 16 [R.S.O. 1990, c. M.40, s. 17]

s. 16(1) [R.S.O. 1990, c. M.40, s. 17(1)]

s. 17 [R.S.O. 1990, c. M.40, s. 18]

Appeals from two decisions determining validity of bonus payment covenants in mortgages.

The judgment of the court was delivered by *McKinlay J.A.*:

1 These two appeals, heard together, raise two closely related issues. The first is whether s. 8 of the *Interest Act*, R.S.C. 1985, c. I-15, prohibits the enforcement of a covenant in the mortgages involved in each appeal, which covenant, following default under the mortgage, requires three months' notice of payment or a bonus in lieu thereof. The second is the applicability of s. 16 of the *Mortgages Act*, R.S.O. 1980, c. 296 (the "*Mortgages Act*") [now R.S.O. 1990, c. M.40, s. 17], to the facts of the two appeals. In the *Mastercraft* case, the judge hearing the application held that the covenant in question was enforceable because it did not offend the provisions of s. 8 of the *Interest Act*. In the *Peace Valley* case, the judge hearing the application held the reverse. The covenants in issue in the cases read as follows:

(In *Mastercraft*) — And the said Mortgagor covenants with the Mortgagee that in the event of non-payment of the said principal moneys at the time or times above provided, he shall not require the Mortgagee to accept payment of the said principal moneys without first giving three months' previous notice in writing, or paying a bonus equal to three months' interest in advance on the said principal moneys.

(In *Peace Valley*) — And the Chargor covenants with the Chargee that in the event of non-payment of the principal amount at the time or times provided in the charge, then he shall not require the Chargee to accept payment of the principal amount without first giving three months' notice in writing, or paying a bonus equal to three months' interest in advance on the principal amount.

The Effect of s. 8 of the Interest Act

2 A provision in a mortgage similar to these was upheld by this court in the case of *Gullett v. Income Trust Co.* (1985), 37 R.P.R. 123. The reasons disclose no argument involving s. 8 of the *Interest Act*. In my view, that is quite understandable, since s. 8 does not deal with covenants requiring the giving of notice before paying off a mortgage debt which is in arrears. That section reads:

8.(1) No fine, penalty or rate of interest shall be stipulated for, taken, reserved or exacted on any arrears of principal or interest secured by mortgage on real property that has the effect of increasing the charge on the arrears beyond the rate of interest payable on principal money not in arrears.

3 What s. 8 interdicts is a "fine, penalty or rate of interest ... on arrears of principal or interest," which has the prohibited effect of "increasing the charge on the arrears beyond the rate of interest" payable under the mortgage. It was argued before us that if operation of the impugned covenant would result in recovery of an amount which, *if treated as interest* over the relevant period, would result in a rate in excess of that stated in the mortgage, then s. 8 would have been contravened.To accept that argument would be to define the terms "fine," "penalty" and "rate of interest" in terms of the result of their payment. That is not the way s. 8 reads. A clear reading of the section requires that unless one first finds a "fine," "penalty," or "rate of interest" charged on "arrears of principal or interest," it is unnecessary to consider whether the charge involved has the prohibited effect. In other words, the covenant must *both* stipulate for a "fine," "penalty" or "rate of interest," *and* have the prohibited effect.

4 In my view, "fine" or "penalty" are interchangeable terms in this context: I cannot distinguish between the two. Each constitutes a form of monetary punishment for breach of the repayment terms of the mortgage contract. In the covenants involved here, the payment is referred to as a "bonus," which is not prohibited by s. 8. It is obvious, of course, that mortgagees do not escape the operation of s. 8 by using the word "bonus" to describe something which is in substance a "fine" or "penalty." However, in these appeals, the "bonus" stipulated for is not an amount paid in punishment for a breach of the mortgage contract, but is a payment required for the privilege of paying arrears without the necessity of giving the three months' notice contracted for. It is not, therefore, a "fine" or "penalty."

5 It is left to consider whether the "bonus" referred to in these covenants constitutes a "rate of interest" charged on "arrears of principal or interest." I am of the view that it does not. An example of a covenant stipulating for such a "rate of interest" would be one stating that interest on arrears was to be paid at the rate of 15 per cent per annum, when the mortgage rate was 6 per cent. That would clearly contravene s. 8. However, the covenants in these appeals do not deal with a "rate of interest" at all, but deal merely with an amount of money calculated with reference to the mortgage rate.

6 It is true that in circumstances where the mortgagor did not wish to give the notice contracted for, the extraction of the bonus could have the effect referred to in s. 8. But, in my view, the effect is irrelevant if the payment stipulated for does not fall within the categories of "fine," "penalty" or "rate of interest."

7 In the *Gullett* case, as in the cases under appeal, the mortgagor, by agreeing to the covenant in question, was not contracting to pay a "fine, penalty or rate of interest" which would have the prohibited effect.What he contracted to do was to pay the mortgage when due or, if not, to give the mortgagee three months' notice of his intent to pay. The obvious purpose of such a stipulation is to give the mortgagee the benefit, when the mortgagor defaults, of a reasonable period during which to arrange for the alternate investment of its funds when the mortgagor does finally retire the mortgage. If the mortgagor wishes (obviously for its own benefit) to retire the mortgage at a date earlier than the termination of the three months' notice period, it has the contractual right to do so, but must pay for that right in an amount equal to three months' interest. In my view, such a contractual arrangement is not what is contemplated by s. 8 of the *Interest Act*. Had the covenant in question required the payment of interest during the notice period *plus* an additional amount equivalent to three months' interest, then the provision, and its attempted enforcement, would clearly have been contrary to s. 8. However, if three months' notice of payment were given by the mortgagor, he would merely pay interest at the mortgage rate during the three-month period, and at the end of the period he would be entitled to a discharge upon payment of all arrears. If he wished a discharge at any time after default without giving notice, he would have to pay all arrears of principal and interest, plus a charge equal to three months' interest, for the privilege of being allowed to pay the arrears without giving the agreed three months' notice. These are the facts in both cases under appeal. Different considerations might arise if three months' notice were given by a mortgagor, and after the passing of a portion of the notice period he wished to obtain a discharge. Such facts are not involved in either of these appeals.

8 Unfortunately, it appears that the attention of the court in the *Gullett* case was not drawn to the provisions of s. 8 of the *Interest Act*. Had that been done, the court could have analyzed the facts in the case in the light of that provision. Although the facts are not clear on the point, it must be assumed that the notice required by the covenant was not given by the mortgagor, and that the amount covenanted to be paid in lieu of such notice was, therefore, appropriately claimed.

9 It is argued by those attacking the covenant that the *Gullett* decision is contrary to the Supreme Court of Canada decision in *Tomell Investments Ltd. v. East Marstock Lands Ltd.*, [1978] 1 S.C.R. 974. That case established the constitutional validity of s. 8 of the *Interest Act* [R.S.C. 1970, c. I-18], and upheld the decisions of the trial judge and of the Ontario Court of Appeal that the covenant in question contravened its provisions. The *Gullett* and *Tomell* cases are clearly distinguishable. The covenant in the *Tomell* case reads:

> PROVIDED also that on default of payment of any of the moneys hereby secured or payable or on any proceedings being taken by the Mortgagee under this Mortgage, he shall be entitled to require payment, *in addition to all other moneys hereby secured or payable hereunder, of a bonus equal to three months' interest* in

> advance at the rate aforesaid upon the principal money hereby secured, and the Mortgagor shall not be entitled to require a discharge of this Mortgage without such payment.

(Emphasis added.)

That covenant purports to extract a bonus *in addition* to any other moneys payable under the mortgage, and is thus in clear contravention of s. 8. However, the covenants in the *Gullett* case, and in the two cases on appeal, merely require notice before repayment. The interest payable during the notice period is at the rate payable under the mortgage. Only if the mortgagor wishes to pay prior to the end of the notice period does the covenant result in a payment in addition to the interest which would otherwise be payable, but that payment is made in return for the privilege of prepayment.

10 We were referred to a line of cases in Ontario in which covenants to pay additional interest on default were held to be invalid, and it was argued that Ontario courts were consistent in so holding until the decision in *Gullett*. The cases cited fall into different factual categories.

11 Some of the cases cited dealt with default occurring prior to maturity of the mortgage where the mortgagee attempted to enforce a covenant, or a combination of covenants, resulting in a claim to pay three months' interest *in addition to* the interest otherwise payable for the use of money over the time period involved. The covenants in those cases did not provide an alternative of simply giving three months' notice of payment. See *Schwartz v. Williams* (1915), 35 O.L.R. 33, and *Glinert v. Kosztowniak*, [1972] 2 O.R. 284.

12 Some cases dealt with default occurring at maturity of the mortgage, where the mortgagee claimed or attempted to enforce a covenant to pay three months' interest *in addition to* payment of interest in full up to the time of repayment of principal. Again, no alternative of simple notice was given. See *Tapio v. Kajander*, [1965] 1 O.R. 431; *Adams Properties Ltd. v. Sherwood Estates Ltd.* (1976), 144 D.L.R. (3d) 562 (B.C. C.A.); *Parkhill v. Moher* (1977), 17 O.R. (2d) 543 (Ont. H.C.); and *459745 Ontario Ltd. v. Wideview Holdings Ltd.* (1987), 59 O.R. (2d) 361 .

13 In all of the above cases the amount claimed would clearly constitute a penalty for default, *and* would result in increasing the interest on the arrears beyond the mortgage rate, thus contravening the provisions of s. 8.

14 The Supreme Court of Canada in the *Tomell* case decided two things only — first, that s. 8 of the *Interest Act* is within the competence of Parliament in exercising its legislative power over "Interest"; and second, that the covenant in question contravened the provisions of s. 8.

15 On the issue of whether or not the covenant in question contravened the provisions of s. 8, Pigeon J. merely repeated excerpts from the reasons of Galligan J. [reported at (1975), 8 O.R. (2d) 396, 58 D.L.R. (3d) 172 (H.C.)] and the confirmatory decision, without reasons, of the Ontario Court of Appeal, and then stated that counsel for the mortgagee had not "made a case for reconsidering this recent decision of the full Court on the construction of the statute."

16 The following excerpt from the reasons of Galligan J. is quoted at p. 979:

> ... It is my opinion ... that the bonus clause in this mortgage has the effect of increasing the charge on arrears of interest beyond ... the rate of interest payable on principal money, and therefore is in violation of Section 8 of the *Interest Act*.

While none of the courts in *Tomell* specifically stated that the bonus required by the covenant involved amounted to a "fine" or "penalty," by necessary implication they must have been of that view since the covenant did not state a "rate of interest" on arrears. Given the fact that the covenant required payment of the bonus *in addition to* all other amounts payable by the mortgagor, such a conclusion was inevitable. However, it is my view that the *Tomell* case does not answer the question of the applicability of s. 8 to the facts of the cases under appeal.

17 The covenants in these appeals are analogous to the provisions of s. 10 of the *Interest Act* and s. 17 of the *Mortgages Act*, which provisions allow the mortgagor to prepay a long-term mortgage after five years on payment of a bonus equal

to three months' interest in lieu of notice. Neither of those provisions has been held to be invalid; and the Supreme Court of Canada in *Tomell* specifically declined to comment on s. 10 of the *Interest Act*.

18 Of course, the right of a mortgagor under s. 10 of the *Interest Act* or s. 17 of the *Mortgages Act* is a statutory right, and the covenants in question are matters of contract between the parties. In my view, however, no real issue arises from that distinction, since no statutory provision prohibits such covenants; indeed, s. 16 of the *Mortgages Act* incorporates a similar provision into all Ontario mortgages. This leads us to the second issue in these appeals — that is, whether s. 16 of the *Mortgages Act* is within the legislative competence of the Ontario legislature.

Is s. 16 of the Mortgages Act Valid Provincial Legislation?

19 The parties supporting the covenants in question argue that they are enforceable covenants because they fall precisely within the provisions of s. 16 of the *Mortgages Act*, which reads:

> 16.(1) Notwithstanding any agreement to the contrary, where default has been made in the payment of any principal money secured by a mortgage of freehold or leasehold property, the mortgagor or person entitled to make such payment may at any time, upon payment of three months interest on the principal money so in arrear, pay the same, or he may give the mortgagee at least three months notice, in writing, of his intention to make such payment at a time named in the notice, and in the event of his making such payment on the day so named he is entitled to make the same without any further payment of interest except to the date of payment.

Section 16 of the *Mortgages Act* clearly constitutes provincial legislation in respect of property and civil rights in the province. Only if it is in conflict with validly enacted federal legislation can it be found unconstitutional.

20 A concurring majority of six in the Supreme Court of Canada answered the question of the constitutionality of s. 8 of the *Interest Act* in *Tomell* by applying "the doctrine of ancillary power and its corollary that of the unoccupied field." At p. 986, Pigeon J., speaking for the majority, stated:

> Although in principle the abstention by the federal Parliament to exercise its exclusive legislative power does not enable the provincial legislatures to enact legislation on the subject, this is true only of what may be called the federal primary power. With respect to matters *which are not strictly within such primary power but can be dealt with ancillarily*, provincial jurisdictions over property and civil rights and over matters of a local nature remains unimpaired *until such time as the field is occupied.* (Emphasis added.)

And at p. 987, Pigeon J. stated:

> In my opinion, s. 8 of the *Interest Act* is valid federal legislation in respect of interest because, although it does not deal exclusively with interest in the strict sense of a charge accruing day by day, *it is, insofar as it deals with other charges, a valid exercise of ancillary power* designed to make effective the intention that the effective rate of interest over arrears of principal or interest should never be greater than the rate payable on principal money not in arrears. (Emphasis added.)

The question, then, is whether or not the provisions of s. 16 of the *Mortgages Act* are in conflict with the provisions of s. 8 of the *Interest Act*. The parties attacking the covenants take the position that s. 16 is unconstitutional because it provides for a "fine" or "penalty" of the type prohibited by s. 8 of the *Interest Act*.

21 By its terms, the provisions of s. 16 are incorporated into every mortgage in Ontario, and override any contrary provision in the mortgage. Section 16 gives a mortgagor a right, when in default of payment of principal, to repay that principal on giving three months' notice to the mortgagee of his intention to pay, and protects him from *any further payment of interest except to the date of payment*. Such interest would merely constitute payment for the use of the principal during the notice period. The provision protects the mortgagor by permitting payment of arrears without penalty, or by permitting early redemption at a price. It protects the mortgagee by giving him a three-month period

during which to arrange for reinvestment of his principal, or monies to compensate for lack of that notice. The option is that of the mortgagor.

22 Covenants which go beyond what is provided for in s. 16 of the *Mortgages Act* may well run afoul of s. 8 of the *Interest Act*. However, that does not affect the constitutional validity of s. 16, or the enforceability of covenants which do not go beyond its provisions. In my view, covenants which provide the protection intended by s. 16 are in harmony rather than in conflict with the provisions of s. 8. Both enactments can stand as constitutionally valid federal and provincial law.

Additional Issues

23 I wish to address very shortly two additional issues raised in these appeals.

24 It was argued that s. 8 of the *Interest Act* could not apply in situations where mortgages have matured, because at that stage there would be no "principal money not in arrears" within the meaning of the section and, therefore, there would be no "rate of interest payable on principal money not in arrears." That argument was addressed by the British Columbia Court of Appeal in *Adams Properties Ltd.*, supra, in which Carruthers J.A., speaking for the court, expressed the view that those words merely referred to the interest rate stated in the mortgage. I can see no other logical interpretation of those words.

25 It was also argued that s. 16(1) of the *Mortgages Act* applies only to situations where the mortgagor is attempting to pay off a mortgage which is in default, and not to situations where the mortgagee is taking action to recover monies owing. I specifically express no opinion on that issue, since it is irrelevant to the facts of these two appeals.

Result

26 In result, I would dismiss the appeal in *Mastercraft* with costs; and would allow the appeal in *Peace Valley* with costs here and below, set aside the judgment below, and replace it with a judgment consistent with the foregoing reasons.

First appeal dismissed; second appeal allowed.

TAB 2

2007 CarswellOnt 1246
Ontario Superior Court of Justice

Ialongo v. Serm Investments Ltd.

2007 CarswellOnt 1246, [2007] O.J. No. 789, 156 A.C.W.S. (3d) 221, 54 R.P.R. (4th) 310

Caroline Luce Ialongo et al. v. Serm Investments Limited

D. Brown J.

Heard: February 6, 2007
Judgment: March 5, 2007
Docket: 06-CV-324925

Counsel: S Schneiderman for Applicants
W. Greenspoon for Respondent

Subject: Property; Corporate and Commercial

Related Abridgment Classifications

Real property
VII Mortgages
VII.6 Interest
VII.6.e Penalty or increased interest on default
Real property
VII Mortgages
VII.6 Interest
VII.6.h Miscellaneous
Real property
VII Mortgages
VII.9 Foreclosure
VII.9.b When right arises
VII.9.b.ii Default of principal

Headnote

Real property --- Mortgages — Foreclosure — When right arises — Default of principal

Parties entered into mortgage agreement with principle amount of $45,000, monthly payments of interest only and term of one year — Respondent mortgagee only advanced $35,000 under mortgage and held rest back pending applicant mortgagors doing renovations to property — When mortgage matured, mortgagors did not pay amount due, but instead requested discharge statement — In discharge statement provided by mortgagee penalty interest of $1,687.50 was sought — Mortgagors asked for forbearance from mortgagee in order to find new financing, which mortgagee agreed to provided mortgagor paid $400 for extension and paid interest that would otherwise fall due — Mortgagor claimed penalty interest was not applicable and mortgagee issued notice of sale claiming both three months' interest payment pursuant to s. 17(1) of Mortgages Act and legal fees relating to notice — Mortgagors applied for interpretation of their rights under mortgage, claiming they were not required to pay three months' interest on discharge of mortgage because s. 17 only applies on default and they were not in default — On issue of default, mortgagors were in default — Mortgagors did not pay mortgagee amount required to discharge mortgage when it matured, and therefore, on that date they were in default — Letters written by mortgagee after that were about mortgagee forbearing from taking steps to enforce mortgage and did not extend term of mortgage.

Real property --- Mortgages — Interest — Penalty or increased interest on default

Parties entered into mortgage agreement with principle amount of $45,000, monthly payments of interest only and term of one year — Respondent mortgagee only advanced $35,000 under mortgage and held rest back pending applicant mortgagors doing renovations to property — When mortgage matured, mortgagors did not pay amount due, but instead requested discharge statement — In discharge statement provided by mortgagee penalty interest of $1,687.50 was sought — Mortgagors asked for forbearance from mortgagee in order to find new financing, which mortgagee agreed to provided mortgagor paid $400 for extension and paid interest that would otherwise fall due — Mortgagor claimed penalty interest was not applicable and mortgagee issued notice of sale claiming both three months' interest payment pursuant to s. 17(1) of Mortgages Act and legal fees relating to notice — Mortgagors applied for interpretation of their rights under mortgage, claiming that by conditioning discharge on payment of three months' interest, mortgagee ran afoul of s. 8 of Interest Act since this had effect of increasing charge on arrears beyond rate payable on amount not in arrears — Mortgagors also claimed that mortgagee could not require s. 17(1) payment once it had issued notice of sale and could not claim legal fees for notice of sale — Mortgagee did not have right to ask for three months' interest on principal money in arrears but could recover legal fees for notice of sale — Mortgagee relied solely on s. 17(1) of Mortgages Act as basis for requiring three months' payment since mortgage itself did not contain such covenant — Mortgagors did not give mortgagee three months' notice of intention to pay amount of principal in arrears, which was also option under s. 17(1), and instead asked for discharge statement since they wanted to pay arrears sooner — Section 17(1) entitled mortgagors to do so, but only upon payment of three months' interest on principal money in arrears — In circumstances, mortgagee was entitled to ask for three months' interest pursuant to s. 17(1) and therefore incompatibility with Interest Act did not arise — However, once mortgagor took steps to realize on security, such as issuing notice of sale, it could not convert rights of mortgagor under s. 17 into obligations of mortgagor on realization of security and therefore could not require payment under s. 17 — Mortgagor was within rights to recover legal fees since mortgage agreement included such term.

Real property --- Mortgages — Interest — Miscellaneous

Parties entered into mortgage agreement with principle amount of $45,000, monthly payments of interest only and term of one year — Respondent mortgagee only advanced $35,000 under mortgage and held rest back pending applicant mortgagors doing renovations to property — When mortgage matured, mortgagors did not pay amount due, but instead requested discharge statement — In discharge statement provided by mortgagee penalty interest of $1,687.50 was sought — Mortgagors asked for forbearance from mortgagee in order to find new financing, which mortgagee agreed to provided mortgagor paid $400 for extension and paid interest that would otherwise fall due — Mortgagor claimed penalty interest was not applicable and mortgagee issued notice of sale claiming both three months' interest payment pursuant to s. 17(1) of Mortgages Act and legal fees relating to notice — Mortgagors applied for interpretation of their rights under mortgage, claiming that since only $35,000 of committed mortgage funds was advanced, they should pay interest calculated on that amount and not on face amount of mortgage — Interest was to be calculated on face amount of mortgage but mortgagee was to give credit to mortgagors for net interest earned on money held back — During term of mortgage it was clear that mortgagee kept held back money ready for mortgagors — Also, mortgagors never complained about paying interest on face amount — Finally, mortgagee had paid syndicated investors in mortgage their share of interest on basis that full amount of principal had been advanced — Therefore, mortgagor was entitled to interest on face amount — However, mortgagor was also required to give mortgagors credit for net interest earned on money held back.

Table of Authorities

Cases considered by *D. Brown J.*:

Bills Investments Ltd. v. First Investors Corp. (1988), 1988 CarswellSask 494, 72 Sask. R. 213 (Sask. Q.B.) — referred to

Dickson v. Bluestein (1990), 16 R.P.R. (2d) 29, 2 O.R. (3d) 131, 1990 CarswellOnt 588 (Ont. Gen. Div.) — considered

Edmonds v. Hamilton Provident & Loan Society (1891), 18 O.A.R. 347 (Ont. C.A.) — followed

Gullett v. Income Trust Co. (1985), 11 O.A.C. 178, 37 R.P.R. 123, 1985 CarswellOnt 728 (Ont. C.A.) — considered

L.I.U.N.A., Local 837 v. 810322 Ontario Ltd. (August 9, 2006), Doc. 06-CL-6488 (Ont. S.C.J.) — considered

Mastercraft Properties Ltd. v. EL EF Investments Inc. (1993), 32 R.P.R. (2d) 312, 64 O.A.C. 308, 14 O.R. (3d) 519, 103 D.L.R. (4th) 759, 1993 CarswellOnt 614 (Ont. C.A.) — followed

O'Shanter Development Co. v. Gentra Canada Investments Inc. (1995), 47 R.P.R. (2d) 24, 25 O.R. (3d) 188, 84 O.A.C. 334, 1995 CarswellOnt 399 (Ont. Div. Ct.) — followed

Parkhill v. Moher (1977), 17 O.R. (2d) 543, 80 D.L.R. (3d) 754, 3 R.P.R. 26, 1977 CarswellOnt 432 (Ont. H.C.) — considered

Shankman v. Mutual Life Assurance Co. of Canada (1985), 36 R.P.R. 125, 11 O.A.C. 1, 21 D.L.R. (4th) 131, 52 O.R. (2d) 65, 1985 CarswellOnt 719 (Ont. C.A.) — referred to

SK Properties & Development Inc. v. Equitable Trust Co. (2003), 2003 CarswellOnt 2130 (Ont. S.C.J.) — considered

Statutes considered:

Interest Act, R.S.C. 1985, c. I-15

Generally — referred to

s. 8 — considered

s. 8(1) — considered

Mortgages Act, R.S.O. 1990, c. M.40

s. 17 — considered

s. 17(1) — considered

APPLICATION by mortgagors for interpretation of rights under mortgage.

D. Brown J.:

1 The applicants, mortgagors under a second mortgage (the "Mortgage") with the respondent on their property in Toronto (the "Property"), applied for the interpretation of their rights under the Mortgage. Specifically, the applicants sought orders that on the discharge of the Mortgage (i) the respondent could not require payment of $1,687.50 in respect of "section 17 penalty interest", (ii) the respondent could not charge $1,750 for legal fees relating to power of sale proceedings, and (iii) the respondent should give them a credit of approximately $3,200 representing the difference between interest calculated on the face amount of the Mortgage and on the amount actually advanced.

2 Following the hearing of the application I asked for and received further submissions from counsel on the applicability of section 17 of the *Mortgages Act*, R.S.O. 1990, c. M.40.

Facts

3 The parties entered into a Mortgage Commitment Agreement dated August 25, 2004 (the "Agreement") which provided that the principal amount of the Mortgage would be $45,000, with monthly payments of interest only. The mortgage would contain the Standard Charge Terms (9320/200033). Section 9 of the Agreement provided:

> $10,000 of advance to be held back pending receipt of bills and inspection of property after improvements completed to mortgaged property.

4 Pursuant to the Agreement the parties executed the Mortgage for the principal amount of $45,000 with a term of one year, expiring September 3, 2005, with monthly interest payments of $562.50.

5 It is common ground that the respondent only advanced $35,000 under the Mortgage.

6 In the late summer of 2005, just before the expiry of the Mortgage, the applicants provided the respondent with invoices totaling $900 for home improvements and requested their payment out of the held back funds. The respondent refused to advance the money taking the position that section 9 of the Agreement only permitted the applicants to access the additional funds upon the completion of all renovations.

7 When the Mortgage matured on September 3, 2005, the applicants sought its renewal. On September 20, 2005 the respondent advised that it would be prepared to renew the Mortgage as long as the first mortgage was brought into good standing, and indicated that it was willing to advance a further $5,000.00 upon renewal. A renewal letter of the same date informed them that the respondent was "prepared to renew the subject mortgage on the same terms and conditions, namely, those set out in the mortgage which matured on September 3, 2005..." The renewal letter specified a principal amount of $45,000.00, monthly interest payments of $562.50 and a one year term expiring September 3, 2006.

8 On October 11, 2005 the respondent proposed to reduce the amount of the renewed mortgage to $39,000.00 because a new first mortgage would exceed an amount previously discussed by the parties. The respondent also advised that it would not advance a further $5,000 on renewal for the same reason. On October 16 the respondent modified its renewal proposal advising that the Mortgage amount would remain at $45,000.00, but the applicants would have to provide evidence that the first mortgage did not exceed $345,000.00.

9 The applicants accepted the terms of renewal on October 19, 2006 and signed back the renewal letter dated September 20, 2005. It is common ground that the amount advanced under the Mortgage remained at $35,000.00.

10 The Mortgage matured on September 3, 2006. The applicants did not pay the amount due on that date. At some point the applicants requested a discharge statement, which the respondent provided on September 20, 2006. It specified a principal amount due of $45,000.00 and "penalty interest — section 17, $1,687.50". The respondent subsequently acknowledged that the principal amount was in error and that only $35,000.00 was due.

11 At this point the applicants requested the respondent to refrain from taking steps to enforce the Mortgage until November 3, 2006 to permit them time to find new financing. Mr. Schaffran, the principal of the respondent, deposed that he agreed to the forbearance as long as the applicants paid a fee and the interest that would otherwise fall due on October 3, 2006. On October 24, 2006 his counsel wrote to the applicants:

> We understand from our client, Sam Schaffran that you have provided him with $400.00 for an extension of the above noted charge along with the October 3 rd, 2006 payment in the amount of $562.50. Our client has instructed that the extension is provided until November 3, 2006. If the above Charge is not discharged by November 3, 2006 we will have no choice but to enforce on the mortgage.

Mr. Schaffran deposed that he did not agree to waive the prior default by the applicants.

12 On November 3, 2006 the applicants' solicitor, Mr. Sullivan, wrote to the respondent's counsel stating: "The extended mortgage matured in September of this year, and the mortgagors requested a discharge statement." Mr. Sullivan raised two objections to the discharge statement. First, he argued that since the full $45,000 had not been advanced, yet monthly interest payments were calculated on that amount, the applicants should be given credit for the difference between interest on the face amount and the amount advanced over the term of the Mortgage. He also contended that a "Section 17 Penalty Interest" was not applicable to a mortgage that had matured.

13 On November 6, 2006 the respondent's solicitors wrote back stating, in part:

> You are correct that $10,000.00 of the advance was held back pending receipt of bills and inspection of property after improvement completed to mortgaged Property. These improvements were never performed. As the borrower requested $45,000.00 it was always intended by both parties that the interest charged would be on the full $45,000.00 as per the registered mortgage. This is the reason why the monthly interest payments commenced and continued for the amount of $562.50 throughout the entirety of the mortgage. This has never been disputed by your clients...
>
> Your clients' mortgage matured on September 3, 2006 and since they failed to renew or payout on the said date, the mortgage went into default. We provided a payout statement to TD to show the outstanding amounts however, again the mortgage was not paid out. As a courtesy, our client contacted your clients and advised that if your clients

provided him with the November 3, 2006 payment and an additional $400.00 fee he would forbear enforcement until after November 15, 2006 and not commence Power of Sale proceedings. At no time did our client agree to waive the default or any of the fees and penalties associated therewith.

14 At that point the parties agreed to disagree. On November 16, 2006 the respondent issued a Notice of Sale in which it claimed both a three month interest payment pursuant to section 17(1) of the *Mortgages Act* and legal fees relating to the Notice of Sale in the amount of $1,750. The respondent subsequently agreed to suspend enforcement of the Mortgage pending the determination of this application.

Analysis

A. Was the respondent entitled to require a payment under section 17 of the Mortgages Act?

15 Section 17(1) of the *Mortgages Act* provides:

> 17(1) Despite any agreement to the contrary, where default has been made in the payment of any principal money secured by a mortgage of freehold or leasehold property, the mortgagor or person entitled to make such payment may at any time, upon payment of three months interest on the principal money so in arrear, pay the same, or the mortgagor or person entitled to make such payment may give the mortgagee at least three months notice, in writing, of the intention to make such payment at a time named in the notice, and in the event of making such payment on the day so named is entitled to make the same without any further payment of interest except to the date of payment.

Applicants' counsel advanced three arguments why the respondent was not entitled to require a bonus payment of 3 months' interest on the discharge of the Mortgage:

> (i) the term of the Mortgage had been extended beyond September 3, 2006 so the applicants were not in default of the Mortgage at that time and section 17(1) therefore did not apply;
>
> (ii) requiring the mortgagors to pay three months' interest to discharge the Mortgage would result in an effective rate of interest higher than that stipulated in the Mortgage thereby running afoul of section 8(1) of the *Interest Act*; and,
>
> (iii) a mortgagee could not require a section 17(1) payment once it had taken steps to enforce a mortgage.

(i) Was the term of the Mortgage extended beyond September 3,2006?

16 Section 17 only applies "where default has been made in the payment of any principal money". The applicants argued that they were not in default when the respondent provided a discharge statement on September 20, 2006 or served the Notice of Sale. Their counsel contended that the respondent, by its solicitor's letters dated October 24, 2006 and November 6, 2006, extended the term of the Mortgage to November 15, 2006.

17 The evidence does not support this contention. It is undisputed that the applicants did not pay the respondent the amount required to discharge the Mortgage when it matured on September 3, 2006. On that date the applicants were in default. Although the respondent's solicitor's letter of October 24, 2006 advised that "our client has instructed that the extension is provided until November 3, 2006", that letter must be read in the context of discussions that Mr. Schaffran deposed having with the applicants in September, 2006 about refraining from taking any steps to enforce the Mortgage. Mr. Sullivan, the applicants' lawyer, in his letter of November 3, 2006 did not contend that the term of the Mortgage had been extended beyond September 3, 2006; he acknowledged that "the extended mortgage matured in September of this year". Finally, Ms. Ialongo's affidavit contained no suggestion that the respondent had extended the Mortgage for a term beyond September 3, 2006. On the contrary, her evidence supported the respondent's position that their conversations were about the respondent forbearing from taking steps to enforce the Mortgage.

18 I therefore find that the applicants were in default of the Mortgage on September 3, 2006 and that the term of the Mortgage was not extended beyond that date.

(ii) Would requiring the applicants to pay three months interest to discharge the mortgage contravene section 8(1) of the Interest Act?

19 Applicants' counsel argued that by conditioning the discharge of the Mortgage on the payment of three months' interest the respondent ran afoul of section 8 of the *Interest Act* which provides that "no fine, penalty or rate of interest shall be stipulated for, taken, reserved or exacted on any arrears of principal or interest secured by mortgage on real property... that has the effect of increasing the charge on the arrears beyond the rate of interest payable on principal money not in arrears." In the present case the respondent did not rely on a covenant in the Mortgage to justify requiring the payment of three months' interest because the Standard Charge Terms (200033) of the Mortgage did not contain such a covenant. The respondent relied solely on section 17(1) of the *Mortgages Act* as the basis for requiring such a payment.

20 In *Mastercraft Properties Ltd. v. EL EF Investments Inc.* (1993), 14 O.R. (3d) 519 (Ont. C.A.) the Court of Appeal held that section 17(1) of the *Mortgages Act*, and mortgage covenants reflecting its terms, operate in harmony with section 8 of the *Interest Act*. As McKinlay J.A. explained at para. 21 of her reasons:

> By its terms, the provisions of s. 16 [now s. 17] are incorporated into every mortgage in Ontario, and override any contrary provision in the mortgage. Section 16 gives a mortgagor a right, when in default of payment of principal, to repay that principal on giving three months' notice to the mortgagee of his intention to pay, and protects him from any further payment of interest except to the date of payment. Such interest would merely constitute payment for the use of the principal during the notice period. The provision protects the mortgagor by permitting payment of arrears without penalty, or by permitting early redemption at a price. It protects the mortgagee by giving him a three-month period during which to arrange for reinvestment of his principal, or monies to compensate for lack of that notice. The option is that of the mortgagor.

As the Court noted at para. 4, where a mortgagor in default is given the choice between providing three months' notice or paying the arrears before the three months expire, the required bonus of three month's interest is not an amount paid in punishment for a breach of the mortgage contract, but a payment required for the privilege of paying arrears without the necessity of giving the three months' notice contracted for. As a result, it held that section 17(1) of the *Mortgages Act* did not conflict with section 8(1) of the *Interest Act*.

21 In *Mastercraft* the Court of Appeal did not squarely address the issue of whether a mortgagee could only insist on payment of a bonus under section 17(1) of the *Mortgages Act* where the mortgagor had defaulted prior to the maturity of the mortgage. In her description of the rationale underlying section 17 and similarly-worded covenants, McKinlay, J.A. suggested that the option provided to the mortgagor would only be available in the event the mortgagor defaulted before the mortgage matured. When she referred to the prior decision of the Court of Appeal in *Gullett v. Income Trust Co.*, [1985] O.J. No. 200 (Ont. C.A.) in which the mortgage contained a covenant similar in terms to section 17 of the *Mortgages Act*, McKinlay, J.A. wrote:

> The obvious purpose of such a stipulation is to give the mortgagee the benefit, when the mortgagor defaults, of a reasonable period during which to arrange for the alternate investment of its funds when the mortgagor does finally retire the mortgage. If the mortgagor wishes (obviously for its own benefit) to retire the mortgage at a date earlier than the termination of the three months' notice period, it has the contractual right to do so, but must pay for that right in an amount equal to three months' interest.

Later in her reasons, at para. 21, McKinlay, J.A. repeated the rationale of section 17 of the *Mortgages Act*:

> It protects the mortgagee by giving him a three-month period during which to arrange for reinvestment of his principal, or monies to compensate for lack of that notice.

The need to give a mortgagee time to arrange for the reinvestment of his principal is one more likely to arise in the event the mortgagor seeks to pay the mortgage prior to its maturity, rather than on the date of its maturity.

22 Notwithstanding this rationale put forward in *Mastercraft*, in its previous decision in *Gullett*, *supra.*, the Court of Appeal permitted a mortgagee to charge a bonus of three months' interest where default had occurred on the maturity of the mortgage. In that case the mortgagor did not pay off the mortgage on maturity, but spent several weeks considering the mortgagee's offer to renew. Having decided to refinance with another lender several weeks after the mortgage had matured, the mortgagor asked for a discharge statement. In it the mortgagee required payment of three months' interest. The mortgage contained a clause in the language of section 17 of the *Mortgages Act*. In holding that the mortgagee was within his rights to insist on the payment, Grange, J.A. stated:

> It is quite clear that if the mortgagee had done nothing on the date for payment of principal the covenant would have taken effect and three months interest in lieu of notice would be payable if the balance were tendered at any time after November 15 (the maturity date).

23 More recently in *SK Properties & Development Inc. v. Equitable Trust Co.*, [2003] O.J. No. 2234 (Ont. S.C.J.), the Court held that section 17 of the *Mortgages Act* applied to a default occurring at the time a mortgage matured, and that where a mortgagor failed to pay off the mortgage on its maturity date, the mortgagee was entitled to require the mortgagor to pay three months' interest to discharge the mortgage.

24 Although a tension exists between the reasoning of the Court of Appeal in *Mastercraft* and the result in *Gullett*, I do not think that the tension can simply be explained away, as submitted by the applicants, as a difference between a mortgagee relying on a statutory right in one case and on a contractual one in the other. McKinlay J.A., at para. 18 of her judgment in *Mastercraft*, clearly stated that she did not see any real issue arising from claims made under section 17 of the *Mortgages Act* in contrast to those made under similar contractual terms. In light of this, *Gullett* remains authority for the ability of a mortgagee to require payment of three months' interest as a bonus upon a default occurring at the maturity of the mortgage.

25 In the present case, the applicants were in default when they failed to pay the Mortgage in full when it matured on September 3, 2006. They did not give the respondent three months' notice of their intention to pay the amount of the principal in arrears. Instead, they asked the respondent to provide them with a discharge statement; they wanted to pay the arrears sooner. Following *Gullett* and *SK Properties & Development Inc.*, *supra.*, section 17(1) of the *Mortgages Act* entitled them to do so, but only upon payment of three months' interest on the principal money in arrears. Given the applicants' request for early payment, the respondent mortgagee was entitled to include a payment of three months' interest in the September 20, 2006 discharge statement. That statement complied with section 17(1) of the *Mortgages Act* and, as a result, no question of incompatibility with the *Interest Act* arose.

(iii) Did the issuance of a Notice of Sale affect the ability of the mortgagee to claim payment of three months interest under Section 17 of the Mortgages Act?

26 That, however, does not end the matter. The respondent issued a Notice of Sale under the Mortgage and in it claimed payment of three months' interest pursuant to section 17 of the *Mortgages Act*. Did the issuance of the Notice of Sale affect the respondent's entitlement to claim interest under section 17?

27 In *Dickson v. Bluestein* (1990), 2 O.R. (3d) 131 (Ont. Gen. Div.), the Court observed that section 17(1) of the *Mortgages Act* is remedial in its objective and speaks only to the mortgagor in default; it is not applicable when the mortgagee takes action to recover monies in default. This echoed the view previously expressed in *Parkhill v. Moher* (1977), 80 D.L.R. (3d) 754 (Ont. H.C.) where, at p. 756, the court held that when a mortgagee takes action to recover monies after default one looks not to section 17, but to the agreement between the parties in the mortgage.

28 By contrast, in the recent decision in *L.I.U.N.A., Local 837 v. 810322 Ontario Ltd.*, [2006] O.J. No. 3260 (Ont. S.C.J.), the court rejected the argument that section 17 of the *Mortgages Act* did not apply once the mortgagor had the right to redeem following the issuance of a notice of sale. Instead, the court held, at para. 4, that "failure to pay the mortgage in full on its due date was a default that triggered s. 17 requiring payment of 3 months interest, just as it did in *SK Properties, supra.*

29 How does one reconcile these two sets of cases? Guidance can be found in the Divisional Court decision in *O'Shanter Development Co. v. Gentra Canada Investments Inc.* (1995), 25 O.R. (3d) 188 (Ont. Div. Ct.) which involved a default on a mortgage followed by the commencement of power of sale proceedings. The case turned on the effect of a prepayment clause in the mortgage. During the course of his reasons, Saunders, J. considered the relationship between section 17 of the *Mortgages Act* and steps taken by a mortgagee to enforce its security. He wrote, at paras. 12 and 13:

> Equity has historically provided a defaulting mortgagor with an opportunity to redeem his property upon six months' notice or interest in lieu of notice: see *Smith v. Smith*, [1891] 3 Ch. 550...The rule has been codified in s. 17 of the *Mortgages Act* where the obligation is reduced to three months...However, if a mortgagee seeks to realize on his security, the equitable right of the mortgagor to redeem is triggered and he is not required to give notice or pay additional interest: *Smith v. Smith, supra*; and *Bovill v. Endle*, [1896] 1 Ch. 648, 65 L.J. 542.

In that case the mortgage contained a clause requiring prepayment of the mortgagee's costs, with a minimum of three months' interest, if default occurred prior to the maturity date. Saunders J. noted, at para. 15, that since section 17 of the *Mortgages Act* overrides a mortgage contract, it was open in that case for the mortgagor, upon default, to have given notice or made the payment provided for in section 17 and thereby avoid the prepayment amount as long as the mortgagee had not yet realized on its security.

30 In my view the reasoning in *O'Shanter Development* is consistent with the view expressed by the Court of Appeal in *Mastercraft, supra.*, that the rights afforded by section 17 are options made available to the mortgagor on default: it can give notice or pay the bonus prior to the expiry of the notice period. Once, however, the mortgagee takes steps to realize on its security, such as by issuing a notice of sale (see: *Shankman v. Mutual Life Assurance Co. of Canada* (1985), 52 O.R. (2d) 65 (Ont. C.A.)), it cannot convert the rights of the mortgagor under section 17 into obligations of the mortgagor upon the realization of the security. The amounts a mortgagee may demand from a mortgagor upon realization are those spelled out in the mortgage contract, not in section 17 of the *Mortgages Act.*

31 In the present case, once the respondent mortgagee issued its Notice of Sale, it was not entitled to demand payment of three months' interest under section 17 of the *Mortgages Act.* It stood in a fundamentally different position than it did on September 20, 2006 when it provided the applicants with a discharge statement at their request. Once the respondent issued the notice of sale, it was required to look to the terms of the Mortgage to ascertain what amounts it could require the mortgagor to pay in order to redeem the Mortgage. Accordingly, I conclude that once it issued the Notice of Sale the respondent was not entitled to require the applicants to make a payment under section 17 of the *Mortgages Act.*

32 However, since section 8 of the Mortgage's Standard Charge Terms permitted the mortgagee to recover legal fees incurred "in taking, recovering and keeping possession of the land", the respondent was within its rights to include in the Notice of Sale a requirement that the applicants pay its legal fees of $1,750.

B. Are the Applicants entitled to a credit equivalent to the difference in interest between the face amount of the Mortgage and the amount advanced?

33 The applicants submitted that since the respondent only advanced $35,000 of the committed mortgage funds, they should only have paid interest calculated on that amount, not on the face amount of the Mortgage.

34 As a general rule a mortgagee can only claim interest from the time the money is advanced, and if a mortgagee advances less than the face value of the mortgage, it can only recover the amount advanced and "all the provisions in

the instrument are in equity made to conform to the less sum, including the interest": *Edmonds v. Hamilton Provident & Loan Society* (1891), 18 O.A.R. 347 (Ont. C.A.), at p. 362, quoted with approval in *Bills Investments Ltd. v. First Investors Corp.*, [1988] S.J. No. 765 (Sask. Q.B.), at p. 7. In *Edmonds*, *supra.*, the Court of Appeal noted an exception to this general rule. Osler, J.A., stated, at page 353:

> If the mortgagee keeps the money ready, he ought to have the interest agreed upon, and the most the mortgagor can expect is that, as was done in this case, the mortgagee shall allow him such interest as the bank may have allowed him pending the completion of the transaction. No doubt such a contract should be clearly made out, as it may work a hardship on the mortgagor, and I yield to the opinion that it has not been so made out in this case.

35 Did the parties agree that the respondent was entitled to interest on the money held back? In my view they did.

36 Section 9 of the Agreement stipulated that the respondent would hold back $10,000 of the advance pending "receipt of bills and inspection of property after improvements completed to mortgaged property." Ms. Ialongo acknowledged that towards the end of the first year of the Mortgage she delivered some interim bills to the respondent and asked for their repayment. The respondent refused, taking the position that section 9 of the Agreement only required further funds to be advanced on the completion of improvements. The language of section 9 of the Agreement permitted the respondent to take that position. It is clear that during the first year of the Mortgage the respondent kept the held back money ready for the applicants and therefore was entitled to interest on the face amount of the Mortgage.

37 A similar result holds for the second year of the Mortgage. First, on October 19, 2005 the applicants accepted the respondent's offer to renew the Mortgage "on the same terms and conditions, namely, those set out in the mortgage which matured on September 3, 2005..." Although in negotiations leading to the renewal the respondent had advised the applicants that it would be prepared to advance a further $5,000 on renewal, the respondent withdrew that offer when it learned that the appraised value of the house was less than what the applicants had represented. In his affidavit Mr. Schaffran deposed that in light of the lesser appraised value he was not prepared to release the holdback until all repairs had been completed and the property inspected to his satisfaction. Mr. Schaffran was not cross-examined on that statement.

38 Second, prior to their default on September 3, 2006 the applicants never complained about paying interest on the face amount of the Mortgage rather than on the amount advanced.

39 Finally, Mr. Schaffran deposed that since the registration of the Mortgage he maintained the additional $10,000 holdback so that it would be available to be advanced, and that he has paid to the syndicated investors in the Mortgage their share of interest on the basis that the full principal amount had been advanced. Again, his evidence was not subjected to cross-examination.

40 Taken as a whole, this evidence leads to the conclusion that section 9 of the Agreement remained in place during the second term of the Mortgage. Accordingly, I am satisfied that the respondent has brought himself within the exception described in the *Edmonds* case: he kept the mortgage money ready for the mortgagor, so he ought to have the interest agreed upon.

41 As an alternative argument the applicants submitted that if the respondent could charge interest on the face amount of the Mortgage, it was obliged to give the applicants credit for interest earned on the money held back. That argument certainly conforms to what Osler, J.A. stated in *Edmonds*, *supra.*, and I therefore require the respondent to give credit to the applicants for the net interest earned on the money held back.

C. Summary

42 In conclusion, I find that in order to discharge this Mortgage the respondent was entitled to require the applicants to pay its legal fees of $1,750 in respect of Notice of Sale proceedings, but not three months' interest in the amount of $1,687.50 purportedly pursuant to section 17 of the *Mortgages Act*. Further, the respondent was entitled to calculate

interest on the face amount of the Mortgage, but the applicants were entitled to a credit in respect of the net interest earned on the funds not advanced.

Costs

43 Since success on the application has been mixed, no order as to costs is appropriate.

Order accordingly.

TAB 3

2010 ONSC 116
Ontario Superior Court of Justice

Mintz (In Trust) v. Mademont Yonge Inc.

2010 CarswellOnt 912, 2010 ONSC 116, 185 A.C.W.S. (3d) 766, 91 R.P.R. (4th) 303

IRWIN MINTZ, IN TRUST (Applicant) and MADEMONT YONGE INC. and PAUL MONTGOMERY (Respondents)

Pepall J.

Judgment: February 18, 2010
Docket: CV-09-383528

Counsel: Shawn Pulver for Applicant
Christine Jonathan for Respondents

Subject: Property; Corporate and Commercial
Related Abridgment Classifications
Real property
VII Mortgages
VII.6 Interest
VII.6.e Penalty or increased interest on default
Headnote
Real property --- Mortgages — Interest — Penalty or increased interest on default
Mortgage matured on March 1, 2009 and was never extended, and mortgagor advised mortgagee on March 13, 2009 that he intended to sell property on May 8, 2009 and requested mortgage discharge statement — In addition to March and April interest, mortgagee claimed three months' interest in amount of $21,249.99 and brought application seeking this amount relying on s. 17 of Mortgages Act — Mortgagee submitted that mortgage was in default and that he was entitled to either three months' notice, which was not given, or three months' interest — Mortgagor brought cross-application seeking declaration that mortgagee was entitled to only one month of interest of $7,083.33 — Application granted; cross-application dismissed — Cases show that payment of three months' interest under s. 17 of Mortgages Act constitutes bonus paid for privilege of paying arrears without necessity of giving three months' notice and such payment is not contrary to s. 8 of Interest Act — Mortgagor failed to give three months' notice and was required to pay additional three months' interest.
Table of Authorities
Cases considered by *Pepall J.*:
Gullett v. Income Trust Co. (1985), 11 O.A.C. 178, 37 R.P.R. 123, 1985 CarswellOnt 728 (Ont. C.A.) — considered
Ialongo v. Serm Investments Ltd. (2007), 54 R.P.R. (4th) 310, 2007 CarswellOnt 1246 (Ont. S.C.J.) — considered
Mastercraft Properties Ltd. v. EL EF Investments Inc. (1993), 32 R.P.R. (2d) 312, 64 O.A.C. 308, 14 O.R. (3d) 519, 103 D.L.R. (4th) 759, 1993 CarswellOnt 614 (Ont. C.A.) — considered
Mastercraft Properties Ltd. v. EL EF Investments Inc. (1994), 35 R.P.R. (2d) 219 (note), 1994 CarswellOnt 5790, 1994 CarswellOnt 5791, 108 D.L.R. (4th) vii (note) (S.C.C.) — referred to
Statutes considered:
Interest Act, R.S.C. 1985, c. I-15
s. 8 — considered
Mortgages Act, R.S.O. 1980, c. 296
s. 16 — considered

Mortgages Act, R.S.O. 1990, c. M.40
s. 17 — considered

APPLICATION by mortgagee seeking three months' extra interest; CROSS-APPLICATION by mortgagor seeking declaration that only one month of interest was owed.

***Pepall J.*:**

Introduction

This case deals with the application of section 17 of the *Mortgages Act* [1].

Facts

1 The Respondent, Mademont Yonge Inc. ("Mademont"), owned property in Newmarket, Ontario. The Respondent, Paul Montgomery, is the President of Mademont. Irwin Mintz, in trust ("Mintz"), provided a mortgage in the amount of one million dollars to Mademont. The maturity date of the mortgage was March 1, 2009. Montgomery guaranteed the mortgage. On December 18, 2008, Mademont wrote to Mintz advising that a sale of the property would not be completed by the mortgage maturity date and requested an extension of the maturity date to June 30, 2009. The term of the mortgage was never extended. The mortgage was not repaid on March 1, 2009. On March 1, 2009 Mademont negotiated an agreement of purchase and sale for the sale of the property to a third party. On March 13, 2009, Mademont's lawyer advised Mintz that Mademont was selling the property with a closing date of May 8, 2009 and requested a mortgage discharge statement. Mademont paid the monthly interest payments for March and April to Mintz.

2 Mintz provided a statement on March 24, 2009. It included an early discharge fee, an extension fee and interest on the extension fee. On April 25, 2009, Mademont disputed these amounts and asserted that there was no extension agreement and no early discharge. In addition to the March and April interest payments already made, Mintz then claimed three months' interest in the amount of $21,249.99. It is this amount that is now in dispute.

3 Mintz states that he is entitled to this amount and relies not on a covenant in the mortgage but on section 17 of the *Mortgages Act*. Mintz states that as the mortgage was in default, in addition to the principal sum in arrears, a mortgagee is entitled to either three months' notice or three months' interest in exchange for a discharge of the mortgage. Notice having been given on March 13 of an intention to sell on May 9, three months' notice was not given. As such, three months' interest is due in addition to the March and April payments.

4 Mademont states that having already received two months' interest, Mintz is only entitled to $7,083.33 which represents the interest payment due May 1, 2009 and seeks a declaration to that effect.

5 No one took the position that the December 18, 2008 letter constituted notice.

6 The mortgage was discharged on May 9, 2009 and the parties agreed that $30,000 should be held in trust pending resolution of the two cross-applications. The applications had been on the civil list where they had been adjourned twice. I agreed to hear the applications because no civil list judge was available. For reasons that are unclear, the parties' materials were not before me and therefore they were passed up to me during argument. There had been an issue as to whether there had been an extension agreement but on the morning of argument, Mintz abandoned that argument.

Discussion

7 Section 17 of the *Mortgages Act* states:

> (1) Despite any agreement to the contrary, where default has been made in the payment of any principal money secured by a mortgage of freehold and leasehold property, the mortgagor or person entitled to make such payment may at any time, upon payment of three months' interest on the principal money so in arrear, pay the same, or the

> mortgagor or person entitled to make such payment may give the mortgagee at least three months' notice, in writing, of the intention to make such payment at a time named in the notice, and in the event of making such payment on the day so named is entitled to make the same without any further payment of interest except to the date of payment.
>
> (2) If the mortgagor or person entitled to make such payment fails to make the same at the time mentioned in the notice, the mortgagor or person is thereafter entitled to make such payment only on paying the principal money so in arrear and interest thereon to the date of payment together with three months' interest in advance.
>
> (3) Nothing in this section affects or limits the right of the mortgagee to recover by action or otherwise the principal money so in arrear after default has been made.

8 Accordingly, if there is a default in payment, to obtain a discharge, a mortgagor may either pay three months' interest on the principal in arrears or may give three months' notice of its intention to pay. Provided payment is made, no further interest need be paid.

9 While one might conclude from a reading of section 17 that it was designed for a default in payment during the currency of a mortgage, in *Gullett v. Income Trust Co.* [2], the Court of Appeal held that it also applies to a mature mortgage. In addition, in *Mastercraft Properties Ltd. v. EL EF Investments Inc.* [3], the Court of Appeal stated that section 17 is incorporated into every mortgage in Ontario.

10 The rationale for section 17 was also described by the Court of Appeal in the *Mastercraft* decision. On the one hand, the section protects the mortgagor by permitting payment of arrears without payment of a penalty. On the other, the section protects the mortgagee by giving it a three month notice period during which to arrange for reinvestment of the principal or money to compensate for lack of notice. The option is that of the mortgagor.

11 In determining whether Mademont is obliged to pay an additional three months' interest, three cases merit discussion.

12 In *Gullett v. Income Trust Co.* [4], the mortgage contained a covenant that provided that if there was a default in payment, the mortgagor could give three months' notice in writing of its intention to pay the mortgage in full or pay a bonus equal to three months' interest. Specifically, it stated "And the said Mortgagor covenants with the Mortgagee that in the event of nonpayment of the said principal moneys at the time or times above provided, then he shall not require the Mortgagee to accept payment of said principal moneys without first giving three months' previous notice in writing, or paying a bonus equal to three months' interest in advance on the said principal moneys." Grange J. A. stated that the covenant was governed by and in conformity with section 16 (now section 17) of the *Mortgages Act*.

13 The mortgage in *Gullett* matured on November 15, 1983. No notice was given by the mortgagor but the mortgagee continued to accept interest payments while the parties negotiated a renewal of the mortgage. In mid-December, the mortgagee was advised that rather than pursuing a renewal, the mortgagor had opted to obtain financing on January 17, 1984 from a third party. In the discharge statement, the mortgagee claimed three months' interest.

14 Grange J.A. noted that had the mortgagee done nothing on the date of maturity, the covenant would have taken effect and three months' interest in lieu of notice would be payable. He then found that the mortgagee had not waived its right to three months' interest simply by accepting interest payments after maturity. He therefore ordered that the mortgagor pay three months' interest as compensation.

15 *Mastercraft* involved a default in interest payments due under a mortgage in circumstances where the mortgagor had not given notice of its intention to pay the mortgage in full. Both section 16 (now section 17) of the *Mortgages Act* and section 8 of the *Interest Act* [5] which prohibited fines or penalties on arrears of principal or interest secured by a mortgage were in issue. McKinlay J.A. stated that the payment of three months' interest contemplated by section 16 of the *Mortgages Act* constituted a bonus paid not in punishment for a breach of the mortgage contract but for the privilege

of paying arrears without the necessity of giving the three months' notice and as such the payment was not contrary to section 8 of the *Interest Act*.

> If he [the mortgagor] wished a discharge at any time after default without giving notice, he would have to pay all arrears of principal and interest, plus a charge equal to three months' interest, for the privilege of being allowed to pay the arrears without giving the agreed three months' notice. [6]

16 McKinlay J.A. noted that the attention of the court in *Gullett* was not drawn to the provisions of Section 8 of the *Interest Act* dealing with penalties. She stated that although the facts were not clear in *Gullett*, it had to be assumed that the notice required was not given by the mortgagor and the amount covenanted to be paid in lieu of such notice was therefore appropriately claimed. [7]

17 The third relevant decision is *Ialongo v. Serm Investments Ltd.* [8]. In that case, the mortgage matured on September 3, 2005. The mortgagor failed to repay the mortgage on that day but requested a discharge statement which the mortgagee provided on September 20. In it, the mortgagee claimed the principal amount and section 17 "penalty interest". Brown J. concluded that *Gullett* was authority for the mortgagee to require three months' interest as a bonus upon a default occurring on the maturity of a mortgage. The mortgagee was entitled to insist on payment of three months' interest as three months' notice had not been given.

18 In the case before me, Mademont did not give three months' notice. Having failed to do so, Mademont is required to pay an additional three months' interest. This is in keeping with the legal principles set forth in *Gullett*, *Mastercraft* and *Ialongo* and it is important for there to be consistency in the law. Furthermore, any other result would do violence to section 17 of the *Mortgages Act*.

19 Both parties submitted costs requests. Mintz was successful and should be entitled to his costs on a partial indemnity scale. While I am of the view that the matter should have been settled, both parties claimed close to the same amount in costs. As such, the quantum of Mintz's request was in the reasonable expectation of the respondents. That said, the extension agreement argument was only abandoned by Mintz the morning of the motion. In the circumstances, the respondents are to pay Mintz the sum of $9,000 inclusive of fees, disbursements and G.S.T. This is fair and reasonable and particularly so given the complexity of the legal issues.

20 If the parties are unable to agree on interest, I may be spoken to at a 9:30 a.m. appointment scheduled with the Commercial List Office.

Application granted; cross-application dismissed.

Footnotes

1 R.S.O. 1990, c. M-40.

2 (1985), 37 R.P.R. 123 (Ont. C.A.).

3 (1993), 14 O.R. (3d) 519 (Ont. C.A.), leave to appeal to S.C.C. refused (1994), 108 D.L.R. (4th) vii (note) (S.C.C.).

4 (1985), 37 R.P.R. 123 (Ont. C.A.)

5 R.S.C. 1985, c.I-15.

6 Supra note 3 at para.7.

7 Ibid at para.8.

8 (2007), 54 R.P.R. (4th) 310 (Ont. S.C.J.).

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TAB 4

2017 ONSC 4641
Ontario Superior Court of Justice

2468390 Ontario Inc. v. 5F Investment Group Inc.

2017 CarswellOnt 20437, 2017 ONSC 4641, 287 A.C.W.S. (3d) 160

2468390 ONTARIO INC. (Plaintiff) and 5F INVESTMENT GROUP INC. and OTT FINANCIAL INC. (Defendants)

Stewart J.

Heard: July 26, 2017
Judgment: August 11, 2017
Docket: CV-17-568310

Proceedings: additional reasons at *2468390 Ontario Inc. v. 5F Investment Group Inc.* (2017), 2017 CarswellOnt 20438, 2017 ONSC 5779, Stewart J. (Ont. S.C.J.)

Counsel: Soloman Lam, for Plaintiff
Scott A. Rosen, for Defendants

Subject: Civil Practice and Procedure; Corporate and Commercial; Property
Related Abridgment Classifications
Real property
VII Mortgages
VII.10 Sale
VII.10.f Miscellaneous
Headnote
Real property --- Mortgages — Sale — Miscellaneous
Plaintiff obtained loan from defendants secured by mortgage on property — Plaintiff defaulted on loan and defendants issued notice of sale in foreclosure proceedings claiming principal, interest to date of notice and three months additional interest — Plaintiff obtained financing and repaid amount asking while challenging additional interest — Plaintiff brought action for recovery of additional interest — Both parties brought motions for summary judgment — Plaintiff's motion granted — Section 17 of Mortgages Act did not permit defendant mortgagees to claim additional interest — Notice of Sale was served by mortgagee to exercise recourse against security after mortgage had matured, and s. 17 of Act does not permit defendants to tack on extra three months' interest to other amounts owing under mortgage — Plaintiff entitled to summary judgment against defendants in amount equivalent to three months' interest, as paid by it under protest.
Table of Authorities
Cases considered by *Stewart J.*:
Hornstein v. Orbach (2016), 2016 ONSC 1458, 2016 CarswellOnt 8376 (Ont. Div. Ct.) — referred to
Ialongo v. Serm Investments Ltd. (2007), 2007 CarswellOnt 1246, 54 R.P.R. (4th) 310 (Ont. S.C.J.) — considered
L.I.U.N.A., Local 837 v. 810322 Ontario Ltd. (2006), 2006 CarswellOnt 9295 (Ont. S.C.J. [Commercial List]) — referred to
Mastercraft Properties Ltd. v. EL EF Investments Inc. (1993), 32 R.P.R. (2d) 312, 64 O.A.C. 308, 14 O.R. (3d) 519, 103 D.L.R. (4th) 759, 1993 CarswellOnt 614 (Ont. C.A.) — referred to
Mintz (In Trust) v. Mademont Yonge Inc. (2010), 2010 ONSC 116, 2010 CarswellOnt 912, 91 R.P.R. (4th) 303 (Ont. S.C.J.) — referred to

O'Shanter Development Co. v. Gentra Canada Investments Inc. (1995), 47 R.P.R. (2d) 24, 25 O.R. (3d) 188, 84 O.A.C. 334, 1995 CarswellOnt 399 (Ont. Div. Ct.) — considered

SK Properties & Development Inc. v. Equitable Trust Co. (2003), 2003 CarswellOnt 2130, [2003] O.T.C. 499 (Ont. S.C.J.) — referred to

Shankman v. Mutual Life Assurance Co. of Canada (1985), 52 O.R. (2d) 65, 36 R.P.R. 125, 11 O.A.C. 1, 21 D.L.R. (4th) 131, 1985 CarswellOnt 719 (Ont. C.A.) — considered

Statutes considered:

Courts of Justice Act, R.S.O. 1990, c. C.43

Generally — referred to

Interest Act, R.S.C. 1985, c. I-15

s. 8 — considered

Mortgages Act, R.S.O. 1990, c. M.40

s. 17 — considered

s. 17(1) — considered

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194

R. 20 — pursuant to

MOTIONS by parties for summary judgment in proceedings related to interest charges in mortgage proceedings.

Stewart J.:

Nature of the Motions

1 There are two motions for summary judgment pursuant to Rule 20 brought by the parties. Each motion seeks a determination of the issue in its favour.

2 It is agreed by the parties that the nature of the issue raised is such that it may be determined on the current record by way of motion for summary judgment.

Issue

3 The issue on this motion is whether section 17 of the *Mortgages Act*, R.S.O. 1990, c. M. 40 (the "*Act*") entitles the Defendants to charge three months' additional interest as claimed in a Notice of Sale in respect of a default by the Plaintiff on a mortgage that has matured.

Facts

4 The parties have jointly provided an Agreed Statement of Facts that provides the evidentiary basis for determining the issue raised.

5 On July 31 2015, the Defendants advanced a loan to the Plaintiff in the amount of $7,875,000.00. The loan was secured by a mortgage registered on title to the Plaintiff's property.

6 The mortgage provided for interest at a rate of 9.0% per annum compounded monthly. The Plaintiff was to make interest-only payments for a term of one year until July 31, 2016 at which time the Plaintiff was to repay the principal in full.

7 The agreement between the parties dated June 26, 2015 provided for a possible extension of the mortgage on terms and at the option of the Defendants.

8 The mortgage incorporated by reference Standard Charge Terms and the agreement. None of these documents contains any clause requiring the Plaintiff to pay three months' additional interest in the event of default.

9 The Plaintiff made the required monthly interest-only payments up to the maturity date. On the maturity date, the Plaintiff failed to repay the principal owing and consequently defaulted on the Mortgage.

10 On August 16 2016, the Defendants commenced an action against the Plaintiff for possession of the property (the "2016 Action").

11 On August 23 2016, the Defendants issued a Notice of Sale in respect of the property. The Notice of Sale claimed a total sum owing of $8,100,348.46, consisting of the following:

(a) $7,875,000.00 for principal;

(b) $44,660.96 for regular monthly interest under the mortgage terms from July 31, 2016 to August 23, 2016;

(c) $177,187.50 for an additional three months interest; and

(d) $3,500.00 for costs up to and including service of the Notice of Sale.

12 On September 22 2016, the Plaintiff filed a Statement of Defence to the action which challenged the validity of the Notice of Sale.

13 In November 2016, the Plaintiff obtained a commitment from a third party lender to refinance the property. In connection with the refinancing, the Defendants sent a mortgage discharge statement to the Plaintiff. The mortgage discharge statement included the amount of $8,100,348.46 charged in the Notice of Sale, as well as other amounts said to be owing.

14 On December 23 2016 the Plaintiff paid the Defendants the amount claimed in the mortgage discharge statement, including the three months' interest charged in the Notice of Sale, plus regular interest under the terms of the mortgage accrued up to that date.

15 The Plaintiff made the payment expressly without admission of the validity of the three months' interest charge and reserved all rights to an accounting and to claim back the three months' interest.

16 The refinancing transaction closed and the mortgage was discharged on December 23, 2016.

17 On January 25 2017, the Plaintiff commenced this action for recovery of the disputed three months' interest paid to the Defendants.

18 On March 27 2017, the Defendants delivered a Statement of Defence which identified section 17 of the *Act* as the basis for their claim to entitlement to three months of additional interest in these circumstances.

19 The only issue for determination is whether the Defendants are correct in their interpretation of s.17 of the *Act*.

Law and Discussion

20 Section 17(1) of the *Act* provides:

Payment of principal upon default

> 17 (1) Despite any agreement to the contrary, where default has been made in the payment of any principal money secured by a mortgage of freehold or leasehold property, the mortgagor or person entitled to make such payment may at any time, upon payment of three months interest on the principal money so in arrear, pay

> the same, or the mortgagor or person entitled to make such payment may give the mortgagee at least three months notice, in writing, of the intention to make such payment at a time named in the notice, and in the event of making such payment on the day so named is entitled to make the same without any further payment of interest except to the date of payment.

21 The interpretation and effect of this provision has been the subject of disagreement in the applicable authorities and of debate among practitioners.

22 Section 17 gives the mortgagor, when in default of payment of principal, an opportunity to repay the principal by either giving the mortgagee three months' notice or interest in lieu thereof of his or her intention to make the payment (see: *Mastercraft Properties Ltd. v. EL EF Investments Inc.*, 1993 CarswellOnt 614 (Ont. C.A.)).

23 The purpose of section 17 is to protect mortgagors by permitting payment of arrears without penalty, or by permitting early redemption at a price, while also protecting the mortgagee by giving him a three-month period during which to arrange for reinvestment of his principal, or monies to compensate for lack of that notice. The option to exercise rights under s. 17 is that of the mortgagor (*Mastercraft Properties Ltd. v. EL EF Investments Inc.*, *supra*).

24 Therefore, it is not up to the mortgagee to decide that the three months interest is due in addition to the principal, interest and costs under the mortgage and impose this requirement unilaterally on the mortgagor without regard to the circumstances.

25 Support for the Plaintiff's position may be found in the decision in *Ialongo v. Serm Investments Ltd.*, 2007 CarswellOnt 1246 (Ont. S.C.J.)). That case dealt with a mortgagor who defaulted on a matured mortgage where the mortgagee had chosen to issue a Notice of Sale. Brown, J. (as he then was) held that the mortgagee in such circumstances could not demand payment of three months' interest under s.17 of the *Act* because:

> . . . the rights afforded by section 17 are options made available to the mortgagor on default: it can give notice or pay the bonus prior to the expiry of the notice period. Once, however, the mortgagee takes steps to realize on its security, such as by issuing a notice of sale, it cannot convert the rights of the mortgagor under section 17 into obligations of the mortgagor upon the realization of the security. The amounts a mortgagee may demand from a mortgagor upon realization are those spelled out in the mortgage contract, not in s.17 of the *Mortgages Act.*
>
> In the present case, once the respondent mortgagee issued its Notice of Sale, it was not entitled to demand payment of three months' interest under section 17 of the *Act.* It stood in a fundamentally different position than it did on September 20, 2006 when it provided the applicants with a discharge statement at their request. Once the respondent issued the notice of sale, it was required to look to the terms of the Mortgage to ascertain what amounts it could require the mortgagor to pay in order to redeem the Mortgage. Accordingly, I conclude that once it issued the Notice of Sale the respondent was not entitled to require the applicants to make a payment under s.17 of the *Act.*

26 Counsel for the Plaintiff has pointed out that the decision in *Ialongo v. Serm Investments Ltd.* is consistent with the traditional notion that if the mortgagee takes the decision out of the mortgagor's hands by exercising recourse against the security the mortgagor can redeem immediately without any bonus whatsoever. By commencing a sale under power of sale the mortgagee takes the repayment decision out of the mortgagor's hands. The mortgagee pays for this acceleration by losing its right to the three-month "bonus".

27 In the present case, and applying the approach taken in *Ialongo v. Serm Investments Ltd.*, once the Defendants issued their Notice of Sale they could rely only on the remedies set out in the mortgage and not on any additional "bonus interest" said to be owing under s.17 of the *Act.*

28 The reasoning in the decision in *Ialongo* was applied recently by me, sitting as a single judge of the Divisional Court (see: *Hornstein v. Orbach*, 2016 ONSC 1458 (Ont. Div. Ct.). In that case, an appeal from three Small Claims Court decisions that permitted a mortgagee to charge three months' interest for three properties pursuant to Notices of Sale

and s. 17 of the *Act*, those decisions were reversed. It was held that the trial judge had erred in permitting the three-month interest charge because the mortgages at issue had already matured and were the subject of power of sale proceedings. It was further held that the provisions of s.17 upon which the trial judge relied apply only to the rights of a mortgagor where default in the payment of principal secured by a mortgage of freehold or leasehold property had occurred prior to maturity of the mortgage.

29 It was further noted in *Hornstein v. Orbach* that much of the case law relied on by the Small Claims Court judge involved mortgage agreements which contained a specific provision providing for three-month bonus interest. This was not the case in the mortgages at issue in *Hornstein v. Orbach*. No such provision is present in this action either.

30 In support of their position to the contrary, the Defendants rely on the decision of the Divisional Court in *O'Shanter Development Co. v. Gentra Canada Investments Inc.*, 1995 CarswellOnt 399 (Ont. Div. Ct.)).

31 In *O'Shanter Development Co. v. Gentra Canada Investments Inc.*, a first mortgagee issued a Notice of Sale which contained no three-month interest charge. A second mortgagee issued its own Notice of Sale, sold the property, and sought to repay the first mortgagee. However, the first mortgagee demanded payment of three months' interest on the basis that the mortgage agreement had a "prepayment" clause requiring three months' interest to be prepaid if the default occurred prior to maturity.

32 The Divisional Court held that, because the mortgage was not redeemed within the period set out in the first mortgagee's Notice of Sale, the first mortgagee was no longer bound to accept only the amount claimed in its notice. It was instead entitled to three months' notice for early redemption or payment of three months' interest in lieu thereof, pursuant to the prepayment clause and section 17 of the *Act*. On the basis of the wording of the mortgage contract itself, and subject to the other issues, the first mortgagee was entitled to claim the prepayment amount (three months' interest) in its Notice of Sale.

33 Several subsequent cases have cited this Divisional Court decision as authority for allowing mortgagees to commence a power of sale, force the repayment of principal and also charge three months' additional interest (see: *SK Properties & Development Inc. v. Equitable Trust Co.*, 2003 CarswellOnt 2130, [2003] O.J. No. 2234 (Ont. S.C.J.); *L.I.U.N.A., Local 837 v. 810322 Ontario Ltd.*, 2006 CarswellOnt 9295, [2006] O.J. No. 3260 (Ont. S.C.J. [Commercial List]); *Mintz (In Trust) v. Mademont Yonge Inc.*, 2010 ONSC 116 (Ont. S.C.J.) (CanLII)).

34 Commentators have criticized the decision and have argued that it was either wrongly decided, erroneously applied in subsequent case law, or has limited application. It has been argued that the main problem is that the approach taken converts what was a privilege in favour of the mortgagor under section 17 of the *Act* into a penalty against the mortgagor (see: Jeffrey Lem, "The 'Final' Word on Section 17's Three Month Notice Bonus", *Practice Gems: Mortgage Enforcement Essentials* (Law Society of Upper Canada, September 16, 2014); Steven I. Pearlstein, "The Three Month Mortgage Penalty: Understanding the Principles" (2008: 5th Annual Real Estate Law Summit)).

35 Indeed, in *O'Shanter Development Co. v. Gentra Canada Investments Inc.*, Rosenberg, J. dissented on that point. Relying on *Shankman v. Mutual Life Assurance Co. of Canada* [1985 CarswellOnt 719 (Ont. C.A.)], 1985 CanLII 2196, Rosenberg, J. agreed with the principle that not only can a mortgagee not assert his option to prevent redemption but he cannot impose a penalty on redemption by contract. In his view, service of a Notice of Sale triggers the right to redeem without such a penalty.

36 In this case, the Notice of Sale was served by the mortgagee to exercise recourse against the security after the mortgage had matured. In my view, a proper interpretation of s.17 of the *Act* does not permit the Defendants to tack on an extra three months' interest to the other amounts owing under the mortgage. In my opinion, the Plaintiff's arguments therefore should prevail.

Conclusion

37 For these reasons, the Plaintiff is entitled to summary judgment against the Defendants in the amount equivalent to three months' interest, as paid by it under protest, together with interest in accordance with the *Courts of Justice Act*, R.S.O. 1990.c.C. 43.

38 In view of this determination, the argument based on s.8 of the *Interest Act*, R.S.C. 1985, c. I-15 need not be addressed.

Costs

39 If the subject of costs cannot be agreed upon, written submissions may be delivered by the Plaintiff within 20 days of the date of this decision, and by the Defendants within 20 days thereafter.

Plaintiff's motion granted.

TAB 5

2010 ONCA 854
Ontario Court of Appeal

Romspen Investment Corp. v. 2126921 Ontario Inc.

2010 CarswellOnt 9582, 2010 ONCA 854, [2010] O.J. No. 5405, 196 A.C.W.S. (3d) 105

Romspen Investment Corporation, Applicant (Respondent in Appeal) and 2126921 Ontario Inc., Sidney Orvitz, Carlo Maltese and The Portuguese Canadian Credit Union Limited, Respondents (Appellants in Appeal)

Feldman J.A., Moldaver J.A., Simmons J.A.

Heard: December 10, 2010
Judgment: December 10, 2010
Docket: CA C51865

Proceedings: reversing in part *Romspen Investment Corp. v. 2126921 Ontario Inc.* (2010), 2010 ONSC 317, 2010 CarswellOnt 863 (Ont. S.C.J.)

Counsel: Harry Korosis, Peter Nicholson, for Appellants
Valerie Edwards, David Preger, for Respondent

Subject: Property; Corporate and Commercial; Public

Related Abridgment Classifications

Real property
VII Mortgages
VII.14 Priorities
VII.14.a General principles
VII.14.a.i Notice

Headnote

Real property --- Mortgages — Priorities — General principles — Notice

Mortgagee financed acquisition of motel, restaurant, and parking lands and took back first mortgage — Parking lands were separate parcel but were necessary for operation of motel — Mortgagee's solicitor mistakenly registered mortgage only against motel and restaurant lands — Mortgagor subsequently granted second mortgage over all lands that were properly registered — Mortgagor defaulted on obligations to mortgagee — Mortgagee applied for declaration that it held first charge over parking lands — Application was granted — Mortgagor appealed — Appeal allowed in part — With respect to formal order, until such time as it was registered, it could only give priority to R over appellants' charge and not any subsequent encumbrances had there been any — Accordingly, order was amended nunc pro tunc to give effect to this — Further, leave granted to exercise this power of sale without notice was subject to following proviso, namely: notice must be given to any subsequent encumbrances that existed on day power of sale was exercised.

Table of Authorities

Cases considered:

Dominion Stores Ltd. v. United Trust Co. (1976), 1 R.P.R. 1, 11 N.R. 97, [1977] 2 S.C.R. 915, 71 D.L.R. (3d) 72, 1976 CarswellOnt 383, 1976 CarswellOnt 404 (S.C.C.) — referred to

Holborn Property Investments Inc. v. Romspen Investment Corp. (2008), 2008 CarswellOnt 6914, 77 R.P.R. (4th) 262 (Ont. S.C.J.) — followed

Statutes considered:

Land Titles Act, R.S.O. 1990, c. L.5

s. 93(3) — considered

APPEAL by mortgagor from judgment reported at *Romspen Investment Corp. v. 2126921 Ontario Inc.* (2010), 2010 ONSC 317, 2010 CarswellOnt 863 (Ont. S.C.J.), which granted mortgagee's application for declaration that it held first charge over parking lands.

***Per curiam*:**

1 We are satisfied that the application judge's finding that the appellants had actual notice of the intended priority of the Romspen mortgage necessarily included a finding that the Romspen mortgage was an equitable mortgage in respect of the parking lot. That being so, contrary to the analysis in *Holborn Property Investments Inc. v. Romspen Investment Corp.* (2008), 77 R.P.R. (4th) 262 (Ont. S.C.J.), the application judge was correct in holding that s. 93(3) of the *Land Titles Act* did not preclude Romspen's equitable mortgage from having priority over the appellants' registered mortgage. (See *Dominion Stores Ltd. v. United Trust Co.* (1976), [1977] 2 S.C.R. 915 (S.C.C.), at pp. 956and 957). To that extent, the appeal must fail.

2 With respect to the formal order, until such time as it was registered, it could only give priority to Romspen over the appellants' charge and not any subsequent encumbrancers had there been any.

3 Accordingly, the order is amended *nunc pro tunc* to give effect to this.

4 Further, the leave granted to exercise this power of sale without notice is subject to the following proviso, namely: notice must be given to any subsequent encumbrancers who exist on the day the power of sale is exercised.

5 In light of our conclusion with respect to s. 93(3), we make no comment on the application judge's analysis of unjust enrichment.

6 Costs to the respondent fixed at $12,000 inclusive of disbursements and applicable taxes.

Appeal allowed in part.

TAB 6

2011 ONSC 3648
Ontario Superior Court of Justice

Romspen Investment Corp. v. Woods Property Development Inc.

2011 CarswellOnt 2380, 2011 ONSC 3648, [2011] O.J. No. 1163,
200 A.C.W.S. (3d) 118, 4 R.P.R. (5th) 53, 75 C.B.R. (5th) 109

In the Matter of Section 47(1) of the Bankruptcy and Insolvency Act, R.S.C. 1985, C. B-3, as Amended, and Section 101 of the Courts of Justice Act, R.S.O. 1990 C. C.43, as Amended

Romspen Investment Corporation (Applicant) v. Woods Property Development Inc. and TDCI Holdings Inc. (Respondents)

H.J. Wilton-Siegel J.

Heard: October 25, 2010; November 8, 2010; December 2, 2010
Judgment: March 17, 2011
Docket: CV-08-00007543-00CL

Counsel: Harvin Pitch for Receiver, SF Partners Inc.
David P. Preger for Romspen Investment Corporation, 2204604 Ontario Inc.
Craig A. Mills for Home Depot Canada Inc.

Subject: Property; Corporate and Commercial; Insolvency; Estates and Trusts; Restitution; Contracts
Related Abridgment Classifications
Debtors and creditors
VII Receivers
VII.6 Conduct and liability of receiver
VII.6.a General conduct of receiver
Real property
II Registration of real property
II.3 Improvements made under mistake of title
II.3.b Requirements for relief
II.3.b.i Mistaken belief
Real property
VII Mortgages
VII.14 Priorities
VII.14.b Between types of creditors
VII.14.b.iv Registered mortgagee and equitable interest holder
Real property
VII Mortgages
VII.14 Priorities
VII.14.b Between types of creditors
VII.14.b.xiv Miscellaneous
Real property
VII Mortgages
VII.15 Right of subrogation

Headnote

Real property --- Mortgages — Priorities — Between types of creditors — Miscellaneous

W Inc. owned property (Property) — Mortgages were registered against Property in favour of R Corp. — H Inc. and W Inc. entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of Property (H Lands) — Sale was conditional upon severance of H Lands — H Inc. chose not to register H Agreement or notice of ground lease — H Inc. commenced construction of store on H Lands — R Corp. refinanced earlier mortgages and advanced further funds, securing total financing by mortgage (R Mortgage) registered on title to Property — W Inc. defaulted on R Mortgage, and receiver was appointed — 220 Inc. was owned and controlled by R Corp. — Receiver brought motion seeking approval of agreement of purchase and sale between receiver and 220 Inc. regarding sale of Property, and order vesting Property free of any claims of H Inc. — H Inc. brought cross-motion for various relief regarding Property — Motion granted in part; cross-motion dismissed — With respect to priorities, R Corp. had interest in Property that ranked prior to H Inc.'s interest under H Agreement and ground lease by way of subrogation to extent of monies refinanced under R Mortgage plus interest — R Corp. had actual notice of H Agreement, but not ground lease, at time of execution and registration of R Mortgage — R Corp. had interest in Property that ranked prior to H Inc.'s interest under H Agreement and ground lease by operation of s. 93(3) of Land Titles Act to extent of all monies secured under R Mortgage — H Inc. failed to establish as undisputed fact that R Corp. consented to H Agreement or ground lease such that R Mortgage was subordinated to either or both of these instruments.

Real property --- Mortgages — Priorities — Between types of creditors — Registered mortgagee and equitable interest holder

W Inc. owned property (Property) — Mortgages were registered against Property in favour of R Corp. — H Inc. and W Inc. entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of Property (H Lands) — Sale was conditional upon severance of H Lands — H Inc. chose not to register H Agreement or notice of ground lease — H Inc. commenced construction of store (H store) on H Lands — R Corp. refinanced earlier mortgages and advanced further funds, securing total financing by mortgage (R Mortgage) registered on title to Property — W Inc. defaulted on R Mortgage, and receiver was appointed — 220 Inc. was owned and controlled by R Corp. — Receiver brought motion seeking approval of agreement of purchase and sale between receiver and 220 Inc. regarding sale of Property, and order vesting Property free of any claims of H Inc. — H Inc. brought cross-motion for various relief regarding Property — Motion granted in part; cross-motion dismissed — With respect to priorities, R Mortgage had priority over any equitable lien in favour of H Inc. arising as result of construction of H store on Property — Fact that R Corp. would obtain value of H store was not, by itself, sufficient to determine issue of priority of H Inc.'s lien — H Inc. failed to identify any other equitable consideration that justified imposition of prior lien in absence of R Corp.'s consent to construction of H store — H Inc. failed to show R Corp. consented to construction of H store on H Lands in circumstances that it understood, or should reasonably have understood, H Inc. would have prior lien over H Lands to extent of value of such improvement.

Debtors and creditors --- Receivers — Conduct and liability of receiver — General conduct of receiver

Mortgages in favour of R Corp. were registered against property owned by W Inc. (Property) — H Inc. and W Inc. entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of Property (H Lands), with sale conditional upon severance of H Lands — H Inc. chose not to register H Agreement or notice of ground lease — H Inc. commenced construction of store on H Lands — R Corp. refinanced earlier mortgages and advanced further funds, securing total financing by mortgage (R Mortgage) registered on title to Property — W Inc. defaulted on R Mortgage — Receiver brought motion for approval of sale agreement between receiver and 220 Inc., owned and controlled by R Corp., for Property, and order vesting Property free of claims of H Inc. — H Inc. brought cross-motion — Motion granted in part; cross-motion dismissed — R Corp.'s interest in Property ranked ahead of H Inc.'s to extent of monies secured under R Mortgage or to extent of monies secured under earlier R Corp. mortgages in existence at date of H Agreement plus interest — R Mortgage had priority over any equitable lien of H Inc. arising as result of construction of store — H Inc. failed to establish as undisputed fact that R Corp. consented to H Agreement, ground lease or store construction in manner intended to affect its rights in Property — No equity in H Inc.'s interest in Property — Equities favoured R Corp., so receiver entitled to order permitting sale on basis that it vested out H Inc. interests — Market might have improved since receiver's effort to market Property — Court could not consider approval of sale agreement until receiver conducted sales process on basis that purchaser would be entitled to acquire Property free of any claim of H Inc.

Real property --- Mortgages — Right of subrogation

W Inc. owned property (Property) — Mortgages were registered against Property in favour of R Corp. — H Inc. and W Inc. entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of Property (H Lands) — Sale was conditional upon severance of H Lands — H Inc. chose not to register H Agreement or notice of ground lease — H Inc. commenced construction of store on H Lands — R Corp. refinanced earlier mortgages and advanced further funds, securing total financing by mortgage (R Mortgage) registered on title to Property — W Inc. defaulted on R Mortgage, and receiver was appointed — 220 Inc. was owned and controlled by R Corp. — Receiver brought motion seeking approval of agreement of purchase and sale between receiver and 220 Inc. regarding sale of Property, and order vesting Property free of any claims of H Inc. — H Inc. brought cross-motion for various relief regarding Property — Motion granted in part; cross-motion dismissed — R Corp. had subrogated claim in amount of monies outstanding under earlier R Corp. mortgages at time of their refinancing by means of R Mortgage, plus interest at rates provided under earlier mortgages — R Corp.'s subrogated interest in Property in respect of amounts outstanding under earlier R Corp. mortgages at time of execution of H Agreement ranked prior to H Inc.'s interest in H Lands under H Agreement and ground lease — R Corp. was entitled to assert subrogated claim against Property in priority to that of H Inc. based on principles of unjust enrichment.

Real property --- Registration of real property — Improvements made under mistake of title — Requirements for relief — Mistaken belief

W Inc. owned property (Property) — Mortgages were registered against Property in favour of R Corp. — H Inc. and W Inc. entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of Property (H Lands) — H Inc. commenced construction of store (H store) on H Lands — R Corp. refinanced earlier mortgages and advanced further funds, securing total financing by mortgage (R Mortgage) registered on title to Property — W Inc. defaulted on R Mortgage — Receiver brought motion for approval of sale agreement between receiver and 220 Inc., which was owned and controlled by R Corp., for Property, and order vesting Property free of any claims of H Inc. — H Inc. brought cross-motion for various relief regarding Property — Motion granted in part; cross-motion dismissed — H Inc. was not entitled to lien sought under s. 37(1) of Conveyancing and Law of Property Act (CLPA) in amount of value by which Property had been improved as result of construction of H store — At best, H Inc. had unregistered equitable agreement to purchase H Lands, and that was subject to important qualification — H Agreement provided it would only be effective to create interest in land if provisions of Planning Act were complied with, and that could not occur until severance of H Lands occurred — H Inc. did not have sufficient interest in land under H Agreement to assert claim under s. 37(1) of CLPA — As to ground lease, language of s. 37(1) of CLPA appeared to require belief that lien claimant was owner of relevant property — Court was not provided with any case law that supported proposition that leasehold interest was sufficient interest to obtain relief under s. 37(1) of CLPA, and there was some authority to contrary.

Table of Authorities

Cases considered by *H.J. Wilton-Siegel J.*:

Armatage Motors Ltd. v. Royal Trust Corp. of Canada (1997), 34 O.R. (3d) 599, 1997 CarswellOnt 2758, 12 R.P.R. (3d) 19, 102 O.A.C. 308, 149 D.L.R. (4th) 398 (Ont. C.A.) — distinguished

Capital Funds (I.A.C.) Ltd. v. Park Marine Apartments Ltd. (1967), 62 D.L.R. (2d) 230 (B.C. S.C.) — considered

Chalmers v. Pardoe (1963), [1963] 1 W.L.R. 677, [1963] 3 All E.R. 552 (Fiji P.C.) — followed

Coast Capital Savings Credit Union v. 482451 B.C. Ltd. (2004), 2004 BCSC 40, 2004 CarswellBC 52, 20 R.P.R. (4th) 62, 1 C.B.R. (5th) 1, 30 B.C.L.R. (4th) 177 (B.C. S.C.) — considered

Derro v. Dube (1948), 1948 CarswellOnt 171, [1948] O.W.N. 287, [1948] 2 D.L.R. 296 (Ont. H.C.) — referred to

Dominion Stores Ltd. v. United Trust Co. (1976), 1 R.P.R. 1, 11 N.R. 97, [1977] 2 S.C.R. 915, 71 D.L.R. (3d) 72, 1976 CarswellOnt 383, 1976 CarswellOnt 404 (S.C.C.) — considered

Elias Markets Ltd., Re (2005), 2005 CarswellOnt 3865, 14 C.B.R. (5th) 20, 77 O.R. (3d) 461, 34 R.P.R. (4th) 127, 8 P.P.S.A.C. (3d) 228 (Ont. S.C.J.) — considered

Elias Markets Ltd., Re (2006), 2006 CarswellOnt 5597, (sub nom. *Elias Markets Ltd. (Bankrupt), Re)* 216 O.A.C. 49, 274 D.L.R. (4th) 166, 47 R.P.R. (4th) 32, 25 C.B.R. (5th) 50, 10 P.P.S.A.C. (3d) 255 (Ont. C.A.) — referred to

Geldhof v. Bakai (1982), 139 D.L.R. (3d) 527, 1982 CarswellOnt 1326 (Ont. H.C.) — considered

Goodyear Canada Inc. v. Burnhamthorpe Square Inc. (1998), 43 B.L.R. (2d) 1, 116 O.A.C. 1, 21 R.P.R. (3d) 1, 1998 CarswellOnt 4156, 166 D.L.R. (4th) 625, 41 O.R. (3d) 321 (Ont. C.A.) — referred to

Halton Hills (Town) v. Row Estate (1993), 1993 CarswellOnt 3499 (Ont. Gen. Div.) — referred to

Hatoum v. Hatoum (1988), 1988 CarswellOnt 1543 (Ont. H.C.) — referred to

Hatoum v. Hatoum (1990), 1990 CarswellOnt 3442 (Ont. C.A.) — referred to

Holborn Property Investments Inc. v. Romspen Investment Corp. (2008), 2008 CarswellOnt 6914, 77 R.P.R. (4th) 262 (Ont. S.C.J.) — considered

Isabelle v. Lahaie (2007), 2007 CarswellOnt 8251, 65 R.P.R. (4th) 299 (Ont. S.C.J.) — referred to

Manias v. Norwich Financial Inc. (2008), 76 R.P.R. (4th) 81, 2008 CarswellOnt 3813, 2008 ONCA 532, 238 O.A.C. 253 (Ont. C.A.) — considered

McGuire v. Warren (2006), 2006 CarswellOnt 4267, 46 R.P.R. (4th) 113 (Ont. S.C.J.) — followed

Meridian Credit Union Ltd. v. 984 Bay Street Inc. (2006), 2006 CarswellOnt 4783 (Ont. S.C.J.) — considered

Metzger Estate v. Gardiner (2000), 34 R.P.R. (3d) 79, [2000] O.T.C. 455, 35 E.T.R. (2d) 102, 2000 CarswellOnt 2125 (Ont. S.C.J.) — considered

Midland Mortgage Corp. v. 784401 Ontario Ltd. (1997), 34 O.R. (3d) 594, 1997 CarswellOnt 2762, 102 O.A.C. 226, 12 R.P.R. (3d) 14 (Ont. C.A.) — followed

Montreuil v. Ontario Asphalt Co. (1922), 1922 CarswellOnt 131, 63 S.C.R. 401, 69 D.L.R. 313 (S.C.C.) — referred to

Romspen Investment Corp. v. 2126921 Ontario Inc. (2010), 2010 ONSC 317, 2010 CarswellOnt 863 (Ont. S.C.J.) — distinguished

Romspen Investment Corp. v. 2126921 Ontario Inc. (2010), 2010 ONCA 854, 2010 CarswellOnt 9582 (Ont. C.A.) — considered

Royal Bank v. Soundair Corp. (1991), 7 C.B.R. (3d) 1, 83 D.L.R. (4th) 76, 46 O.A.C. 321, 4 O.R. (3d) 1, 1991 CarswellOnt 205 (Ont. C.A.) — followed

Terastar Realty Corp., Re (2005), 16 C.B.R. (5th) 111, 39 R.P.R. (4th) 1, 2005 CarswellOnt 5985 (Ont. S.C.J.) — considered

Toronto Dominion Bank v. Faulkner (1990), 11 R.P.R. (2d) 161, 71 D.L.R. (4th) 364, 40 O.A.C. 61, 74 O.R. (2d) 92, 1990 CarswellOnt 536 (Ont. C.A.) — referred to

Winick v. 1305067 Ontario Ltd. (2008), 41 C.B.R. (5th) 81, 2008 CarswellOnt 900 (Ont. S.C.J. [Commercial List]) — considered

1420111 Ontario Ltd. v. Paramount Pictures (Canada) Inc. (2001), 45 R.P.R. (3d) 109, [2001] O.T.C. 821, 2001 CarswellOnt 4067, 56 O.R. (3d) 447 (Ont. S.C.J.) — considered

1565397 Ontario Inc., Re (2009), 2009 CarswellOnt 3614, 54 C.B.R. (5th) 262, 81 R.P.R. (4th) 214 (Ont. S.C.J.) — considered

2022177 Ontario Inc. v. Toronto Hanna Properties Ltd. (2005), 203 O.A.C. 220, 17 C.B.R. (5th) 12, 2005 CarswellOnt 5194, 37 R.P.R. (4th) 1 (Ont. C.A.) — considered

Statutes considered:

Conveyancing and Law of Property Act, R.S.O. 1990, c. C.34

s. 37 — referred to

s. 37(1) — considered

Land Titles Act, R.S.O. 1990, c. L.5

Generally — referred to

s. 71(1.1) [en. 1998, c. 18, Sched. E, s. 129] — referred to

s. 93(3) — considered

s. 111(1) — referred to

Planning Act, R.S.O. 1990, c. P.13

Generally — referred to

MOTION by receiver for approval of agreement of purchase and sale regarding certain property, and order vesting property free of any claims of company; CROSS-MOTION by company for various relief relating to property.

H.J. Wilton-Siegel J.:

1 On this motion SF Partners Inc. (the "Receiver") seeks approval of an agreement of purchase and sale dated October 13, 2009 between the Receiver and 2204604 Ontario Inc. (the "Purchaser") (the "Sale Agreement") regarding the sale of a property known municipally as 50 High Street, in the Town of Collingwood, (the "Property") and an order in connection with the completion of such sale vesting in the Purchaser all of the assets of Woods Property Development Inc. ("Woods"), the owner of the Property, free of any claims of Home Depot of Canada Inc. ("Home Depot").

2 By a cross-motion, Home Depot seeks an order that it is entitled to purchase a portion of the Property defined below as the "Home Depot Lands" pursuant to the Home Depot Agreement (as defined below) or to a lease defined below as the "Ground Lease" or, alternatively, that it is entitled to a lien pursuant to section 37 of the *Conveyancing and Law of Property Act*, R.S.O. 1990, c. C-34 (the "CLPA") or in equity that ranks prior to the Romspen Mortgage (as defined below) and, accordingly, should not be affected by any court approval of the transaction contemplated by the Sale Agreement.

Background

The Parties

3 Woods is an Ontario corporation that is the owner of the Property.

4 Romspen Investment Corporation ("Romspen") is a secured lender to Woods and a sister corporation, TDCI Holdings Inc. ("TDCI"), which is the owner of another property in the Town of Collingwood (the "Raglan Property"). The lending arrangements between Romspen and Woods/TDCI are described below. Wesley Roitman ("Roitman") is the chief financial officer of Romspen and the person at Romspen principally responsible for the Woods/TDCI loan arrangements.

5 Holborn Property Investments Inc. ("Holborn") was a proposed purchaser of the Property under the Holborn Sale Agreement (as defined below). Holborn no longer claims an interest in the Property and is no longer a party to these proceedings. The priority of its interest under the Holborn Sale Agreement was the subject of earlier litigation. The judgment of the Court in that litigation was reported as *Holborn Property Investments Inc. v. Romspen Investment Corp.*, [2008] O.J. No. 5722 (Ont. S.C.J.) (the "Holborn Judgment").

6 The Receiver was appointed the interim receiver of all assets, undertakings and properties of Woods and TDCI by order of this Court dated November 25, 2008 (the "Receivership Order").

7 The Purchaser is an Ontario corporation that is owned and controlled by Romspen.

8 Landex Holdings Inc. ("Landex") is an Ontario corporation that owns property immediately to the south of the Property. Landex has entered into a joint venture with the Purchaser to develop the Property should the Purchaser acquire the Property pursuant to the Sale Agreement.

The Property

9 The Property consists of approximately 43 acres. An industrial building on the Property is leased to two tenants with whom the Receiver has reached an agreement and who, therefore, do not oppose the motion.

10 A portion of the industrial building was demolished in 2006. Home Depot constructed a store of approximately 85,000 square feet on a part of the Property that includes the demolished portion of the industrial building (defined below

as the Home Depot Lands) at a total cost of approximately $14.5 million. Construction was completed in January 2007, and a Home Depot store has been operated on that part of the Property since then.

Home Depot's Interest in the Property

11 On or about May 19, 2005, Home Depot entered into an agreement of purchase and sale with Woods whereby Woods agreed to sell Home Depot 8.67 acres of the Property, which included the acreage on which the new Home Depot store was to be located, (the "Home Depot Lands") for $3,250,000. Among other terms, the sale is conditional upon receipt of a severance of the Home Depot Lands from the Property under the *Planning Act*, R.S.O. 1990, c. P-13.

12 On October 17, 2005, Woods entered into a further agreement for the sale of the rest of the Property to Holborn (the "Holborn Sale Agreement"). The Holborn Sale Agreement provided that Home Depot could purchase the Home Depot Lands from Holborn under the Home Depot Agreement for $3,250,000 when a severance was obtained under the *Planning Act*. It was Woods' expectation that the proceeds of sale of the two transactions with Holborn and Home Depot would repay the indebtedness of Woods and TDCI to Romspen described below and leave a profit for Woods.

The Home Depot Agreement

13 The agreement between Woods and Home Depot was amended on November 30, 2005 (as so amended, the "Home Depot Agreement"). It is this agreement upon which Home Depot relies in asserting that it has an interest in the Property. As mentioned, in order to complete the sale transaction, a severance of the Home Depot Lands is required. The severance is, in turn, conditional on among other things, demolition of the industrial building on the Property in its entirety and, as described below, a plan of subdivision for the Property.

14 The Home Depot Agreement contains the following material provisions:

- First, the portion of the industrial building referred to above was to be demolished to permit construction of a Home Depot store.

- Second, Home Depot was obligated to apply for a consent under the *Planning Act* to sever the Property.

- Third, section 4.5 of the Home Depot Agreement states that it shall be effective to create an interest in land only if the provisions of the *Planning Act* have been complied with.

- Fourth, Home Depot shall be entitled to apply to the Town of Collingwood for approval and a building permit to construct a Home Depot store on the Home Depot Lands.

- Fifth, if within 270 days of the date of execution, Home Depot fulfilled all zoning conditions and obtained all necessary approvals for its proposed store including a building permit, Home Depot would take possession of an area slightly larger than the Home Depot Lands pursuant to a ground lease (the "Ground Lease"). As there does not appear to be any significance to this slight difference, in this Endorsement the lands subject to the Ground Lease are also referred to as the "Home Depot Lands" to avoid unnecessary complexity.

15 The Home Depot Agreement set out the following terms for the Ground Lease:

- The Ground Lease was to run for a term of 50 years at a rental of $300,000 per year for the first seven years and thereafter at $100 per year.

- The Ground Lease would terminate upon receipt of the severance of the Property under the *Planning Act*, at which point the Home Depot Agreement would be completed by Home Depot's purchase of the Home Depot Lands, and the rental payments already made would be credited against the purchase price.

16 It was a condition of Home Depot's obligation to enter into the Ground Lease that Woods would deliver to Home Depot an acknowledgement of Romspen's agreement to:

> (1) permit the demolition of the existing industrial building to occur without acceleration of the Romspen mortgages described below; and
>
> (2) provide a partial discharge of the Romspen mortgages upon payment of the purchase price of $3,250,000 under the Home Depot Agreement, without any restriction that such mortgages shall be in good standing at the time.

17 Section 7.11 of the Home Depot Agreement permitted Home Depot to register a caution in respect of its rights under the Home Depot Agreement pursuant to section 71(1.1) of the *Land Titles Act* R.S.O., c. L5, as amended (the "Act"). However, Home Depot chose not register the Agreement. It is understood that Home Depot made this decision in order to avoid the payment of land transfer tax. For the purposes of this proceeding, however, the significant fact is that Home Depot bargained for, but did not exercise, a right of registration and not the particular reason it decided to forgo that registration.

The Ground Lease

18 With the exception of delivery of the acknowledgement, which is described below, Home Depot satisfied the conditions entitling it to take a Ground Lease of the Property on the terms set out above within the time period required under the Home Depot Agreement,. The Ground Lease was signed by Woods and Home Depot on May 4, 2006.

19 Prior to doing so, on April 19, 2006, solicitors for Home Depot conducted a title search against the Property. Accordingly, Home Depot would have been aware at the time it executed the Ground Lease that the Romspen mortgages on the Property at such time had an aggregate face amount of $11.1 million.

20 On May 2, 2006, two days before the Ground Lease was signed, Woods had its mortgage broker Lee Mondrow ("Mondrow") contact Romspen to obtain the acknowledgment from Romspen contemplated by the Home Depot Agreement. However, Romspen was only willing to provide an acknowledgement that demolition of the industrial building would not accelerate the Romspen mortgages (because such demolition would increase the value of the Property). An acknowledgment to this effect was executed by Romspen on May 5, 2006, one day after the Ground Lease was executed.

21 Roitman says that Mondrow and Clive Figuera, on behalf of Woods, had been pressing him to provide a broader acknowledgment to Home Depot in respect of Home Depot's rights under the Home Depot Agreement and that he was unwilling to do so because he did not wish to compromise the priority or other rights of the two Romspen mortgages on the Property at the time. He says further that he would have refused to sign the acknowledgement if it had expressly or impliedly purported to be a postponement or a subordination of Romspen's rights as mortgagee. Home Depot did not contradict this evidence, which I have therefore taken to be an undisputed fact.

22 The Ground Lease contains a representation of Woods that the Home Depot Lands are subject to mortgages in favour of Romspen dated August 22, 2004 (for $8.6 million) and January 26, 2006 (for $2.5 million). In the absence of a Romspen acknowledgment in the form contemplated by the Home Depot Agreement, the Ground Lease contains a further representation of Woods to the effect that Romspen had agreed:

> (1) to permit the demolition of the portion of the industrial building located on the Home Depot Lands without accelerating the Romspen mortgages on the Property at the time; and
>
> (2) to give partial discharges of the Property from the Romspen mortgages "with the aggregate consideration for all such partial discharges being an amount not in excess of the balance of the purchase price payable by

> [Home Depot] under the [Home Depot Agreement] upon the completion of the purchase of the [Home Depot Lands] by [Home Depot] pursuant to the [Home Depot Agreement]."

It is unclear on what basis Woods gave the representation in (2), above, as the Romspen mortgages did not contain partial discharge provisions.

23 Section 19.6 of the Ground Lease addressed registration of the Ground Lease. It provides that Home Depot shall not register the Ground Lease but that either party may register a notice of the Ground Lease pursuant to section 111(1) of the *Land Titles Act* by way of a short form of notice providing certain stipulated information. Home Depot also decided not to register a notice of the Ground Lease, again apparently to avoid the payment of land transfer tax.

24 I think it is obvious from all of the circumstances, including the testimony of Sylvain Rivet, a senior real estate manager of Home Depot, the fact that Home Depot was advised by experienced solicitors, Home Depot's experience in real estate law given its extensive real estate operations, and the title subsearch of its solicitors in April 2006, that Home Depot made a conscious decision to execute the Ground Lease without obtaining the form of acknowledgment of Romspen contemplated by the Home Depot Agreement, and to forego registration of the Ground Lease, with full knowledge of the potential risks that such actions could entail.

Construction of the Home Depot Store

25 As mentioned, during 2006, Home Depot commenced construction of a store upon the Home Depot Lands.

26 In connection with such construction, on or about July 25, 2006, Romspen signed a site plan control agreement dated July 20, 2006 to which Woods, Home Depot and the Town of Collingwood were also parties (the "Site Plan Agreement'). The Site Plan Agreement specifically recites the existence of the Home Depot Agreement, although not the Ground Lease. It also recites the proposed demolition of the portion of the existing industrial building and the proposed construction of the Home Depot store.

27 Paragraph 32 of the Site Plan Agreement refers to the existence of Romspen charges on the Property in the respective amounts of $8.6 million and $2.5 million (being the earlier Romspen mortgages, which, by this time, however, had been replaced by the Romspen Mortgage) and contains an express postponement and subordination by Romspen of its interest in the Property to that of the Town of Collingwood under the Site Plan Agreement (but not to that of Home Depot). This is the only express covenant of Romspen in the Site Plan Agreement, which otherwise contains covenants of Woods and Home Depot regarding the construction of the Home Depot store on the Property.

28 Home Depot has applied for severance of the Home Depot Lands. However, it is understood that the Town of Collingwood will not consent to a severance until a comprehensive plan of subdivision is filed and approved for the entire Property. No plan of subdivision has been filed by Woods or any other party having a present or future interest in the Property. The Receiver is not proposing to file a plan of subdivision on its own.

Romspen's Interest in the Property

Mortgages Prior to July 6, 2006

29 At the time of the first agreement between Woods and Home Depot dated May 19, 2005, there were two mortgages registered against the Property in favour of Romspen. The first mortgage dated August 27, 2004 secured a loan in the principal amount of $8.6 million. The second mortgage dated January 26, 2005 secured a loan in the principal amount of $1,550,000 made to TDCI that was guaranteed by Woods. This second mortgage was also secured against the Raglan Property.

30 In September 2005, Romspen loaned an additional $500,000 to Woods that was secured by a further mortgage on the Property, bringing the total amount secured against the Property to $10,650,000. None of these mortgages contained a right of partial discharge in favour of Woods to allow it to sell the Home Depot Lands, although the mortgage dated

January 26, 2005 provided for a discharge of the Property upon repayment of an amount to be determined by Romspen in its discretion up to the full outstanding amount.

31 Accordingly, at the time of the Home Depot Agreement dated November 30, 2005, there were three mortgages registered against the Property in favour of Romspen, securing loans totalling $10.65 million in principal amount.

32 On January 26, 2006, Romspen refinanced the second and third mortgages on the Property and made a further secured advance. This was effected through the issue of a new second mortgage loan dated January 17, 2006 in the principal amount of $2.5 million made to TDCI of which Woods was the guarantor. This new second mortgage was also registered against both the Property and the Raglan Property. The new second mortgage did not contain a partial discharge provision.

33 Accordingly, at the time of execution of the Ground Lease on or about May 4, 2006, there were two mortgages registered against the Property in favour of Romspen securing loans totalling $11.1 million — the mortgage dated August 27, 2004 and the mortgage dated January 17, 2006. Neither mortgage contained a partial discharge provision.

The $17 Million Romspen Mortgage

34 On June 1, 2006, Romspen provided Woods with a commitment letter (the "Commitment Letter") regarding an advance of further funds to discharge the existing Romspen mortgages against the Property, as well as a further mortgage in the principal amount of $3.6 million secured against the Raglan Property only, and to finance improvements on the Raglan Property. All such advances were to be secured against both the Property and the Raglan Property.

35 This transaction was completed on or about July 6, 2006, at which time Romspen advanced a total of approximately $17 million, of which $11,338,090.84 was advanced to discharge the three existing Romspen mortgages secured against the Property and to pay realty taxes on High Street. The total financing was secured against the Property and the Raglan Property by a joint mortgage of Woods and TDCI in the principal amount of $17 million (the "Romspen Mortgage"), which was registered on title on July 6, 2006. Subsequently, the earlier Romspen mortgages were discharged after an appropriate "seasoning period".

36 The Romspen Mortgage contained a provision allowing Woods a partial discharge of the Home Depot Lands upon payment of the purchase price under the Home Depot Agreement, provided that the Romspen Mortgage was not in default and that a loan-to-value covenant was satisfied in Romspen's sole determination after giving effect to the partial discharge.

37 The Romspen Mortgage also incorporated the following provision from the Commitment Letter, which contemplated land lease payments under the Home Depot Agreement without specifically referring to the Ground Lease:

> Monthly principal payments of $130,000 shall be due and payable on the same day each month. In addition, any land lease payments made by Home Depot pursuant to the Home Depot Agreement (both as defined below) which in aggregate exceed $250,000 shall be due and payable on account of principal, upon receipt and the Borrower shall direct Home Depot to make such payments directly to Lender.

Romspen's Knowledge of the Home Depot Agreement and the Ground Lease

Knowledge of the Home Depot Agreement

38 Roitman acknowledges that Romspen received a copy of the Home Depot Agreement in or about November 2005. Accordingly, it had knowledge from that time of the arrangements contemplated in that Agreement in respect of both the sale of the Home Depot Lands and a possible ground lease of the Home Depot Lands.

Knowledge of the Ground Lease

39 Home Depot submits that the Court should infer that Romspen had actual knowledge of the existence of the Ground Lease, if not its actual contents, as of the date of execution and delivery of the Romspen Mortgage or, alternatively, as of the date of execution of the Site Plan Agreement. It relies upon the covenant in the Romspen Mortgage (by incorporation of the terms of the Commitment Letter) requiring payment to Romspen of land lease payments in excess of $250,000 as evidence of such actual knowledge at the time of the Romspen Mortgage. In the alternative, it says that, given the structure of the Home Depot Agreement, Roitman must have known that Woods and Home Depot had executed the Ground Lease when he was presented with the Site Plan Agreement for Romspen's execution.

40 As this is a motion, the Court cannot make findings of fact by way of inference. The Court must make its determinations on the basis of undisputed facts.

41 In this case, there is no evidence that Romspen had actual knowledge of the existence of the Ground Lease prior to receiving a copy of the Ground Lease in 2008, much less that such knowledge is an undisputed fact. At best, and as Home Depot states in its factum, "Romspen was aware that an interim land lease might be entered into at a later date". This falls short of actual knowledge of the existence of the Ground Lease prior to 2008.

42 Even if the Court were able to draw inferences of fact, I do not think that such knowledge could be inferred as of the date of execution of the Romspen Mortgage, even on a balance of probabilities standard, from the facts before the Court. The language of the Romspen Mortgage is hardly unequivocal evidence of knowledge. Moreover, the fact that the Commitment Letter did not refer specifically to the Ground Lease but rather to "any land lease payments made by Home Depot", and the fact that Romspen did not pursue repayment of the Romspen Mortgage due as a result of rental payments under the Ground Lease, are both consistent with an absence of actual knowledge on Romspen's part.

43 Similarly, I do not think that the Court could infer knowledge of the Ground Lease from Romspen's execution of the Site Plan Agreement. While Romspen may have had suspicions that Home Depot had received a Ground Lease when it received the Site Plan Agreement for execution, Home Depot has not established actual knowledge as of that time. As Romspen also points out, execution of the Ground Lease was inconsistent with several conditions of the Home Depot Agreement as Romspen understood them.

Romspen's Alleged Consent to the Home Depot Agreement and the Ground Lease and to the Construction of the Home Depot Store

44 Home Depot also argues that Romspen consented to the Home Depot Agreement and the Ground Lease as well as to the construction of the Home Depot store. I will address each of these issues in turn. Again, as this is a motion, Home Depot must establish any alleged consent as an undisputed fact. In my view, it has failed to satisfy this onus.

Alleged Romspen Consent to the Home Depot Agreement and the Ground Lease

45 Romspen had actual knowledge of the Home Depot Agreement from November 2005. However, such knowledge does not automatically imply or constitute consent to the subordination of Romspen's earlier mortgages to the Home Depot Agreement. After learning of the Home Depot Agreement, Romspen had no obligation to contact Home Depot to inquire as to whether it sought, or assumed that it had received, Romspen's consent to the Agreement. It was entitled to assume that Home Depot would do what it considered necessary to protect itself as a party having a subordinate interest in the Property. That legal position remained unchanged at the time of execution of the Romspen Mortgage notwithstanding that the Romspen Mortgage was executed after the Home Depot Agreement.

46 Home Depot acknowledges that it never sought any form of consent, subordination and postponement of rights, or non-disturbance agreement from Romspen with respect to the Home Depot Agreement. Nor did Romspen ever agree in favour of Woods or Home Depot to a partial discharge of the Property to permit the sale of the Home Depot Lands. There is, therefore, no evidence that Romspen ever consented, orally or in writing, to the sale of the Home Depot Lands

pursuant to the Home Depot Agreement or to the subordination of its interest in the Property, whether under the earlier Romspen mortgages or under the Romspen Mortgage, to the interest of Home Depot under the Home Depot Agreement.

47 I have concluded above that Romspen did not have actual knowledge of the Ground Lease prior to 2008. Home Depot never sought the consent of Romspen to the Ground Lease. Nor did it ever seek any form of subordination or non-disturbance agreement from Romspen in respect of the Ground Lease. Collectively, these facts exclude any determination that Romspen consented to the Ground Lease or to the subordination of its interest in the Property to the interest of Home Depot under the Ground Lease.

48 Insofar as it may be argued that Romspen's knowledge of the Home Depot Agreement constituted an implied consent to a lease as described in the Home Depot Agreement, even without actual knowledge of the execution of the Ground Lease, I think the argument must fail for the same reasons as I concluded that knowledge of the Home Depot Agreement did not imply Romspen's consent to that document.

49 Generally, Home Depot relies on the affidavit of Sylvain Rivet, a senior real estate manager of Home Depot, in which he deposed that it was Home Depot's understanding at all times that Romspen had consented to the Home Depot Agreement and the Ground Lease, as well as to Home Depot's interest in the Home Depot Lands. There is, however, no basis in the evidence for this understanding. To the extent that Home Depot says that it relied on Woods' representation in the Ground Lease that Romspen had consented to the Home Depot Agreement and the Ground Lease, such reliance was clearly unreasonable. Neither Woods nor Home Depot has provided any evidence of Romspen's advice or other comfort to Woods or Home Depot that supports this representation.

50 Accordingly, I have proceeded on the basis that Romspen did not consent at any time to either the Home Depot Agreement, the Ground Lease, or to any interest in the Home Depot Lands that Home Depot may have acquired thereunder.

Alleged Romspen Consent to the Construction of the Home Depot Store

51 There is a separate question regarding whether Romspen consented at some point in time to the construction of the Home Depot store. This issue is relevant to the priority of any lien against the Property in Home Depot's favour in respect of an improvement to the Property as opposed to the priority of the Home Depot Agreement and the Ground Lease in the Property *per se*.

52 There is no evidence of any such consent, and it cannot be inferred from the existence of the Home Depot Agreement. Nor can it be inferred from the existence of the Ground Lease of which, in any event, I have found Romspen had no knowledge prior to 2008. The remaining possibility is that, in some manner, Romspen's execution of the Site Plan Agreement constitutes its consent, or constitutes evidence of its consent given elsewhere, to the construction of the Home Depot store in a manner that is meaningful for this proceeding.

53 Home Depot cannot, however, establish as an undisputed fact that Romspen's execution of the Site Plan Agreement either constituted, or evidenced, its consent to such construction. The reasons for this conclusion are set out below in addressing the priority of any lien of Home Depot against the Property in respect of such improvement.

The Proposed Sale of the Property

54 Woods first defaulted on the Romspen Mortgage in 2007, and payments ceased on the Romspen Mortgage in January 2008, leading to the Receiver's appointment on November 25, 2008. The Receivership Order authorized the Receiver to market the Property.

55 The Receiver listed the Property for sale with Parallel Realty Inc. ("Parallel") for a listing price of $450,000 per acre. In an offering fact sheet prepared by Parallel for distribution to prospective purchasers, the Home Depot Agreement was disclosed in the following terms:

> The developer has agreed to sell 8.67 acres of the property to Home Depot, which has constructed and opened its 85,500 square foot store. Home Depot is currently leasing its portion of the property until a severance can be applied for...

56 The Receiver's report lists the efforts of Parallel to market the Property. They include listing the property on MLS and a further listing service, advertising in two editions of the Report on Business, and responding to inquiries of numerous interested parties. Parallel has followed up on expressions of interest from more than 25 prospective purchasers. Despite such efforts, no offers have been received.

57 On October 13, 2009, the Receiver and the Purchaser entered into the Sale Agreement. The material terms of the Sale Agreement are:

> (1) a purchase price of $14.1 million satisfied by a partial reduction of the current indebtedness to Romspen under the Romspen Mortgage (apart from certain cash expenses to be paid, including outstanding realty taxes and the Receiver's fees and borrowings, if any); and
>
> (2) vacant possession of the Property or arrangements with any remaining tenants on terms satisfactory to the Purchaser in its sole discretion.

58 As no arrangements have been made with Home Depot, as the lessee under the Ground Lease, the Receiver seeks an order vesting the Property free and clear of the Home Depot Sale Agreement, the Ground Lease and any other lien in favour of Home Depot arising in respect of the construction of the Home Depot store.

Applicable Law

59 The factors that a Court should consider in determining whether to approve a sale by a Court-appointed receiver were set out by Galligan J.A. in *Royal Bank v. Soundair Corp.* (1991), 4 O.R. (3d) 1 (Ont. C.A.) at para. 16 as follows:

> 1. It should consider whether the receiver has made a sufficient effort to get the best price and has not acted improvidently.
>
> 2. It should consider the interests of all parties.
>
> 3. It should consider the efficacy and integrity of the process by which offers are obtained.
>
> 4. It should consider whether there has been unfairness in the working out of the process.

60 In the present proceeding, there are two specific issues to be considered:

> 1. whether the Court should vest the Property in the Purchaser free and clear of the interest of Home Depot in the Property, which is a condition of the completion of the transaction contemplated by the Sale Agreement; and
>
> 2. whether the Property has been marketed to prospective purchasers on the same basis as is contemplated in the Sale Agreement.

61 The first issue relates to the consideration of the interests of the parties. The second relates to the efficiency and integrity of the sales process. I will deal with each in turn.

Should the Court Order a Vesting of the Property Free and Clear of any Claims of Home Depot?

62 This motion raises four general issues that are addressed below:

1. Does the Court have the authority to grant an order "vesting out" Home Depot's interest in the Property?

2. Does Romspen have an interest in the Property ranking prior to Home Depot's interest?

3. Is Romspen's interest in the Property subordinated to Home Depot's interest by virtue of a consent?

4. Is Home Depot entitled to a lien against the Property ranking in priority to Romspen's interest by virtue of the construction of the Home Depot store?

I propose to address each issue in turn. I will then address the Receiver's request for an order vesting out Home Depot's interest in the Property setting out my assessment of the equities between the parties.

Does the Court Have the Authority to Grant the Requested Relief?

63 The first issue is whether the Court has the authority to issue an order granting the requested relief. Home Depot makes two arguments that it does not. It says that a court-appointed receiver is not entitled to evict a tenant merely because it would be advantageous to do so. It also submits that that the Receiver did not receive the equity in the Home Depot Lands upon its appointment and therefore does not have the power to convey the Property free of Home Depot's interest. I will address each issue in turn.

Authority of the Court to Issue A "Vesting Out" Order in Respect of a Leasehold Interest

64 Home Depot relies on the following cases in support of its position that the Court cannot order the Receiver to sell the Property free and clear of the interest of Home Depot in the Home Depot Lands and, in particular, free and clear of the Ground Lease: *Coast Capital Savings Credit Union v. 482451 B.C. Ltd.*, [2004] B.C.J. No. 46 (B.C. S.C.) at paras. 12-14; *Capital Funds (I.A.C.) Ltd. v. Park Marine Apartments Ltd.*, [1967] B.C.J. No. 132 (B.C. S.C.) at paras. 9-10; and *Winick v. 1305067 Ontario Ltd.*, [2008] O.J. No. 695 (Ont. S.C.J. [Commercial List]) at para. 15.

65 These decisions do not articulate an absolute and unqualified rule that the Court lacks the authority to vest out a leasehold interest. Instead, they mandate that a receiver take into consideration the equities of the positions of the various parties involved. The principle is well summarized by Ground J. in *Meridian Credit Union Ltd. v. 984 Bay Street Inc.*, [2006] O.J. No. 3169 (Ont. S.C.J.) at para. 19 as follows:

> I think the law is clear that, if Meridian had proceeded by way of power of sale, it could have sold the Property to a purchaser free and clear of the leasehold interest of BW Health and Integrated on the basis that the subordination provision contained in the leases clearly subordinate the rights of the tenants to the rights of Meridian under the Meridian Charge and on the basis that none of the leases was registered on title to the property. This sale is, however, being conducted by a court-appointed receiver and, when seeking to convey title to assets free and clear of the interest of other parties, a receiver must apply to the court for a vesting order. In *New Skeena Products Inc. v. Kitwanga Lumber Co.* (2005), 75 D.L.R. (4th) 328, the British Columbia Court of Appeal clearly states that, in determining whether to issue a vesting order terminating in the interests of parties in a property, the court must review the equitable considerations supporting the respective positions of the parties.

The same conclusion was expressed by Gill J. in *Capital Funds, supra* in his reference to the fiduciary obligation of a court-appointed receiver to all the parties involved in a contest.

66 Accordingly, I have proceeded on the basis that the Court has the authority to grant the relief requested provided it is appropriate to do so after reviewing the equitable considerations supporting the respective positions of the parties.

67 I would note, as well, that the cases relied upon by Home Depot do not provide much assistance with respect to the equitable considerations to be taken into account in the present proceeding inasmuch as the circumstances in those decisions were very different.

68 *Coast Capital Savings*, *supra* involved residential tenancies which were not registrable and for which the tenants had prepaid the rental for the year. It is also unclear from the incomplete recitation of the facts whether the mortgagee seeking the relief was likely to be repaid or not; the references of the trial judge to the obligation of a court-appointed receiver to protect the goodwill of a business suggests that there may have been other subsequent encumbrancers with an interest in the preservation of the existing tenancies.

69 In *Capital Funds*, it was established that the tenant had paid considerable amounts for rent and for renovations to the property in respect of a commercial tenancy.

70 In *Winick*, *supra*, Pepall J. considered the issue in the context of the requirement in *Soundair*, *supra* that the Court address whether there has been unfairness in the working out of the sale process. In that case, the purchaser had agreed to acquire the property subject to the relevant lease. There was therefore no suggestion that the sale price would have been affected by the continuation of the lease. In such circumstances, it would have been unconscionable to order a vesting out of the lease.

71 As mentioned above, I propose to consider the equitable considerations between the parties after discussion of the remaining issues outlined above, which will themselves involve a consideration of certain equitable considerations.

The Home Depot Lands Were Previously Conveyed

72 Home Depot also submits that that the Receiver did not receive the equity in the Home Depot Lands upon its appointment and therefore does not have the power to convey the Property free of Home Depot's interest. In making this submission, it relies on the decisions in *2022177 Ontario Inc. v. Toronto Hanna Properties Ltd.* (2005), 203 O.A.C. 220 (Ont. C.A.); *Terastar Realty Corp., Re* (2005), 16 C.B.R. (5th) 111 (Ont. S.C.J.); and *1565397 Ontario Inc., Re* (Ont. S.C.J.).

73 The Home Depot argument on this issue is based on the legal consequences of the Home Depot Agreement and the Ground Lease. It submits that the Home Depot Agreement created an equitable interest in the Property in favour of Home Depot that was therefore excluded from the assets subject to the Receivership Order. Similarly, Home Depot has a leasehold interest in the Home Depot Lands under the Ground Lease. Home Depot submits that these interests were excluded from the assets subject to the Receivership Order and cannot be extinguished by a transfer of the Property by the Receiver.

74 I accept the starting point of Home Depot's analysis. Because the Receiver has been appointed as the receiver of Woods' assets, the effect of the Receivership Order is to transfer possession of the Property to the Receiver, subject to Home Depot's interest in the Property under the Home Depot Agreement and the Ground Lease. Nevertheless, I conclude that Home Depot's submission must fail for two reasons.

75 First, in respect of the Home Depot Agreement, section 4.5 provides that it is effective to create an interest in land only if the provisions of the *Planning Act* have been complied with. This has not yet occurred. It would therefore appear that Home Depot does not presently have an enforceable equitable interest in the land under the Home Depot Agreement and may never have such an interest.

76 Second, and in any event, the issue in the present proceedings is not whether Woods granted Home Depot a lease pursuant to the Ground Lease and an equitable interest pursuant to the Home Depot Agreement to the extent it has such an interest notwithstanding section 4.5. That is conceded by Romspen. At issue are the priorities and the equities between Home Depot and Romspen.

77 In this context, while Home Depot is correct that the Receivership Order did not give the Receiver such authority, its submission ignores the nature of the Court's authority in the present circumstances. The Receiver does not rely on

its authority under the Receivership Order in seeking a "vesting out" order. Instead, it relies upon the Court's inherent jurisdiction to order a vesting out of interests in property after a consideration of the equities between the parties.

78 Accordingly, I do not accept Home Depot's argument that the Receiver lacks the power to convey the Property free of Home Depot's interest because it did not receive the equity in the Home Depot Lands upon its appointment. The Court has the authority to authorize the Receiver to sell the Property free and clear of the interest of Home Depot after a consideration of the equities between the parties. Put another way, the Court may refuse to exercise its equitable jurisdiction to enforce Home Depot's equitable interests if it determines that it is appropriate to refrain from doing so after considering the equities between the parties.

Conclusion Regarding Authority of the Court

79 Based on the foregoing, I conclude that the Court has the authority to grant the requested relief if, in the circumstances, after reviewing the applicable equitable considerations relating to the respective positions of the parties, it is appropriate to do so.

Does Romspen Have an Interest in the Property Ranking Prior to Home Depot's Interest?

80 Romspen asserts that its interest in the Romspen Mortgage ranks prior to Home Depot's interest in the Home Depot Lands on two general grounds. First, it submits that the Romspen Mortgage is entitled to priority by virtue of its registration under the *Land Titles Act*, notwithstanding actual notice of the Home Depot Agreement and the Ground Lease, which were executed earlier but never registered under the Act. Second, it argues that it has a subrogated claim under the Romspen Mortgage to the extent of the monies secured under the earlier Romspen mortgages and refinanced by the Romspen Mortgage plus interest thereon at the rates provided under such mortgages.

81 I propose to consider the two submissions of Romspen in reverse order.

Romspen's Assertion of Priority Based on Subrogation

Romspen's Position

82 Romspen submits that it has a claim against the Property under the Romspen Mortgage by way of subrogation in respect of the amounts outstanding under the Romspen mortgages as of either November 30, 2005 (the date of the Home Depot Agreement) or April 26, 2006 (the date Romspen uses as the date of execution of the Ground Lease).

83 On either calculation, the total of the monies outstanding under these mortgages, as of February 1, 2010, appears to substantially exceed the value of the Property. According to Romspen's calculation, as of February 1, 2010, the amount outstanding under the two Romspen mortgages secured against the Property as of the date of the Home Depot Agreement (November 30, 2005) — being the mortgages in the principal amounts of $8.6 million and $1.550 million, respectively — was $17,844,975.38. In addition, as of February 1, 2010, the amount outstanding under the two Romspen mortgages secured against the Property as of the date of the Ground Lease (the date used by Romspen is April 26, 2005) — being the mortgages in the principal amounts of $8.6 million and $2.5 million, respectively — was $18,102,971.09.

84 Romspen acknowledges that the priority of its claim by way of subrogation is limited to the monies paid at the time of the refinancing of the relevant Romspen mortgages to discharge such mortgages plus interest thereon at the rates applicable under such mortgages. It is my understanding that the calculations set out above have been prepared on this basis and are not challenged by Home Depot.

85 Romspen's argument is based on the line of cases that establishes that a mortgagee who pays off prior encumbrances is entitled to be subrogated to the payee's priority position relative to other clients: see, for example, *Elias Markets Ltd., Re* (2005), 34 R.P.R. (4th) 127 (Ont. S.C.J.) at para. 43 per Rady J., aff'd (2006), 47 R.P.R. (4th) 32 (Ont. C.A.). The principle was applied to a first mortgagee who "renews, replaces, refinances, amends or increases his mortgage": see *Midland Mortgage Corp. v. 784401 Ontario Ltd.* (1997), 34 O.R. (3d) 594 (Ont. C.A.) at para. 14 per Austin J.A. The

doctrine also applies to the extent a mortgagee pays taxes on behalf of a mortgagor: see *Elias Markets Ltd., Re, supra*, at para. 50 per Rady J.

86 Romspen argues that it is entitled to rank prior to Home Depot's interest in the Home Depot Lands to the extent of this subrogated claim based on the equities between the parties. In particular, it relies on the fact that Home Depot had knowledge of the Romspen mortgages on the Property at the time it executed the Home Depot Agreement and the Ground Lease based on their registration against title to the Property. It also relies on the fact that Home Depot did not seek either a non-disturbance or priority agreement from Romspen notwithstanding the priority of the Romspen mortgages at the time. Nor did Home Depot receive any consent or other protection from Romspen. Instead, it relied on incorrect representations from Woods in the Ground Lease when it was executed, without seeking confirmation of the validity of these representations. Romspen notes that Home Depot took these decisions without any representation on the part of Romspen. In addition, Romspen relies on its right to control partial discharges of the Property from its security, of which Home Depot had knowledge by virtue of the registration of Romspen's earlier mortgages.

Home Depot's Position

87 Home Depot notes that subrogation is a discretionary remedy for which the foundation is fairness. In reliance on J. McGhee, ed. *Snell's Equity* 31st ed. (Toronto: Thomson, 2005) at p. 869, it argues there are three conditions that must be satisfied before the doctrine can operate: (1) the subsequent encumbrancer is unjustly enriched at the lender's expense; (2) such enrichment is unjust; and (3) there are no policy reasons for denying the prior encumbrancer a remedy. It makes four submissions for denying the remedy of subrogation in the present circumstances, which I will address below.

Analysis and Conclusions

Preliminary Issue

88 Before addressing this issue, it is necessary to consider whether Romspen's subrogated claim should be considered in respect of monies outstanding under the earlier Romspen mortgages at the date of execution of the Home Depot Agreement, the date of execution of the Ground Lease, or both. The Home Depot Agreement and Ground Lease were both granted after the earlier Romspen mortgages described above but before the Romspen Mortgage. Although the parties have distinguished the rights and interests of Home Depot under the Home Depot Agreement and the Ground Lease, I do not think this distinction is meaningful for the purposes of determining against which mortgages Home Depot's priority based on subrogation is to be considered.

89 The Ground Lease was an interim measure to bridge the period until a severance was obtained and the transaction contemplated by the Home Depot Agreement could be completed. The possibility of a ground lease having terms substantially similar to the terms of the Ground Lease was contemplated in the Home Depot Agreement. The rental payments under the Ground Lease were a credit against the purchase price under the Home Depot Agreement. In these circumstances, I think that the priority of Romspen's subrogated claim under the Romspen Mortgage should be considered in respect of the monies outstanding under the earlier Romspen mortgages outstanding as of the date of the Home Depot Agreement.

Validity of Romspen's Claim for Priority By Way of Subrogation

90 On the facts of this case, I do not think that there is any doubt that Romspen has a subrogated claim in the amount of the monies outstanding under the earlier Romspen mortgages at the time of their refinancing by means of the Romspen Mortgage, plus interest at the rates provided under the earlier Romspen mortgages. The principle in *Midland Mortgage*, *supra* is well established law. There are no facts that exclude the operation of this principle in the present proceeding. The issue for the Court is whether the test for entitlement to the remedy of subrogation is met.

Assessment of the Equitable Considerations

91 In making their submissions on this issue, Home Depot relies on the test for subrogation set out in *Snell*, described above. Romspen relies on the analysis of unjust enrichment. I am not convinced that there is any significant difference between the two approaches, subject to one consideration discussed in the next paragraph. I will, however, consider each of these approaches in turn.

92 It should be noted that, in respect of Romspen's claim of priority for its interest in the Property based on subrogation, the interest of Home Depot at issue is its interest under the Home Depot Agreement and the Ground Lease, not the Home Depot store. In the absence of any evidence that Romspen consented to the construction of the Home Depot store in a manner that was intended to affect its legal rights in the Property, the issue of the Home Depot store must be considered in the context of an improvement on the Property. That is addressed later. In this section, the issue is limited to the right of Home Depot to acquire the Home Depot Lands under the Home Depot Agreement and, possibly, to hold a leasehold interest in the Home Depot Lands under the Ground Lease.

93 The starting point for the analysis of unjust enrichment is whether Home Depot would be enriched if the remedy of subrogation were unavailable to Romspen. I think it is clear that it would be. The Home Depot Agreement and the Ground Lease were executed after the earlier Romspen mortgages. Therefore, they ranked after such mortgages. If subrogation were not granted, Home Depot's interest in the Property would rank in priority to the interest of Romspen in the Property. Accordingly, in the present circumstances, there would be an enrichment of Home Depot and a corresponding deprivation of Romspen if subrogation were not ordered.

94 I am also satisfied that there is an absence of a juristic reason for Home Depot's enrichment. In respect of this issue, the following considerations are relevant.

95 First, insofar as Home Depot seeks to enforce the Home Depot Agreement, it is effectively seeking an order compelling Romspen to discharge the security contained in the earlier Romspen mortgages which has been continued in the Romspen Mortgage. The Court should not relieve Home Depot of the risk that it knowingly assumed by its own actions.

96 As mentioned, the Romspen mortgage loans were secured against the entire Property and provided Romspen with an absolute control over partial discharges. Even if a severance had been obtained, Home Depot could only have completed the purchase if Romspen had been willing to deliver a partial discharge. Home Depot had full knowledge of that risk. By entering into the Home Depot Agreement without obtaining a non-disturbance or priority agreement with Romspen, Home Depot took the risk that the Home Depot Lands would not be deliverable to it. Home Depot could not have obtained an order of the Court compelling delivery to it of the Home Depot Lands free of the earlier Romspen mortgages. There is no reason why the refinancing of those mortgages should increase its rights in this respect.

97 Second, the evidence before the Court suggests that the present circumstances were not anticipated by either party. However, at the time of execution of the Home Depot Agreement and the Ground Lease, the priority of the Romspen mortgages registered on title to the Property was absolutely clear. Both parties were sophisticated business entities with access to experienced and knowledgeable legal counsel. Romspen did everything that it could to protect itself against unanticipated circumstances. Home Depot did not.

98 To protect itself, Home Depot needed to obtain a consent, a priorities agreement, or a non-disturbance agreement directly from Romspen in respect of the Home Depot Agreement, the Ground Lease, or both. It made a business decision not to require Woods to obtain the form of comfort contemplated by the Home Depot Agreement and to rely instead upon representations from Woods — which proved to be incorrect — without seeking any indication from Romspen regarding the validity of those representations.

99 On the other hand, Romspen chose to protect its security position by retaining absolute control over any partial discharges of the Property under the earlier Romspen mortgages. It was under no obligation to anticipate the situation

that subsequently developed. Nor did it have an obligation to advise Home Depot of the risks associated with failure to seek a consent or other comfort from Romspen.

100 Third, Home Depot argues that there is no evidence that it has derived any value or enrichment from Romspen's refinancing of the earlier Romspen mortgages by means of the Romspen Mortgage and that, on the other hand, Romspen has derived real value from Home Depot's construction and operation of its store on the Home Depot Lands. For the same reason, Home Depot says that, if its interest is vested out, Romspen will be unjustly enriched by virtue of the construction of the Home Depot store on the Property.

101 These two amount to a single argument. More importantly, I do not think this argument has any force to the extent that it relates to Home Depot's interest in the Home Depot Lands as opposed to the improvement on those Lands. As mentioned above, the present issue of priorities is a contest between Home Depot's interest in the Home Depot Lands, as a prospective purchaser under the Home Depot Agreement and as a tenant under the Ground Lease, and Romspen's interest in the Property under the Romspen Mortgage by way of subrogation. While there is no evidence that Home Depot derived any value from the refinancing of the earlier Romspen mortgages, there is equally no evidence that Romspen has derived any value from either the Home Depot Agreement or the Ground Lease between Woods and Home Depot.

102 In particular, there is no suggestion that the Ground Lease provided for a market rental. In the absence of any severance of the Home Depot Lands, the Ground Lease reverts to a 21-year term with a nominal annual rent. Further, if the Home Depot Agreement were enforceable against Romspen, the purchase price payable on closing of the sale of the Home Depot Lands would be significantly reduced by the prior rental payments made to Woods, of which it has not been established that Romspen had knowledge.

103 Fourth, as a related matter, while it may be implied in Home Depot's submission that most, if not all, of the value of the Property is attributable in the present economic circumstances to the Home Depot Lands, I do not think that this is determinative of the equitable considerations. The fact that the remainder of the Property, apart from the Home Depot Lands, if sold separately may have a value significantly less than that at the time of the Romspen mortgage loans to Woods ignores the reality that at all relevant times both Home Depot and Romspen were dealing with a single property. It also ignores the fact that Romspen did address this risk to the extent it could do so by means of the loan-to-value covenant in the Romspen Mortgage.

104 Fifth, I do not accept the Home Depot argument that the issue of fairness does not come into play in the present circumstances because Romspen discharged the earlier mortgages with full knowledge of the Home Depot Agreement rather than as a result of a mistake or inadvertence. This argument may have been made on an erroneous assumption that the earlier Romspen mortgages were discharged prior to the execution and delivery of the Romspen Mortgages. If it is not, this argument is objectionable for two reasons. It casts the fairness consideration in the context of subrogation far too narrowly. It also flies in the face of common sense and well established practice, which reflects the practical reality that there should be no reason to maintain on title mortgages that have been refinanced by a later mortgage from the same lender.

105 Sixth, the present circumstances are not analogous to those in *Armatage Motors Ltd. v. Royal Trust Corp. of Canada* (1997), 34 O.R. (3d) 599 (Ont. C.A.) in which injury to the party against whom subrogation was sought was a relevant consideration. *Armatage Motors* is a curious case in which the Court of Appeal appears to have denied subrogation on the basis that the first mortgagee had other assets against which it could recover the monies owed to it that were not also secured in favour of the second mortgagee, as well as the second mortgagee's reliance on the abstract of title. In the present proceedings, there is no evidence before the Court that Romspen will recover the outstanding loan amount from the remainder of the security under the Romspen Mortgage should subrogation not be granted. Insofar as there is any issue of reliance on the title to the Property, the present facts also favour Romspen.

106 Lastly, I do not accept Home Depot's submission that the doctrine of subrogation has no application in the context of a vesting order motion brought by a court-appointed receiver. Home Depot has offered no reason in principle why subrogation should not operate. I do not see any reason for excluding the operation of subrogation as an equitable consideration in determining whether to vest out a subsequent encumbrancer's interest.

107 On the basis of the foregoing, I conclude that Romspen is entitled to assert a subrogated claim against the Property in priority to that of Home Depot based on the principles of unjust enrichment. If it were necessary to consider the application of the principles in *Snell's Equity* upon which Home Depot relies, I would reach the same conclusion for the following reasons.

108 Turning to the test set out in *Snell's Equity*, satisfaction of the first requirement has already been addressed above. Absent subrogation, Home Depot will be enriched at Romspen's expense.

109 Similarly, for the reasons set out above pertaining to the absence of a juristic reason for such enrichment, I also conclude that such enrichment is unjust.

110 Lastly, I think that the third prong of the test in *Snell*, if in fact it is separate from the issue of a juristic reason for such enrichment, is also satisfied for the following reason. Provided that the issue of the Home Depot store is excluded from this analysis and dealt with below, as I believe is appropriate, there is no remaining policy reason for denying Romspen the remedy of subrogation. Romspen retained control over the discharge of all or any part of the Property from its security. Romspen did not benefit in any respect from the execution or performance of the Home Depot Agreement or the Ground Lease. The loss suffered by Home Depot — being the loss of the rental payments under the Ground Lease totaling $3,210,000 — was directly attributable to Home Depot's own actions in assuming a foreseeable risk.

Conclusion

111 Based on the foregoing, I conclude that Romspen's subrogated interest in the Property in respect of amounts outstanding under the earlier Romspen mortgages at the time of the execution of the Home Depot Agreement ranks prior to Home Depot's interest in the Home Depot Lands under the Home Depot Agreement and the Ground Lease.

Romspen's Assertion of Priority Based on the Romspen Mortgage

112 Romspen's alternative claim is that the Romspen Mortgage has priority over both the Home Depot Agreement and the Ground Lease by virtue of the absence of registration of these documents.

Preliminary Comments

113 Before addressing this submission, I wish to make two observations.

114 First, given the determination above in respect of Romspen's subrogation claim, it is likely that, as a practical matter, it is unnecessary to address this issue. It would appear that the amount of Romspen's subrogated claim is, by itself, substantially in excess of the current value of the Property. I have addressed this issue, however, in case this assumption proves to be incorrect in marketing the Property.

115 Second, the focus of this claim differs in one important respect from that of Romspen's subrogated claim. The subrogated claim is based on the priority of the earlier Romspen mortgages by virtue of their registration at the time of execution of the Home Depot Agreement and the absence of any subsequent consent or other agreement in favour of Home Depot affecting such priority. The claim in respect of the Romspen Mortgage is based principally on the ouster of the doctrine of actual notice in respect of the Home Depot Agreement and the Ground Lease by operation of the registration provisions under the *Land Titles Act* relating to charges.

Positions of the Parties

116 Romspen argues that the Romspen Mortgage, as a registered charge against title to the Property, ranks prior to the Home Depot Agreement and the Ground Lease by virtue of section 93(3) of the *Land Titles Act* notwithstanding actual notice of the Home Depot Agreement at the time of registration of the Romspen Mortgage. Section 93(3) reads as follows:

> The charge, when registered, confers upon the chargee a charge upon the interest of the chargor as appearing in the register subject to the encumbrances and qualifications to which the chargor's interest is subject, but *free from any unregistered interest in the land.* [Emphasis added]

117 Home Depot argues that section 93(3) of the *Land Titles Act* does not displace the operation of the doctrine of actual notice in Ontario and that, by virtue of Romspen's actual knowledge of the Home Depot Agreement at the time of execution of the Romspen Mortgage, the Romspen Mortgage is subordinated to this instrument.

118 Home Depot submits that it is entitled to rely on the doctrine of actual notice by virtue of the principle articulated by the Supreme Court in *Dominion Stores Ltd. v. United Trust Co.*, [1977] 2 S.C.R. 915 (S.C.C.). It argues that wording comparable to that in the Alberta legislation referred to by Spence J. in *United Trust* is required in order to exclude the operation of actual notice in Ontario. It says that the wording of section 93(3) is insufficient for this purpose.

119 In making this submission, Home Depot also relies on the more recent decisions of Mesbur J. in *1420111 Ontario Ltd. v. Paramount Pictures (Canada) Inc.*, [2001] O.J. No. 4461 (Ont. S.C.J.), as well as the Court of Appeal in *Manias v. Norwich Financial Inc.*, [2008] O.J. No. 2612 (Ont. C.A.) and *Romspen Investment Corp. v. 2126921 Ontario Inc.*, [2010] O.J. No. 5405 (Ont. C.A.).

Analysis and Conclusions

120 I propose to consider the following two issues in respect of the issue of the priority of the Romspen Mortgage relative to the Home Depot Agreement and the Ground Lease:

> (1) does section 93(3) of the *Land Titles Act* oust the operation of the doctrine of actual notice in the present circumstances? and
>
> (2) if not, is the Romspen Mortgage subordinated to the Home Depot Agreement and the Ground Lease by operation of the doctrine of actual notice?

Does Section 93(3) Oust the Doctrine of Actual Notice?

121 There is no dispute that Romspen had actual notice of the Home Depot Agreement at the time of execution and registration of the Romspen Mortgage. Accordingly, the issue in this section is whether the doctrine of actual notice could operate to subordinate the Romspen Mortgage to the interest of Home Depot under the Home Depot Agreement in accordance with the principle in *United Trust, supra.* The issue does not arise in respect of the Ground Lease given the determination above that Romspen did not have actual notice of the Ground Lease at the time of execution of the Romspen Mortgage.

122 The operation of section 93(3) of the *Land Titles Act* was previously addressed in the Holborn Judgment in the context of a contest between a registered mortgage and another unregistered agreement of purchase and sale. For the reasons set out therein, I concluded that section 93(3) operates to oust the doctrine of actual notice in Ontario in respect of a registered charge notwithstanding the chargee's actual notice of an unregistered agreement of purchase and sale.

123 Subsection 93(3) specifically addresses the operation of actual notice in the phrase "free from any unregistered interest in the land". In my view, this wording is sufficiently explicit to satisfy the test in *United Trust.* There is nothing in that decision that requires language substantially similar to the wording in the Alberta legislation to exclude the operation of the doctrine of actual notice. I am not persuaded that the conclusion reached in the Holborn Judgment was in error.

124 I do not think it is necessary to restate the reasons for my conclusion on this issue in this Endorsement. For present purposes, I adopt the reasons in the Holborn Judgment on the operation of section 93(3), with the exception of the alternative reasons of effective subordination, given the absence of any covenant against registration in the present proceedings. Subject to the qualification that section 93(3) has been read subject to section 155, which deals with the invalidity of the registration of fraudulent instruments and is not at issue in this proceeding, I conclude that section 93(3) provides a mortgagee with an absolute defence to a claim based on actual notice.

125 I wish, however, to set out several additional observations regarding this issue in response to Home Depot's submissions.

126 First, in reaching this conclusion, I have also considered the absence of any alternative interpretation of the language of section 93(3). Home Depot's position is that section 93(3) does not operate where a receiver seeks to vest out an equitable interest. It seeks to avoid the priority issue by identifying a different fact situation. It did not, however, provide a meaningful alternative interpretation of section 93(3) that demonstrates a purpose for that provision that does not address the doctrine of actual notice. In the absence of an alternative interpretation of section 93(3), the Court must conclude that the provisions of section 93(3) are directed to the present situation.

127 In addition, I have the following observations regarding the extent to which the additional decisions cited by Home Depot on this motion can be taken as authority for the proposition that the wording of section 93(3) does not exclude the operation of the doctrine of actual notice.

128 First, section 93(3) was not cited in the decisions of either the Court of Appeal in *Manias*, *supra* or Mesbur J. in *Paramount Pictures*, *supra*. Second, *Manias* addresses an altogether different situation of a contest of priorities among registered charges, where a mistake was made in the order of registration. That issue did not invoke section 93(3). Third, *Paramount Pictures* addresses a contest between a mortgagee and a tenant in which the tenant wished to resile from its lease, rather than a situation in which a mortgagee sought to vest out a tenant's interest. This dispute therefore also does not involve section 93(3).

129 Fourth, in *Romspen Investment Corp. v. 2126921 Ontario Inc.*, [2010] O.J. No. 639 (Ont. S.C.J.), Tucker J. held that section 93(3) did not apply where a party sought to rely on that provision to take advantage of a registration error in respect of a prior mortgage in order to obtain a better position than had been bargained for. Subsequent to the hearing in the present proceeding, the Court of Appeal upheld this decision in *Romspen Investment Corp. v. 2126921 Ontario Inc.* (Ont. C.A.) [*Romspen Investment Corp. v. Orvitz*] by way of an appeal book endorsement.

130 The relevant portion of the appeal book endorsement on the substantive issue reads as follows:

> We are satisfied that the application judge's finding that the appellants had actual notice of the intended priority of the Romspen mortgage necessarily included a finding that the Romspen mortgage was an equitable mortgage in respect of the parking lot. That being so, contrary to the analysis in *Holborne* [*sic*] *Property v. Romspen* (2008), 77 R.P.R. (4th) 262, the application judge was correct in holding that section 93(3) of the *Land Titles Act* did not preclude Romspen's equitable mortgage from having priority over the appellants' registered mortgage. (See *United Trust v. Dominion Stores et al.*, [1977] 2 S.C.R. 915 at pp. 956 and 957). To that extent, the appeal must fail.

131 I do not think the decision in *Romspen Investment Corp. v. Orvitz* applies to the present circumstances for the following reasons.

132 First, I do not think that the Court of Appeal intended to state, as a general principle, that the doctrine of actual notice continued to operate in all circumstances in Ontario notwithstanding the enactment of section 93(3). The issue of the ambit of section 93(3) was not addressed by Tucker J. The Court of Appeal was also silent on the issue.

133 Second, as Tucker J. expressly noted at para. 25 of her judgment, the facts in this decision are profoundly different from those in the Holborn Judgment. She noted "[t]his is not a case where priorities are in issue; the second mortgagee always knew it was to be a second". I see nothing in the decisions of Tucker J. or of the Court of Appeal that addresses, let alone excludes, the operation of section 93(3) in substantive priority contests.

134 Third, as a related matter, it is not necessary to exclude the operation of section 93(3) in order to reach the result ordered in *Orvitz*. It appears that the solicitor's error in *Orvitz* was a failure to include a legal description — that was included in the second mortgage — of a second parcel of land intended to be charged. As Tucker J. recognized in her judgment, *Orvitz* is essentially an unjust enrichment case based on an implied contractual subordination agreement among the parties, rather than a case of actual notice. It would be unconscionable to allow the second mortgage to retain its priority even if, in the first instance, section 93(3) operated. Moreover, the implication from *Manias* is that section 93(3) does not operate in a priority dispute between charges. Essentially, that is the situation in *Orvitz*— a contest between two mortgagees where one mortgagee seeks rectification of his instrument to reflect the intended security as between the mortgagor and mortgagee in circumstances in which rectification would be ordered notwithstanding its impact on the second mortgagee because of the intended priorities as between the two mortgages.

135 In summary, while I accept that the wording of the endorsement of the Court of Appeal may be read in different ways, I think the intention is clear and the circumstance are entirely different from those in the present case or in the Holborn Judgment.

136 Based on the foregoing, I conclude that, while Romspen had actual knowledge of the Home Depot Agreement, the Romspen Mortgage ranks prior to the Home Depot Agreement based on the operation of section 93(3) of the *Land Titles Act*.

The Operation of the Doctrine of Actual Notice

137 In the event that the doctrine of actual notice is held to operate in the present circumstances, however, I also do not think that it would be applied to subordinate the Romspen Mortgage to either the Ground Lease or the Home Depot Agreement.

138 The Court has previously concluded that Romspen did not have actual knowledge of the Ground Lease at the time that it executed the Romspen Mortgage. This excludes the operation of the doctrine of actual notice in respect of the Ground Lease.

139 With respect to the Home Depot Agreement, the doctrine of actual notice is an equitable doctrine. Its application is not automatic. If it were held that the doctrine of actual knowledge operated with respect to the Home Depot Agreement, the Court must still consider the equities between the parties.

140 In this case, in my opinion, the considerations discussed above in the context of Romspen's claim for priority by way of subrogation are equally applicable to the issue of the operation of the doctrine of actual knowledge. On this basis, I would conclude that the equities between the parties did not favour the application of the doctrine of actual notice to subordinate the Romspen Mortgage to the Home Depot Agreement.

Conclusion Regarding Priority of Romspen's Interest in the Property

141 Based on the foregoing, I conclude that Romspen's interest in the Property under the Romspen Mortgage ranks prior to Home Depot's interests in the Home Depot Lands under the Home Depot Agreement and the Ground Lease.

Is Romspen's Interest in the Property Subordinated to Home Depot's Interest By Virtue of a Consent?

142 As a matter of law, if a lease is executed by a mortgagor after the mortgage has been granted, the mortgagee will be bound by the terms of the lease if it is made with his express or implied consent: see *Goodyear Canada Inc. v.*

Burnhamthorpe Square Inc. (1998), 41 O.R. (3d) 321 (Ont. C.A.) at paras. 54-57. The same principle can operate in respect of an agreement to purchase land.

143 Romspen's claim for subrogation is based on the prior registration of the earlier Romspen mortgages at the time of execution of the Home Depot Agreement. This claim could, however, be defeated by evidence that it consented to the Home Depot Agreement or the Ground Lease at some point thereafter.

144 Similarly, Romspen's claim of priority in respect of its interest under the Romspen Mortgage could also be defeated by evidence of such consent at some point after execution and registration of the Romspen Mortgage notwithstanding an initial priority position for the reasons set forth above.

145 The issue in this section is purely factual — did Romspen consent to the Home Depot Agreement or the Ground Lease? This matter has been addressed above, where I concluded that Home Depot has failed to establish as an undisputed fact that Romspen consented to either the Home Depot Agreement or the Ground Lease such that the Romspen Mortgage is subordinated to either or both of these instruments.

146 I would add only the observation that the issue of actual notice arises in circumstances such as the present precisely because knowledge does not automatically constitute consent. Accordingly, the significance, if any, of Romspen's knowledge of the existence of the Home Depot Agreement at the time of the Romspen Mortgage is properly addressed, not as a matter of consent, but as a matter of actual notice.

Is Home Depot Entitled to a Lien Against the Property Ranking in Priority to Romspen's Interest by Virtue of the Construction of the Home Depot Store?

147 Based on the foregoing, Romspen has an interest in the Property that ranks prior to Home Depot's interest under the Home Depot Agreement and the Ground Lease on two grounds: (1) by way of subrogation to the extent of the monies refinanced under the Romspen Mortgage plus interest; and (2) by operation of section 93(3) of the *Land Titles Act* to the extent of all monies secured under the Romspen Mortgage.

148 In these circumstances, Home Depot claims a lien against the Property under section 37(1) of the CLPA or, alternatively, in equity, in either case in the amount by which the value of the Property has been increased by the construction of the Home Depot store. It should be noted that the claim for lien is asserted against the owner of the Property. To the extent a lien claimant is successful, there is a further issue regarding the priority of any such lien relative to Romspen's interest in the Property. I will first address the validity of Home Depot's lien claims before considering the issue of priority.

The Conveyancing and Law of Property Act

149 Section 37(1) of the CLPA provides as follows:

> Where a person makes lasting improvements on land under the belief that it is the person's own, the person or the person's assigns are entitled to a lien upon it to the extent of the amount by which its value is enhanced by the improvements, or are entitled or may be required to retain the land if the Superior Court of Justice is of opinion or requires that this should be done, according as may under all circumstances of the case be most just, making compensation for the land, if retained, as the court directs.

Home Depot seeks a lien under this provision in the amount of the value by which the Property has been improved as a result of the construction of the Home Depot store on the Home Depot Lands.

150 As set out in *McGuire v. Warren* (2006), 46 R.P.R. (4th) 113 (Ont. S.C.J.) at para. 7 per Wood J., before granting relief under section 37(1) of the CLPA, the Court must apply a three-part test:

> ... First, it must be satisfied that the person making the improvements genuinely believed that he or she owned the land. Secondly, it must be satisfied that the improvements made are of a "lasting" nature. Finally, if the first two parts are met, the court must weigh the equities between the owner of the encroached upon lands and the person who has made the improvements, to determine whether it is appropriate to either grant a lien on the lands for the value of the improvements or to transfer the lands to the person who made the improvements for appropriate compensation.

151 There is no question that Home Depot has made improvements of a lasting value to the Property. The issue is whether Home Depot has satisfied the requirement that it have a sufficient ownership interest in the Property.

152 The Receiver and Romspen make three submissions with respect to the first part of the test.

153 Firstly, they refer to para. 12 of *McGuire*, in which Wood J. observed that section 37(1) was enacted at a time when serious inadequacies or deficiencies in conveyancing practice resulted in disputed property boundaries. They argue the present case does not result from such factors, suggesting that the provision is therefore unavailable. However, I do not think that the purpose of section 37(1) is limited to addressing issues arising from historical conveyancing practice.

154 Second, Romspen argues that demonstration of a genuine belief that the claimant owns the relevant land requires demonstration of not only an honest belief but also a reasonable basis for that belief: *Derro v. Dube*, [1948] O.W.N. 287 (Ont. H.C.) at paras. 3-4 per McRuer C.J.H.C.; and *Halton Hills (Town) v. Row Estate*, [1993] O.J. No. 1222 (Ont. Gen. Div.) per MacKenzie J. It argues that Home Depot did not have such a belief at the time it erected its store on the Property.

155 I do not think it can reasonably be suggested that, as between Home Depot and Woods, Home Depot did not believe that it had an interest in the Property that was sufficient for the purposes of claiming relief under section 37(1). It had spent $14.5 million in improvements on the Property. The only reasonable inference is that it did so in the belief that, at a minimum, it had a right to remain on the Property for the remainder of the term of the Ground Lease.

156 Third, Romspen argues that, irrespective of that belief, Home Depot does not have a sufficient ownership interest in the Home Depot Lands to obtain relief under section 37(1). It argues that a purchaser under an unexecuted agreement of purchase and sale, while an equitable owner of the property, does not have a sufficient ownership interest to obtain relief under section 37(1). It relies on *Geldhof v. Bakai* (1982), 139 D.L.R. (3d) 527 (Ont. H.C.) at para. 8 per Callaghan J. Insofar as it is suggested that this is a general principle of law, I think it is incorrect notwithstanding that this was the result in *Geldhof v. Bakai*. It is clear that Callaghan J. based his decision on a finding of fact in the particular circumstances of that case, including specific advice that neither plaintiff believed that they would own the land in question until the date of the closing of the agreement of purchase and sale entered into with the defendants.

157 However, on the facts of the present case, I conclude that Home Depot does not have a sufficient ownership interest under the Home Depot Agreement or the Ground Lease to seek relief under section 37(1) for the following reasons.

158 As mentioned, at best, Home Depot has an unregistered equitable agreement to purchase the Home Depot Lands. Moreover, that is subject to an important qualification. Section 4.5 of the Home Depot Agreement provides that the Agreement shall only be effective to create an interest in land if the provisions of the *Planning Act* have been complied with. That cannot occur until severance of the Home Depot Lands has occurred. Given the combination of these two factors, I think the Court must conclude that Home Depot does not have a sufficient interest in land under the Home Depot Agreement to assert a claim under section 37(1).

159 I have some sympathy for the argument that Home Depot's leasehold interest under the Ground Lease, which is effective currently, is a sufficient ownership interest in the Home Depot Lands to obtain relief under section 37. Section 3.3(a) of the Ground Lease contains a covenant for quiet possession from Woods. The Ground Lease has a fixed term of 50 years and rental payments fixed for the entire period. In short, Home Depot has security of tenure as between itself and Woods. Such a long-term lease is often a substitute for ownership of the freehold interest. However, the language

of section 37(1) appears to require a belief that the lien claimant is an owner of the relevant property. The Court has not been provided with any case law that supports the proposition that a leasehold interest in a property is a sufficient interest to obtain relief under section 37(1). Moreover, there is some authority to the contrary in *Metzger Estate v. Gardiner*, [2000] O.J. No. 2280 (Ont. S.C.J.).

160 On the basis of the foregoing, I therefore conclude that Home Depot is not entitled to a lien against the Property under section 37(1) of the CLPA.

Claim for Equitable Lien

161 As mentioned, in the alternative, Home Depot claims an equitable lien in the Property equal to the amount by which the value of the Property has been enhanced by the construction of the Home Depot store. It relies on a line of cases in which equitable relief has been granted to parties who make improvements to a property at a time when they mistakenly believe they will be able to acquire the property: see, for example, *Montreuil v. Ontario Asphalt Co.* (1922), 63 S.C.R. 401 (S.C.C.) at p. 429 per Anglin J.; *Isabelle v. Lahaie*, [2007] O.J. No. 4981 (Ont. S.C.J.); and *Hatoum v. Hatoum*, [1988] O.J. No. 1216 (Ont. H.C.) at p. 6-8 per Southey J., aff'd (Ont. C.A.).

162 I do not think that this principle is limited in operation to circumstances in which a claimant has an honest belief in his or her right to acquire the subject property. It is framed more broadly in *Chalmers v. Pardoe*, [1963] 3 All E.R. 552 (Fiji P.C.) as follows:

> There can be no doubt on the authorities that where an owner of land has invited or expressly encouraged another to expend money on part of his land on the faith of an assurance or promise that that part of the land will be made over to the person so expending his money a court of equity will prima facie require the owner by appropriate conveyance to fulfil his obligation; and when, for example for reasons of title, no such conveyance can effectively be made, a court of equity may declare that the person who has expended the money is entitled to an equitable charge or lien for the amount so expended.

163 On this issue, the equities clearly favour Home Depot over Woods. There is no apparent equitable consideration in favour of Woods. Home Depot had a right to purchase the Home Depot Lands as well as a leasehold interest under the Ground Lease having a term of at least 21 years. It appears that, at the time that it constructed the Home Depot store, there was no indication of the onset of Woods' financial difficulties, which later prevented completion of the sale transaction. In addition, the Home Depot store was constructed in accordance with arrangements that were specifically agreed to by Woods. Further, Woods did not appear on this motion and does not oppose a lien in favour of Home Depot. The Receiver effectively does not oppose this relief either as it is more concerned with the issue of the priority of such lien relative to the Romspen mortgages.

164 Based on the breadth of this principle, as well as the equitable considerations set out above, I think Home Depot would satisfy the test for an equitable lien based on its honest belief that, pursuant to the Ground Lease, it had a valid leasehold interest in the Property having a term of at least 21 years.

165 Accordingly, to the extent that Home Depot is not entitled to a lien against the Property under section 37(1) of the CLPA, I am of the opinion that it has satisfied the requirements of an equitable lien in the Property against the interest of Woods in the amount by which the value of the Property has been enhanced by the construction of the Home Depot store.

The Priority Issue

166 The real issue in this proceeding is not, however, whether Home Depot is entitled to a lien against the Property but whether such lien should rank in priority to Romspen's interest under the Romspen Mortgage. This issue appears to be a matter of first impression.

167 The Receiver and Romspen argue that equity cannot permit the priority of Romspen's interest in the Property to be reversed by equitable lien rights on the principle that, where the equities are equal between competing claims in a property, legal title prevails: see *Toronto Dominion Bank v. Faulkner* (1990), 74 O.R. (2d) 92 (Ont. C.A.) at para. 18. However, this submission begs the question of whether the equities between Home Depot and Romspen are equal.

168 Home Depot points to a number of factors that it says should be taken into consideration by the Court. Home Depot's principal argument is that, in its view, Romspen allowed the construction of the Home Depot store on the Home Depot Lands and now seeks to take advantage of that improvement without compensation, which it characterizes as a windfall gain. It also argues that the Court should infer Romspen's consent to the construction of the Home Depot store from its execution of the Site Plan Agreement. Lastly, it says that if Romspen is successful, the Home Depot employees will lose their employment.

169 I have considerable sympathy for Home Depot's position notwithstanding the fact that they have contributed in a significant way to the present situation by deciding not to register the Home Depot Agreement or the Ground Lease. The reality is that, if the order is granted, Romspen will obtain the benefit of an improvement that it did not originally anticipate insofar as the parties did not expect, at the time the Home Depot store was constructed, that Woods would go into default on the Romspen Mortgage prior to completion of the sale of the Home Depot Lands.

170 However, I have concluded that Romspen's interest in the Property should have priority over Home Depot's equitable lien for the following reasons.

171 First, the mere fact that Romspen will obtain the value of the Home Depot store is not, by itself, sufficient to determine the issue of the priority of Home Depot's lien. To succeed in this claim, Home Depot must do more than demonstrate that it has improved the Property and that Romspen, as the mortgagee, will benefit if it is denied a prior equitable lien in respect of the improvement. It must establish either a consent of Romspen to the construction of the Home Depot store in circumstances indicating that the issue of priority was understood to be involved or another equitable consideration that justifies imposition of a prior lien in the absence of such consent.

172 In my opinion, Home Depot has failed to identify any other equitable consideration that justifies imposition of a prior lien in the absence of Romspen's consent to the construction of the store. Home Depot suggests that the Court should consider the possibility that its employees will lose their jobs. This is always an important consideration for courts in a receivership context. However, there is simply no basis in the evidence before me that would support such a conclusion. There are a number of possible outcomes to the present situation depending upon the business decisions of the parties after the release of this Endorsement.

173 Accordingly, the issue turns on whether Romspen consented to the construction of the Home Depot store on the Home Depot Lands in circumstances that it understood, or should reasonably have understood, that Home Depot would have a prior lien over such Lands to the extent of the value of the improvement. I conclude that Home Depot has failed to demonstrate any such consent of Romspen for the following reasons.

174 First, there is no evidence that Romspen ever consented directly to the construction of the Home Depot store. There is no evidence that Home Depot ever approached Romspen for such a consent. Nor is there any evidence of any communication between the parties that Romspen should reasonably have considered constituted a request for such a consent or required a response to protect its security position. Accordingly, there is no evidence that supports Home Depot's suggestion that Romspen "allowed" the construction of the Home Depot store in some manner.

175 Second, it is not suggested that the existence of the Home Depot Agreement implied a consent to the construction of the Home Depot store. Insofar as Home Depot suggests that the execution of the Ground Lease implies such a consent, I reject the submission for two reasons. Home Depot was not a party to the Ground Lease and gave no assurances in respect of Woods' representations therein. In addition, I have concluded that Home Depot did not have actual knowledge

of, and did not consent to, the Ground Lease. There is also no basis for implying consent to the construction of the Home Depot store from Romspen's execution of the Romspen Mortgage.

176 The issue therefore turns principally on whether Romspen's execution of the Site Plan Agreement somehow changes this result — that is, whether it constitutes consent to the construction of the Home Depot store or evidence of Romspen's consent given elsewhere to such construction. I do not think it does for four reasons.

177 First, there is nothing in the Site Plan Agreement that constitutes the express or implicit consent of Romspen to the construction of the Home Depot store. There is also nothing in the Site Plan Agreement that expressly contemplated that Home Depot would require or seek Romspen's consent to the construction of the Home Depot store. Romspen was entitled to assume from the absence of any contractual relationship between it and Woods, as well as the limited scope of the Site Plan Agreement, that Home Depot would approach it separately if it required a consent or other protection from Romspen in respect of the construction of the store on the Property.

178 Moreover, the Site Plan Agreement specifically referred to the earlier Romspen mortgages, which were registered against the Property and which maintained Romspen's control over the Property by the mechanism of Romspen's control over partial discharges of its security. The express subordination set out in the Site Plan Agreement related only to the rights of the Town of Collingwood. While rights of subordination of an interest in the Property are not the same as consent to the construction of the Home Depot store, the absence of any provision in the Site Plan Agreement dealing with Home Depot's rights in respect of the Property in the event of construction of the store is significant. If the Site Plan Agreement had been intended to grant Home Depot rights in respect of Romspen, it had to do so explicitly.

179 Second, more generally, there is no sense in which it can be said that Home Depot "allowed" the construction of the Home Depot store by executing the Site Plan Agreement. As mentioned, the only purpose of its execution of the Site Plan Agreement was to subordinate its interest in the Property to the interest of the Town of Collingwood. The Site Plan Agreement did not set out a timetable for the construction of the Home Depot store. Romspen could not know of Home Depot's intentions in this regard unless Home Depot chose to advise it. There is no evidence that Home Depot ever communicated its intention to construct the Home Depot store to Romspen.

180 Third, the circumstances in July 2006 were not such that Romspen's execution of the Site Plan Agreement can be taken as necessarily implying that Romspen turned its mind to the issue of the priority of any lien in favour of Home Depot in the Property that might arise after construction of the store and, by implication, agreed to subordinate Romspen' interest to any such lien. As mentioned above, the Romspen Mortgage was in good standing in July 2006. There was no reason to expect that Woods would be unable to obtain a partial discharge of the Home Depot Lands, in which case the priority issue would not arise.

181 Fourth, Home Depot has failed to identify any circumstances at the time of execution of the Site Plan Agreement that would have imposed an obligation on Romspen to take positive action to protect its position even if it suspected from the request to sign the Site Plan Agreement that Home Depot intended to construct the Home Depot store on the Home Depot Lands.

182 At all times, Home Depot's contractual relationships were restricted to Woods. The only exception was the Romspen acknowledgement, which addressed only the demolition of a portion of the industrial building on the Property. Home Depot was not required to notify Romspen of the commencement of construction of the Home Depot store or to seek its consent to such construction. Conversely, Romspen was not obligated to inquire as to Home Depot's intentions and to advise Home Depot that it did not consent to the construction of the Home Depot store insofar as it would give rise to a lien in priority to the Romspen Mortgage.

183 Ultimately, Home Depot's position is that Romspen ought to have known from the fact of the demolition of the portion of the industrial building and from the Site Control Agreement that it was proposing to build the Home Depot store on the Home Depot Lands and that Romspen had an obligation to advise Home Depot that it did not consent to

such construction. There is no evidence that Romspen actually knew of Home Depot's intentions prior to commencement of construction beyond knowing that it was possible that Home Depot might construct a store on the Property. I do not think that Romspen could reasonably have known of Home Depot's intention to commence construction immediately from the demolition and the Site Control Agreement alone. It certainly could not have known that Home Depot intended to commence construction without obtaining any consent or assurance from Romspen to protect its position in the event of realization proceedings by Romspen. In any event, however, neither actual nor constructive knowledge imposed any obligation on Romspen to approach Home Depot to protect its security position in the circumstances of unilateral action by Home Depot. There was no contractual relationship between the parties. There was no prior representation from Romspen to Home Depot. I know of no legal principle that would impose such an obligation in the circumstances of this case in the absence of any express communication from Home Depot to Romspen that could ground a claim based on reliance.

184 Accordingly, I conclude that the Romspen Mortgage has priority over any equitable lien in favour of Home Depot arising as a result of the construction of the Home Depot store on the Property.

185 In addition to the equitable considerations addressed above, I would add, if it were necessary to address this issue, that I see no basis for excluding the operation of section 93(3) of the *Land Titles Act* in respect of an equitable lien. There is nothing in the language of section 93(3) that provides that the principles of equity are intended to override the operation of this provision of the *Land Titles Act*. Indeed, an unregistered inequitable lien would appear to be the very type of interest to which section 93(3) is directed.

Conclusion Regarding the Equities Between the Parties Relative to the Receiver's Request for an Order Vesting Out the Interest of Home Depot in the Property

186 The foregoing issues, while they involve a consideration of the equities between the parties in relation to specific issues, are not determinative of the question of whether the Receiver should be granted an order approving the sale of the Property on a basis that vests out the interest of Home Depot. That requires a consideration of the equities between the parties based on the determinations made above and any other applicable considerations.

187 Based on the foregoing, the Court must consider the equities between the parties in the context of findings that

> (1) Romspen's interest in the Property ranks ahead of that of Home Depot to the extent of the monies secured under the Romspen Mortgage or, alternatively, to the extent of the monies secured under the earlier Romspen mortgages in existence at the date of the Home Depot Agreement, plus interest at the rates provided for under those mortgages;
>
> (2) Home Depot's equitable lien against the Property arising as a result of the construction of the Home Depot store does not rank prior to the interest of Romspen in the Property; and
>
> (3) Home Depot is unable to establish as an undisputed fact that Romspen consented to the Home Depot Agreement, the Ground Lease or the construction of the Home Depot store in a manner that was intended to affect its rights in the Property.

188 I conclude that the Receiver should be granted an order permitting the sale of the Property free of the interest of Home Depot for the following reasons.

189 The equitable considerations addressed in the context of the determinations of the priorities of the respective interests of Romspen and of Home Depot in the Property are also applicable for the present assessment. In particular, Romspen bargained with Woods for the right to control the discharge of any portion of the Property from its security. Registration of the earlier Romspen mortgages, and of the Romspen Mortgage, was notice to Home Depot of the existence of such right. In addition, Romspen did not in any way provide assurance or comfort to Home Depot with respect to the priority of its interest in the Property or the protection of its interest in the event of realization proceedings.

190 The only other consideration to be addressed by the Court is, therefore, the value of the Property. As suggested in *1565397 Ontario Inc., Re* (Ont. S.C.J.), while a court can sell property free of a contract entered into between a debtor and a third party, the Court cannot do so in circumstances where the effect is to extinguish an interest in property except in limited circumstances. Those circumstances appear to be limited to those in which the third party has no equity in the subject property given the value of the property and prior encumbrances.

191 While the circumstances in the present proceedings are more complex than other decisions in which this principle has been applied, I think that the facts before the Court establish that there is no equity in Home Depot's interest in the Property.

192 The Sale Agreement contemplates a sale price of $14.1 million. This is substantially below the amount secured under the Romspen Mortgage, which is at least $17,844,975.38 plus interest since February 1, 2010. On this basis, there is no equity value in Home Depot's subordinate interests in the Property. Given the existing priorities, Home Depot's interest would only have value if the Receiver received an offer for the Property that fully satisfied the monies owing to Romspen.

193 Based on the foregoing analysis of the applicable equitable considerations as between Romspen and Home Depot, I conclude that the equities favour Romspen and, accordingly, that the Receiver is entitled to an order permitting the sale of the Property on a basis that vests out the Home Depot interests in the Property under the Home Depot Agreement and the Ground Lease.

Should the Court Approve the Sale Agreement?

194 The remaining issue is whether the Court should also approve the Sale Agreement at this time.

195 As mentioned, the Receiver's report sets out in detail the exposure of the Property to the market. In the usual circumstance, the nature and extent of such activities would be sufficient to satisfy the Court that the proposed sale price for the Property represented the fair market value of the Property.

196 There are, however, two unusual features of the present circumstances.

197 First, the Receiver's effort to market the Property took place principally in the first six months of 2009. While there are legitimate reasons for the delay in bringing on this motion, the stock market and residential real estate market have nevertheless improved significantly since then. There is, therefore, a possibility that the real estate market in Collingwood has improved in a like manner since then. The Court must be concerned that the sale price under the Sale Agreement may not represent the current fair market value of the Property.

198 Second, and more importantly, the Receiver marketed the Property on the basis that a purchaser was bound to sell the Home Depot Lands to Home Depot in accordance with the Home Depot Agreement. It is possible that the Property would be attractive to other potential purchasers as a result of the determination in this Endorsement that the Receiver has the authority to sell the Property free of any claim by Home Depot. This consideration is relevant to the question as to whether the sale price under the Sale Agreement represents the current fair market value of the Property.

199 Further, the Receiver itself suggests that Home Depot is financially able to acquire the Romspen Mortgage and develop the Property itself if this motion is decided against it and it wishes to avoid the loss of its investment in the Home Depot store. I do not suggest that any such action is probable. However, it does raise the possibility that, as a result of the determination in this proceeding, Home Depot may itself wish to participate in the sales process in some manner.

200 Given these circumstances, the Court is of the view that it cannot consider approval of the Sale Agreement until the Receiver has conducted a further sales process in respect of the Property on the basis that a purchaser would be entitled to acquire the Property free and clear of any lien or claim of Home Depot. Rather than address the nature of

and length of any such sales process, the Court is of the view that it should leave such details to the Receiver subject, of course, to the Receiver's right to seek the advice and directions of the Court at any time.

Further Order

201 At the request of the Receiver, an appraisal of the Property obtained by the Receiver from High Point Danbury Realty Advisors Corporation is hereby sealed pending completion of the sale of the Property or further order of this Court.

Costs

202 If the parties are unable to agree on costs of this motion, they shall have thirty days to make written submissions to the Court through the Commercial List Office, not to exceed seven pages in length.

Motion granted in part; cross-motion dismissed.

Most Negative Treatment: Recently added (treatment not yet designated)
Most Recent Recently added (treatment not yet designated): Third Eye Capital Corporation v. Ressources Dianor Inc./Dianor Resources Inc. | 2018 ONCA 253, 2018 CarswellOnt 3694 | (Ont. C.A., Mar 15, 2018)

2011 ONCA 817
Ontario Court of Appeal

Romspen Investment Corp. v. Woods Property Development Inc.

2011 CarswellOnt 14462, 2011 ONCA 817, 14 R.P.R. (5th) 1, 210 A.C.W.S. (3d) 302, 286 O.A.C. 189, 346 D.L.R. (4th) 273, 85 C.B.R. (5th) 21

Romspen Investment Corporation (Applicant / Respondent) and Woods Property Development Inc. and TDCI Holdings Inc. (Respondents)

John Laskin, M. Rosenberg, Paul Rouleau JJ.A.

Heard: November 18, 2011
Judgment: December 22, 2011
Docket: CA C53496, C54375

Proceedings: reversing *Romspen Investment Corp. v. Woods Property Development Inc.* (2011), 2011 CarswellOnt 2380, 75 C.B.R. (5th) 109, 2011 ONSC 3648, 4 R.P.R. (5th) 53 (Ont. S.C.J.); and reversing *Romspen Investment Corp. v. Woods Property Development Inc.* (2011), 2011 CarswellOnt 10053, 2011 ONSC 5704 (Ont. S.C.J. [Commercial List])

Counsel: Ronald Slaght, Q.C., John J. Chapman for Appellant, Home Depot Canada Inc.
David P. Preger, Lisa Corne for Respondent
Harvin D. Pitch for Respondent, SF Partners Inc.

Subject: Property; Corporate and Commercial; Insolvency; Estates and Trusts; Evidence; Civil Practice and Procedure

Related Abridgment Classifications

Bankruptcy and insolvency
XIV Administration of estate
XIV.6 Sale of assets
XIV.6.a Sales of asset subject to charge, mortgage, or hypothec

Civil practice and procedure
XX Trials
XX.4 Conduct of trial
XX.4.i Powers and duties of trial judge
XX.4.i.iii Miscellaneous

Debtors and creditors
VII Receivers
VII.6 Conduct and liability of receiver
VII.6.a General conduct of receiver

Evidence
II Proof

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Real property
II Registration of real property
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Real property
VII Mortgages
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Real property
VII Mortgages
VII.14 Priorities
VII.14.b Between types of creditors
VII.14.b.xiv Miscellaneous

Real property
VII Mortgages
VII.15 Right of subrogation

Headnote

Real property --- Mortgages — Priorities — Between types of creditors — Miscellaneous
Mortgages were registered against property owned by debtor W Inc. in favour of secured creditor R Corp. — H Inc. and debtor entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of property (H Lands) — H Inc. built store on H Lands — Debtor defaulted on mortgage, and receiver was appointed — Receiver partly succeeded in its motion seeking approval of sale of property to purchaser free of any claims by H Inc. — H Inc. unsuccessfully brought cross-motion for various relief regarding property — Motion judge held that secured creditor's interest in property ranked higher in priority to H Inc.'s interest — Motion judge held that H Inc. failed to establish as undisputed fact that secured creditor consented to H Agreement or ground lease such that its mortgage was subordinated to instruments — H Inc. appealed — Receiver and secured creditor cross-appealed — Appeal allowed; cross-appeal dismissed — Matter was remitted for new hearing — Motion judge's application of incorrect standard of proof and his belief that he was not allowed to draw inferences on motion were errors that went to very basis of factual matrix — Errors committed by motion judge were not harmless, as result may have been different — Motion judge excluded possibility of finding implied consent by secured creditor because of his belief that he was prevented from drawing inferences from facts — Motion judge did not look at totality of considerations in weighing equities between parties.

Real property --- Mortgages — Priorities — Between types of creditors — Registered mortgagee and equitable interest holder
Mortgages were registered against property owned by debtor W Inc. in favour of secured creditor R Corp. — H Inc. and debtor entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of property (H Lands) — H Inc. built store on H Lands — Debtor defaulted on mortgage, and receiver was appointed — Receiver partly succeeded in its motion seeking approval of sale of property to purchaser free of any claims by H Inc. — H Inc. unsuccessfully brought cross-motion for various relief regarding property — Motion judge held that mortgage had priority over any equitable lien in favour of H Inc. arising from construction of its store — Motion judge held that H Inc. failed to identify any equitable consideration, other than secured creditor obtaining value of store, that justified imposition of prior lien in absence of secured creditor's consent to construction of store — H Inc. appealed — Receiver and secured creditor cross-appealed — Appeal allowed; cross-appeal dismissed — Matter was remitted for new hearing — Motion judge applied incorrect standard of proof — Motion judge's failure to draw reasonable inferences rendered his findings of fact unreliable — Errors committed by motion judge were not harmless, as result may have been different — Motion judge excluded possibility of finding implied

consent by secured creditor because of his belief that he was prevented from drawing inferences from facts — Motion judge did not look at totality of considerations in weighing equities between parties.

Debtors and creditors --- Receivers — Conduct and liability of receiver — General conduct of receiver
Mortgages were registered against property owned by debtor W Inc. in favour of secured creditor R Corp. — H Inc. and debtor entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of property (H Lands) — H Inc. built store on H Lands — Debtor defaulted on mortgage, and receiver was appointed — Receiver partly succeeded in its motion seeking approval of sale of property to purchaser free of any claims by H Inc. — H Inc. unsuccessfully brought cross-motion for various relief regarding property — Motion judge held that equities favoured secured creditor, so receiver was entitled to order permitting sale on basis that it vested out H Inc. interests — Motion judge did not approve sale to purchaser until receiver conducted sales process on basis that purchaser would be entitled to acquire property free of any claim of H Inc. — H Inc. appealed — Receiver and secured creditor cross-appealed — Appeal allowed; cross-appeal dismissed — Matter was remitted for new hearing — Motion judge applied incorrect standard of proof — Motion judge's failure to draw reasonable inferences rendered his findings of fact unreliable — Errors committed by motion judge were not harmless, as result may have been different — Motion judge did not look at totality of considerations in weighing equities between parties — Decision as to whether H Inc.'s interest should be vested out could not properly be made until fact-finding process, including drawing reasonable inferences, was complete.

Real property --- Mortgages — Right of subrogation
Mortgages were registered against property owned by debtor W Inc. in favour of secured creditor R Corp. — H Inc. and debtor entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of property (H Lands) — H Inc. built store on H Lands — Debtor defaulted on mortgage, and receiver was appointed — Receiver partly succeeded in its motion seeking approval of sale of property to purchaser free of any claims by H Inc. — H Inc. unsuccessfully brought cross-motion for various relief regarding property — Motion judge held that secured creditor had subrogated claim in amount of monies outstanding under earlier mortgages at time of their refinancing, plus interest at rates provided under earlier mortgages — Motion judge held that secured creditor was entitled to assert subrogated claim against property in priority to that of H Inc. based on principles of unjust enrichment — H Inc. appealed — Receiver and secured creditor cross-appealed — Appeals allowed; cross-appeal dismissed — Matter was remitted for new hearing — Motion judge applied incorrect standard of proof — Motion judge's failure to draw reasonable inferences rendered his findings of fact unreliable — Errors committed by motion judge were not harmless, as result may have been different — Motion judge did not look at totality of considerations in weighing equities between parties.

Real property --- Registration of real property — Improvements made under mistake of title — Requirements for relief — Mistaken belief
Mortgages were registered against property owned by debtor W Inc. in favour of secured creditor R Corp. — H Inc. and debtor entered into purchase and sale agreement (H Agreement) and ground lease regarding portion of property (H Lands) — H Inc. built store on H Lands — Debtor defaulted on mortgage, and receiver was appointed — Receiver partly succeeded in its motion seeking approval of sale of property to purchaser free of any claims by H Inc. — H Inc. unsuccessfully brought cross-motion for various relief regarding property — Motion judge held that H Inc. was not entitled to lien under s. 37(1) of Conveyancing and Law of Property Act (CLPA) in amount of value by which property had been improved as result of construction of store — Motion judge held that H Inc. might have unregistered equitable agreement to purchase H Lands, but only if provisions of Planning Act were complied with — Motions judge held that H Inc. did not have sufficient interest in land under H Agreement or ground lease to assert claim under s. 37(1) of CLPA — H Inc. appealed — Receiver and secured creditor cross-appealed — Appeals allowed; cross-appeal dismissed — Matter was remitted for new hearing — Motion judge applied incorrect standard of proof — Motion judge's failure to draw reasonable inferences rendered his findings of fact unreliable — Errors committed by motion judge were not harmless, as result may have been different — Motion judge did not look at totality of considerations in weighing equities between parties.

Bankruptcy and insolvency --- Administration of estate — Sale of assets — Sales of asset subject to charge, mortgage, or hypothec
Debtor W Inc. owned property subject to lien by H Inc. — Lien of H Inc. ranked behind interest of secured creditor R Corp. — Receiver obtained order for sale of property, free and clear of interest held by H Inc. — H Inc. and secured creditor began appeal proceedings — Receiver reached agreement for sale of property — Receiver successfully brought motion for approval of sale and vesting order — Order was not stayed pending outcome of appeal proceedings, and H Inc.'s rights in property not preserved — Motion judge held that receiver made sufficient effort to get best price for property and did not act

improvidently — Motion judge held that sales process was not unfair — Motion judge held that all other known creditors ranked junior to secured creditor's mortgage — H Inc. appealed — Appeal allowed — Matter was remitted for new hearing — Motion judge applied incorrect standard of proof — Motion judge's failure to draw reasonable inferences rendered his findings of fact unreliable — Errors committed by motion judge were not harmless, as result may have been different — Motion judge did not look at totality of considerations in weighing equities between parties — Decision as to whether H Inc.'s interest should be vested out could not properly be made until fact-finding process, including drawing reasonable inferences, was complete.

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Civil practice and procedure --- Trials — Conduct of trial — Powers and duties of trial judge — Miscellaneous
Findings of fact — Debtor W Inc. owned property subject to lien by H Inc. — Lien of H Inc. ranked behind interest of secured creditor R Corp. — Receiver obtained order for sale of property, free and clear of interest held by H Inc. in first motion — Motion judge held that secured creditor's interest in property ranked higher in priority to H Inc.'s interest — Motion judge held that H Inc. failed to establish as undisputed fact that secured creditor consented to H Agreement or ground lease such that its mortgage was subordinated to instruments — Receiver successfully brought second motion approving sale and vesting order to purchaser — H Inc. appealed both decisions — Receiver and secured creditor cross-appealed first decision initially refusing to approve sale to purchaser — Appeals allowed; cross-appeal dismissed — Matter was remitted for new hearing — Motion judge applied incorrect standard of proof — Motion judge's failure to draw reasonable inferences rendered his findings of fact unreliable — Errors committed by motion judge were not harmless, as result may have been different — Motion judge did not look at totality of considerations in weighing equities between parties — Decision as to whether H Inc.'s interest should be vested out could not properly be made until fact-finding process, including drawing reasonable inferences, was complete.

Table of Authorities

Cases considered by *Paul Rouleau J.A.*:

C. (R.) v. McDougall (2008), [2008] 11 W.W.R. 414, 83 B.C.L.R. (4th) 1, (sub nom. *F.H. v. McDougall)* [2008] 3 S.C.R. 41, 2008 CarswellBC 2041, 2008 CarswellBC 2042, 2008 SCC 53, 60 C.C.L.T. (3d) 1, (sub nom. *H. (F.) v. McDougall)* 297 D.L.R. (4th) 193, 61 C.P.C. (6th) 1, 61 C.R. (6th) 1, (sub nom. *F.H. v. McDougall)* 380 N.R. 82, (sub nom. *F.H. v. McDougall)* 439 W.A.C. 74, (sub nom. *F.H. v. McDougall)* 260 B.C.A.C. 74 (S.C.C.) — considered

Meridian Credit Union Ltd. v. 984 Bay Street Inc. (2006), 2006 CarswellOnt 4783 (Ont. S.C.J.) — considered

Royal Bank v. Soundair Corp. (1991), 7 C.B.R. (3d) 1, 83 D.L.R. (4th) 76, 46 O.A.C. 321, 4 O.R. (3d) 1, 1991 CarswellOnt 205 (Ont. C.A.) — followed

York (Regional Municipality) v. Thornhill Green Co-Operative Homes Inc. (2010), 68 C.B.R. (5th) 73, 262 O.A.C. 232, 94 R.P.R. (4th) 1, 2010 CarswellOnt 3658, 2010 ONCA 393 (Ont. C.A.) — considered

Statutes considered:

Conveyancing and Law of Property Act, R.S.O. 1990, c. C.34
s. 37(1) — referred to

Land Titles Act, R.S.O. 1990, c. L.5
s. 71(1.1) [en. 1998, c. 18, Sched. E, s. 129] — referred to

s. 111(1) — referred to

Planning Act, R.S.O. 1990, c. P.13
Generally — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 37.13(2)(b) — referred to

Words and phrases considered:

inference

Inferences are not undisputed facts and, as a general rule, inferences need only flow reasonably and logically from established facts.

APPEALS by store owner H Inc. from judgments reported at *Romspen Investment Corp. v. Woods Property Development Inc.* (2011), 2011 CarswellOnt 2380, 75 C.B.R. (5th) 109, 2011 ONSC 3648, 4 R.P.R. (5th) 53 (Ont. S.C.J.), allowing receiver to sell property but not approving sale to purchaser and not allowing H Inc. to purchase portion of property, and *Romspen Investment Corp. v. Woods Property Development Inc.* (2011), 2011 CarswellOnt 10053, 2011 ONSC 5704 (Ont. S.C.J. [Commercial List]), approving purchase of property by purchaser; CROSS-APPEAL by receiver and secured creditor from judgment reported at *Romspen Investment Corp. v. Woods Property Development Inc.* (2011), 2011 CarswellOnt 2380, 75 C.B.R. (5th) 109, 2011 ONSC 3648, 4 R.P.R. (5th) 53 (Ont. S.C.J.), not approving sale of property to purchaser.

Paul Rouleau J.A.:

Overview

1 The appellant, Home Depot Canada Inc. ("Home Depot"), appeals from two orders. The first order is dated March 17, 2011 and granted, in part, a motion brought by SF Partners Inc., the receiver of Woods Property Development Inc. ("Woods"), (the "Receiver"). It authorized the Receiver to sell the property known as 20 High Street in Collingwood, Ontario (the "Woods Property") free and clear of any lien or claim of Home Depot. The motion judge, however, refused to approve the purchase of the Woods Property by 2204604 Ontario Inc. (the "Purchaser") without further marketing efforts.

2 The first order also dismissed Home Depot's cross-motion requesting an order that it be entitled to purchase a portion of the Woods Property or to lease the Woods Property. Alternatively, Home Depot requested that it be entitled to a statutory lien pursuant to s. 37(1) of the *Conveyancing and Law of Property Act*, R.S.O. 1990, c. C.34 or an equitable lien ranking prior to the mortgage over the Woods Property held by the respondent, Romspen Investment Corporation ("Romspen").

3 The second order under appeal is dated September 28, 2011. It approved the purchase of the Woods Property by the Purchaser and vested title in the Purchaser.

4 Romspen and the Receiver cross-appeal the first order seeking to set aside the refusal, at that time, to approve the purchase of the Woods Property by the Purchaser and substituting an order approving the purchase. Romspen recognized that the cross-appeal is moot but argues that it raises issues of importance such that this court should exercise its discretion to hear

it.

Facts

5 Woods is an Ontario corporation that owns the Woods Property. Romspen is a secured lender to Woods and Woods' sister company, TDCI Holdings Inc. ("TDCI"). Romspen's security includes an approximate $17 million mortgage over the Woods Property, which was used, in part, to discharge earlier mortgages given by Romspen (the "Romspen Mortgage"). The Receiver was appointed the interim receiver of all assets, undertakings and properties of Woods and TDCI by order of the Superior Court of Justice dated November 25, 2008. The Purchaser of the Woods Property is an Ontario corporation owned and controlled by Romspen.

6 These appeals center on a store built by Home Depot on an 8.67 acre parcel of land, which forms part of the larger 43 acre Woods Property (the "Home Depot Lands"). Home Depot constructed the store at a total cost to it of approximately $14.5 million. The issue in the motions under appeal was the fate of that store and the Home Depot Lands. Specifically, whether Home Depot could retain the store and either lease or purchase the Home Depot Lands.

7 On May 19, 2005, Home Depot entered into a purchase agreement with Woods for the purchase of the Home Depot Lands for a purchase price of $3.25 million. Among other terms, the purchase is conditional upon severance of the Home Depot Lands from the Woods Property in compliance with the *Planning Act*, R.S.O. 1990, c. P.13.

8 The purchase agreement between Woods and Home Depot was amended on November 30, 2005 (the "Home Depot Agreement"). Romspen received a copy of the Home Depot Agreement. Home Depot, however, did not register a caution in respect of its rights under the Home Depot Agreement pursuant to s. 71(1.1) of the *Land Titles Act*, R.S.O. 1990, c. L.5.

9 As the Home Depot Agreement is central to these appeals, I will outline the material provisions. The Home Depot Agreement provides as follows:

> 1) a portion of an industrial building located on the Woods Property is to be demolished to permit construction of the Home Depot store;
>
> 2) Home Depot is obligated to apply for a consent under the *Planning Act* to sever the Woods Property;
>
> 3) the Home Depot Agreement will be effective to create an interest in land only if the provisions of the *Planning Act* for severance are complied with;
>
> 4) Home Depot is entitled to apply to the Town of Collingwood for approval and a building permit to construct the Home Depot store on the Home Depot Lands;
>
> 5) if, within 270 days of the date of execution of the Home Depot Agreement, Home Depot fulfills all zoning conditions and obtains all necessary approvals for its proposed store, including a building permit, Home Depot will take possession of an area slightly larger than the Home Depot Lands pursuant to a ground lease (as there is no significance to the slight difference between the area covered by the ground lease and the area of land subject to the purchase agreement, both will be referred to as the "Home Depot Lands");
>
> 6) the ground lease is to run for a term of 50 years at a rental of $300,000 per year for the first seven years and thereafter at $100 per year;
>
> 7) the ground lease will terminate upon the severance of the Woods Property under the *Planning Act*, at which point, the purchase of the Home Depot Lands by Home Depot will be completed and the rental payments already made will be credited against the purchase price;
>
> 8) prior to entering into the ground lease and as a condition thereof, Woods will deliver an acknowledgment of Romspen's agreement to:

(a) permit the demolition of the existing industrial building without acceleration of the Romspen mortgages secured against the Woods Property; and

(b) provide a partial discharge of the Romspen mortgages upon payment of the purchase price of $3.25 million under the Home Depot Agreement, without requiring that the mortgages be in good standing at the time; and

9) Home Depot is entitled to register a caution in respect of its rights under the Home Depot Agreement pursuant to s. 71(1.1) of the *Land Titles Act*.

10 On May 4, 2006, Home Depot entered into the ground lease with Woods as contemplated by the Home Depot Agreement (the "Ground Lease"). Although the Ground Lease contained a provision relating to the registration of a notice of Ground Lease pursuant to s. 111(1) of the *Land Titles Act*, Home Depot did not register the notice nor did it obtain an express postponement or subordination of Romspen's rights as mortgagee.

11 In the Ground Lease, Woods represented that it had obtained the acknowledgement from Romspen contemplated in the Home Depot Agreement to the effect that Romspen had agreed that:

1) the demolition of the portion of the industrial building would not accelerate the Romspen mortgages on the Woods Property at the time so as to allow construction of the Home Depot store; and

2) Romspen would provide a partial discharge of its mortgage should Home Depot purchase the Home Depot Lands.

12 Romspen had agreed to the demolition of a portion of the industrial building but denies that there was any agreement respecting the partial discharge of the mortgage. The materials filed in the motion show that Woods requested that acknowledgment but that Romspen refused to give it. The motion judge simply observed that: "It is unclear on what basis Woods gave the representation".

13 To allow construction of the Home Depot store, Romspen signed a site plan control agreement dated July 20, 2006 to which Woods, Home Depot and the Town of Collingwood were also parties (the "Site Plan Agreement"). The Site Plan Agreement refers to the Home Depot Agreement as well as to the demolition of the portion of the industrial building and the proposed construction of the Home Depot store. It also refers to the existence of the Romspen mortgages and contains an express postponement and subordination by Romspen of its interest in the Woods Property to that of the Town of Collingwood. There is no postponement or subordination by Romspen to Home Depot.

14 Home Depot applied for severance of the Home Depot Lands but the Town of Collingwood will not consent to the severance until a comprehensive plan of subdivision is filed and approved for the entire Woods Property.

15 The Home Depot store was constructed and has been operating since early 2007.

16 Woods first defaulted on the Romspen Mortgage in 2007. Payments ceased on the Romspen Mortgage in early 2008, leading to the Receiver's appointment. The receivership order authorized the Receiver to market the Woods Property. After approximately 10 months, the Receiver accepted the Purchaser's offer dated October 13, 2009 regarding the sale of the Woods Property for a purchase price of $14.1 million (the "Purchase Agreement"). The Purchase Agreement is conditional upon the Woods Property being delivered free and clear of any claims of Home Depot unless arrangements are reached on terms satisfactory to the Purchaser in its sole discretion. No such arrangements were reached. The proceeds of the sale are insufficient to cover the indebtedness owing to Romspen under its mortgage.

17 The Receiver moved for court approval of the Purchase Agreement and for an order vesting title to the Woods

Property in the Purchaser. Home Depot took the position that the Receiver could not sell the Woods Property on which the Home Depot store is located free and clear of any interest of Home Depot and argued that it should be entitled to purchase the Home Depot Lands or to a lease or, alternatively, to a statutory or equitable lien ranking ahead of the Romspen Mortgage.

18 In very thorough reasons, the motion judge laid out the factual situation and the relevant case law. He concluded that Home Depot's leasehold interest in the Home Depot Lands ranked after the Romspen Mortgage and, although Home Depot was entitled to an equitable lien against the Woods Property, that lien was subordinate to the Romspen Mortgage. He then considered the equities between the parties in relation to the specific issues and concluded that the equities favoured Romspen.

19 Accordingly, in the first order, he authorized the Receiver to proceed with the sale of the Woods Property free and clear of any lien or claim of Home Depot. That is, he vested out or expunged any interest Home Depot had in the Woods Property. The motion judge, however, refused to approve the Purchase Agreement at that time and ordered the Receiver to conduct a further sales process in respect of the Woods Property.

20 Further efforts at finding a purchaser for the Woods Property were unsuccessful and a new motion was brought seeking the approval of the Purchase Agreement. On September 28, 2011, the motion judge granted the second order approving the sale transaction and vesting the Woods Property in the Purchaser free and clear of any lien or claim of Home Depot.

21 By order of this court, the motion judge's order approving the sale transaction was stayed until the hearing of the appeals or further order of this court.

Issues

22 Home Depot raised several grounds of appeal. In oral submissions, however, Home Depot focused on the following two grounds:

> 1) Did the motion judge apply an incorrect standard of proof? Specifically, did his failure to draw reasonable inferences render his findings of fact unreliable?
>
> 2) Did the motion judge fail to consider the ownership of the Home Depot store separate and apart from the Ground Lease?

23 I need only deal with the first issue as, in my view, it is dispositive of the appeals. The motion judge's misapprehension of the standard of proof requires that the orders be set aside and that the matter be remitted to the Superior Court of Justice for a new hearing. As I would remit the matter for a new hearing, I would dismiss Romspen and the Receiver's cross-appeal of the first order.

Analysis

Applicable Law

24 The parties agree that the criteria to be applied by the court in a receivership sale are those set out by this court in *Royal Bank v. Soundair Corp.* (1991), 4 O.R. (3d) 1 (Ont. C.A.). At p. 6, this court summarized the factors a court must consider when deciding whether a receiver, who has sold a property, acted properly:

> 1) It should consider whether the receiver has made a sufficient effort to get the best price and has not acted

improvidently.

2) It should consider the interests of all parties.

3) It should consider the efficacy and integrity of the process by which offers are obtained.

4) It should consider whether there has been unfairness in the working out of the process.

25 The central issue raised on the motions and in these appeals is the application of the second criterion, the consideration of the interests of all parties, when deciding whether the court should vest the Woods Property in the Purchaser free and clear of Home Depot's interest. In considering this criterion, the motion judge referred to Ground J.'s statement in *Meridian Credit Union Ltd. v. 984 Bay Street Inc.* [2006 CarswellOnt 4783 (Ont. S.C.J.)], 2006 CanLII 26476, at para. 19, that: "[I]n determining whether to issue a vesting order terminating the interests of parties in a property, the court must review the equitable considerations supporting the respective positions of the parties." The motion judge then set about making the findings of fact necessary to apply these legal principles.

Position of the Parties on Appeal: Standard of Proof in Making Findings of Fact

26 Home Depot argues that the motion judge committed an error of law in the standard of proof he applied when making findings of fact. Throughout his reasons, the motion judge indicates that he is required to make factual determinations "on the basis of undisputed facts" and that he "cannot make findings of fact by way of inference." Home Depot maintains that this is clearly an error and that the failure to apply the correct standard of proof resulted in the motion judge's failure to draw reasonable inferences from the evidence.

27 Home Depot submits that several important inferences were available on the evidence. Specifically, it could be inferred from the evidence that Romspen gave its express or implied consent to the construction of the Home Depot store and to entering into the Ground Lease. Alternatively, Home Depot submits that if there is no express or implied consent, the record is sufficient to draw the inference that, from the outset, Romspen knew about the construction of the Home Depot store, knew about the Ground Lease and knew or ought to have known that Home Depot believed it had Romspen's consent to build the store and enter into the Ground Lease. These and other possible inferences, if drawn, would have been relevant considerations in the exercise of the court's equitable jurisdiction when deciding whether to vest out Home Depot's interest and/or whether to grant Home Depot some form of equitable relief.

28 The respondents could provide no legal basis for the motion judge's statement that factual findings must be made on the basis of "undisputed facts" and that the court could not "make findings of fact by way of inference." It may be that, because this was a motion argued on affidavit evidence, the motion judge understood that he was constrained in this way. In any event, the respondents did not seriously dispute that these constituted errors, rather, they argued that these errors were harmless because:

1) there were no disputed facts;

2) the errors were mere inadvertent slips and, when read as a whole, it is apparent that the motion judge nonetheless applied the appropriate standard of proof;

3) it was clear from the evidence that Romspen's mortgage had legal priority over any interest Home Depot had in the Woods Property;

4) there was insufficient evidence on the record before the motion judge from which actual or implied consent to the Ground Lease or construction of the Home Depot store could be drawn; and

5) even accepting that the court could infer or imply consent, the equities nonetheless favoured Romspen and the

vesting out of Home Depot's interest.

Discussion

29 In my view, the appeals must be allowed and the matter remitted to the Superior Court of Justice for a new hearing. I acknowledge that, in granting equitable relief, motion judges have a good deal of latitude and ought to be afforded considerable deference. As set out by this court in *York (Regional Municipality) v. Thornhill Green Co-Operative Homes Inc.*, 2010 ONCA 393, 68 C.B.R. (5th) 73 (Ont. C.A.), at para. 20, an order approving a sale by a receiver is discretionary and attracts great deference from appellate courts. Appellate courts will only interfere where the trial judge (or the motion judge) "erred in law, seriously misapprehended the evidence, exercised his or her discretion based upon irrelevant or erroneous considerations, or failed to give any or sufficient weight to relevant considerations."

30 In the present case, however, the motion judge's application of an incorrect standard of proof and his belief that he was not allowed to draw inferences on a motion such as this one are errors that go to the very basis upon which the court's equitable discretion is exercised: the factual matrix. As explained by Rothstein J. in *C. (R.) v. McDougall*, 2008 SCC 53, [2008] 3 S.C.R. 41 (S.C.C.), at para. 40, "there is only one civil standard of proof at common law and that is proof on a balance of probabilities." Therefore, facts in issue are to be proved on a balance of probabilities and, as a general rule, this applies to motions[1] as well as to trials.

31 As I will explain, the errors committed by the motion judge are not, as suggested by the respondents, harmless. Had the motion judge applied the appropriate standard of proof and been willing to draw inferences where appropriate, the result may well have been different. I turn now to the five points raised by the respondents in response to the appeals.

1) There were no disputed facts

32 The respondents argue that the motion judge's adoption of a higher standard of proof — undisputed fact — is a harmless error as there was no dispute as to the facts. It was therefore unnecessary for the motion judge to engage in an assessment of the weight to be given to the evidence or to make credibility findings.

33 The argument put forward by Home Depot, however, is not that it disputed the facts set out in the record, but rather that the motion judge ought to have drawn inferences from the record and the conduct of the parties.

34 Inferences are not undisputed facts and, as a general rule, inferences need only flow reasonably and logically from established facts. By limiting himself to undisputed facts, the motion judge did not assess the landscape of facts presented to him with a view to determining what inferences could appropriately be drawn.

35 The potential importance of inferences is apparent when considering whether Romspen's interest in the Woods Property should be subordinate to the Ground Lease by virtue of Romspen having consented to it. In dealing with this issue, the motion judge set out the law as follows, at para. 142: "[I]f a lease is executed by a mortgagor after the mortgage has been granted, the mortgagee will be bound by the terms of the lease if it is made with his express or implied consent" (footnote omitted).

36 The record did not contain an express consent by Romspen. The relevant question on the issue of subordination was, therefore, whether consent by Romspen to the Ground Lease could be implied. Home Depot argued that the conduct of Romspen and the various documents in the record were more than sufficient to show that consent ought to be implied.

37 The motion judge, however, does not appear to have turned his mind to the issue of implied consent. The motion judge simply stated, at para. 145, that: "Home Depot has failed to establish as an *undisputed fact* that Romspen consented to either the Home Depot Agreement or the Ground Lease" (emphasis added). The motion judge's use of the expression "undisputed fact" clearly reflects his understanding that, absent Romspen expressly acknowledging that it consented to the Ground Lease or it being set out in the written materials, he could not find that Romspen had consented. In effect, the motion judge

excluded the possibility of finding an implied consent because of his belief that he was somehow prevented or unable to draw appropriate inferences from the available facts. Inferences are important tools in the fact-finding process and the motion judge erred in refusing to avail himself of that source.

2) The errors were inadvertent slips

38 The respondents argue that the motion judge's references to the need for "undisputed facts" and his inability to "make findings of fact by way of inference" were simply inadvertent slips and that, read as a whole, it was apparent that the motion judge nonetheless applied the appropriate standard of proof.

39 I disagree. A critical portion of the motion judge's reasons is the portion dealing with Romspen's knowledge and alleged consent to the Home Depot Agreement, the Ground Lease and the construction of the Home Depot store. In that portion of his reasons, he repeats, at paras. 40 and 44 of his March 17, 2011 reasons, that the court must make its determination on the basis of "undisputed facts". He also states, at para. 40 of those reasons, that the court "cannot make findings of fact by way of inference." After making these statements, he concludes, at para. 52, that "[t]here is no evidence of any such consent, and it *cannot be inferred* from the existence of the Home Depot Agreement. Nor *can it be inferred* from the existence of the Ground Lease" (emphasis added). The motion judge then goes on to state, at para. 53, that "Home Depot cannot, however, establish as an *undisputed fact* that Romspen's execution of the Site Plan Agreement either constituted, or evidenced, its consent to ... [the] construction [of the Home Depot store]" (emphasis added).

40 However, despite the motion judge having stated that he could not draw inferences, the respondents argue that his statement that he did "not think that ... knowledge [of the Ground Lease] could be inferred" (at para. 42), suggests that he did in fact consider whether inferences could be drawn. I disagree.

41 When that statement is viewed in the context of the entire paragraph, it does not, as the respondents suggest, indicate that the motion judge was applying the correct standard of proof. The balance of the paragraph shows that the motion judge was still operating on the premise that Home Depot had to demonstrate either actual knowledge or knowledge as an undisputed fact.

42 The fact that the motion judge applied the incorrect higher standard of proof is confirmed later in his March 17, 2011 reasons where, at para. 145, he confirms that he has "concluded that Home Depot has failed to establish as an *undisputed fact* that Romspen consented to either the Home Depot Agreement or the Ground Lease" (emphasis added).

43 Further, it was central to Home Depot's case to determine whether knowledge or implied consent of the Ground Lease and construction of the Home Depot store could be inferred from all of the circumstances. Given the motion judge's extensive and comprehensive reasons, I simply cannot accept that, had he understood that he could draw reasonable inferences from all of the facts and circumstances, his analysis of whether to draw the inference would be limited to a single paragraph without reference to the facts both for and against drawing such an inference.

3) Romspen's mortgage has legal priority

44 The respondents submit that the errors are of no consequence because the Romspen Mortgage had clear legal priority over any Home Depot interest and the funds generated from the sale of the Woods Property are not even sufficient to pay off the mortgage debt. Moreover, nothing in the record suggests that Romspen ever intended to waive any of its legal rights.

45 The respondents argue that the motion judge correctly weighed the equities between the parties. More specifically, in granting the Receiver's request for an order vesting out the interest of Home Depot in the Woods Property, the motion judge stated, at para. 187, that:

> [T]he court must consider the equities between the parties in the context of findings that:

> (1) Romspen's interest in the Woods Property ranks ahead of that of Home Depot to the extent of the monies secured under the Romspen Mortgage ...;
>
> (2) Home Depot's equitable lien against the [Woods] Property arising as a result of the construction of the Home Depot store does not rank prior to the interest of Romspen in the [Woods] Property; and
>
> (3) Home Depot is unable to establish as an undisputed fact that Romspen consented to the Home Depot Agreement, the Ground Lease or the construction of the Home Depot store in a manner that was intended to affect its rights in the [Woods] Property.

46 There are two problems with this submission. First, although the motion judge appears to view the need, in considering the equities, to look beyond the legal priorities created by the instruments registered on title, he limits his equitable considerations to: (1) a recitation of the legal priorities; and (2) the single additional question of whether there was consent "in a manner that was *intended* to affect its right in the [Woods] Property" (emphasis added). The motion judge had to look beyond these considerations. He had to consider all of the facts and circumstances in order to decide whether consent should be inferred and whether equitable principles, such as estoppel, applied in making the determination to vest out Home Depot's interest.

47 Second, although the motion judge refers to his earlier analysis of the equitable considerations and the need to take them into account in the weighing exercise, that earlier analysis was, as I have explained, tainted by his understanding that he was limited to undisputed facts and could not draw inferences.

4) There was no basis from which to draw the inferences sought by Home Depot

48 In the alternative, the respondents argue that even if the motion judge erred with respect to his ability to draw inferences, this court should find that there was no basis from which the inferences sought by Home Depot could be drawn.

49 As I would remit the matter to the Superior Court of Justice, it would be inappropriate for this court to draw inferences and make findings of fact. In order to address the respondents' submission that there was no basis in the evidence to draw relevant inferences, I must, however, review the record to determine whether facts exist from which a motion judge might draw at least one of the inferences sought by Home Depot. I will focus on Home Depot's submission that the motion judge ought to have inferred that Romspen knew of and by implication consented to the Ground Lease. If such an inference were drawn, it would clearly be a significant fact to be weighed in resolving the issues raised in the motion.

50 In my view, there are several facts from which such an inference might be drawn, for example:

> 1) the earlier Romspen mortgages provided that Romspen could not unreasonably withhold its consent to any lease by Woods;
>
> 2) in November 2005, Romspen received a copy of the Home Depot Agreement which contained the material terms of the contemplated ground lease to Home Depot;
>
> 3) the Home Depot Agreement contemplated the construction of a store on the Home Depot Lands within 270 days of the signature of the Home Depot Agreement;
>
> 4) the Home Depot Agreement set out the terms of the Ground Lease and contemplated the purchase of the Home Depot Lands by Home Depot if severance had been obtained or the Ground Lease if severance had not been obtained (these broad terms were known to Romspen);
>
> 5) although Romspen refused to provide an acknowledgment that it would provide a partial discharge to allow Home Depot to purchase the Home Depot Lands, Woods asked Romspen to sign an acknowledgment that a portion

of the industrial building located on the Woods Property could be demolished to allow construction of the Home Depot store without accelerating the Romspen Mortgage. Romspen was asked to provide this acknowledgement so that Home Depot would not "stop moving forward." This acknowledgment was provided in May 2006 and refers to a proposed ground lease between Woods and Home Depot;

6) the Romspen Mortgage included a provision that contemplated that "any land lease payments made by Home Depot pursuant to the Home Depot Agreement ... which in aggregate exceed $250,000 shall be due and payable, on account of principle, upon receipt and [Woods and TDCI] shall direct Home Depot to make such payments directly to [Romspen]";

7) the Site Plan Agreement executed by Romspen made specific reference to the Home Depot Agreement and to the proposed partial demolition of the existing industrial building;

8) under the Site Plan Agreement, Romspen would have known that Home Depot was spending millions of dollars to build a store on the Woods Property and that, pursuant to the Home Depot Agreement, Home Depot was entitled to enter into the Ground Lease; and

9) Romspen's representative testified in cross-examination that, by August 2006, after the Site Plan Agreement had been signed, he was able to draw the inference that Home Depot had received the Ground Lease.

51 These are some of the facts from which an inference might be drawn. Of course, there are many facts that suggest that the inference should not be drawn. I need not list them here. Suffice it to say that a basis does exist from which a relevant inference could be drawn and, contrary to the respondents' submission, I do not view the motion judge's error as being necessarily harmless.

5) Even assuming that the inferences sought by Home Depot could be drawn, the equities still favour vesting out Home Depot's interest in the Woods Property

52 The respondents argue that regardless of the inferences that might be drawn, the equities will still inevitably favour the vesting out of Home Depot's interest. I disagree. The inferences Home Depot argues ought to have been drawn are central to the decision of whether to vest out its interest. This decision therefore cannot properly be made until the fact-finding process, including drawing reasonable inferences, is complete. That fact-finding process is more appropriately done by the Superior Court.

Conclusion

53 I would, therefore, allow the appeals, dismiss the cross-appeal and remit the matter to the Superior Court of Justice for a new hearing. If the parties cannot agree as to costs, they are to make brief written submissions within 20 days hereof.

John Laskin J.A.:
I agree

M. Rosenberg J.A.:
I agree

Appeals allowed; cross-appeal dismissed.

Footnotes

[1] A motion judge can, in appropriate circumstances, order the trial of an issue pursuant to rule 37.13(2)(b) of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194.

End of Document

TAB 7

2015 ONSC 2794
Ontario Superior Court of Justice

Trez Capital Limited Partnership v. Wynford Professional Centre Ltd.

2015 CarswellOnt 18914, 2015 ONSC 2794, [2015] O.J. No. 6514, 261 A.C.W.S. (3d) 456, 63 R.P.R. (5th) 138

In the Matter of Section 101 of the Courts of Justice Act and Section 243 of the Bankruptcy and Insolvency Act

Trez Capital Limited Partnership and Computershare Trust Company of Canada, Applicants and Wynford Professional Centre Ltd. and Global Mills Inc., Respondents

L.A. Pattillo J.

Heard: April 28, 2015
Judgment: December 10, 2015 *
Docket: CV-14-10493-00CL

Counsel: Shawn Pulver, Debora Miller-Lichtenstein, for Metro Toronto Condominium Corporation No. 1037
Irving Marks, Dominique Michaud, for Trez Capital Limited Partnership
Danielle Glatt, for DBDC Spadina Ltd. et al.

Subject: Corporate and Commercial; Insolvency; Property
Related Abridgment Classifications
Real property
VII Mortgages
VII.2 Nature and form of mortgage
VII.2.g Equitable mortgage
VII.2.g.vi Miscellaneous
Real property
VII Mortgages
VII.14 Priorities
VII.14.b Between types of creditors
VII.14.b.v Equitable mortgagee and equitable interest holder

Headnote

Real property --- Mortgages — Nature and form of mortgage — Equitable mortgage — Miscellaneous

TC was limited partnership that operated as commercial mortgage lender, and CTC held mortgage security as custodian for TC on its loans — W Ltd. purchased 83 condominium units and 297 parking spaces in commercial condominium and became majority owner — As security for mortgage financing provided by TC, W Ltd. provided charge/mortgage to CTC which was registered as first charge on W Ltd.'s units — Condominium corporation provided status certificates stating that there were no arrears of common element expense fees — Unit owners subsequently learned that W Ltd. was in arrears of payment of its common element fees and that no statutory lien for fee arrears had been registered against its units — Receiver was appointed and held monies from proceeds of sale of W Ltd.'s units in trust in respect of corporation's priority claim for common expense arrears — Corporation brought motion seeking priority over mortgage held by TC and CTC ("applicants") on W Ltd.'s units — Motion dismissed — Corporation was not entitled to equitable lien based on alleged unjust enrichment of W Ltd. on account of arrears of common expenses — Condominium Act, 1998 clearly sets out corporation's right to lien for common expense arrears; it was not proper for court to create equitable lien in its place — Purpose of ss. 85 and 86 of Act is to safeguard financial viability of condominium corporation in manner

that balances rights of all stakeholders — To interfere with that balance by granting equitable lien in circumstances where statutory lien had expired would be contrary to purpose of Act — Even if equitable lien were available, it would not have priority over mortgage — Receiver authorized to pay monies held in trust pursuant to order to applicants based on their priority.

Real property --- Mortgages — Priorities — Between types of creditors — Equitable mortgagee and equitable interest holder

TC was limited partnership that operated as commercial mortgage lender, and CTC held mortgage security as custodian for TC on its loans — W Ltd. purchased 83 condominium units and 297 parking spaces in commercial condominium and became majority owner — As security for mortgage financing provided by TC, W Ltd. provided charge/mortgage to CTC which was registered as first charge on W Ltd.'s units — Condominium corporation provided status certificates stating that there were no arrears of common element expense fees — Unit owners subsequently learned that W Ltd. was in arrears of payment of its common element fees and that no statutory lien for fee arrears had been registered against its units — Receiver was appointed and held monies from proceeds of sale of W Ltd.'s units in trust in respect of corporation's priority claim for common expense arrears — Corporation brought motion seeking priority over mortgage held by TC and CTC ("applicants") on W Ltd.'s units — Motion dismissed — Equitable lien was not available but even if it were, corporation would not have priority over mortgage — Under s. 93(3) of Land Titles Act, registered charge/mortgage takes priority over all unregistered interests in land — Prior to advancing loan, TC did extensive due diligence — There was nothing in status certificates that should have raised any concerns about corporation or its financial situation and, in particular, W Ltd.'s common expense fees — TC was entitled to rely on status certificates and explicit representation that W Ltd. had no common expense arrears — Revival of lien would upset balance provided in Act and would deprive TC of proper and timely notice to enable it to consider all its options — Receiver authorized to pay monies held in trust pursuant to order to applicants based on their priority.

Table of Authorities

Cases considered by *L.A. Pattillo J.*:

Rafat General Contractor Inc. v. 1015734 Ontario Ltd. (2005), 2005 CarswellOnt 7519, 52 C.L.R. (3d) 63, 81 O.R. (3d) 798 (Ont. S.C.J.) — referred to

Romspen Investment Corp. v. Woods Property Development Inc. (2011), 2011 CarswellOnt 2380, 2011 ONSC 3648, 75 C.B.R. (5th) 109, 4 R.P.R. (5th) 53 (Ont. S.C.J.) — followed

Romspen Investment Corp. v. Woods Property Development Inc. (2011), 2011 ONCA 817, 2011 CarswellOnt 14462, 85 C.B.R. (5th) 21, 286 O.A.C. 189, 14 R.P.R. (5th) 1, 346 D.L.R. (4th) 273 (Ont. C.A.) — referred to

Talbot v. Pawelzik (2005), 2005 CarswellOnt 741, 29 R.P.R. (4th) 56 (Ont. S.C.J.) — referred to

Toronto Standard Condominium Corp. No. 1908 v. Stefco Plumbing & Mechanical Contracting Inc. (2014), 2014 ONCA 696, 2014 CarswellOnt 14131, 47 R.P.R. (5th) 15, 377 D.L.R. (4th) 369, 325 O.A.C. 231 (Ont. C.A.) — distinguished

Statutes considered:

Condominium Act, 1998, S.O. 1998, c. 19

Generally — referred to

s. 37 — considered

s. 37(1)(b) — considered

s. 76 — considered

s. 76(1) — considered

s. 76(1)(i) — considered

s. 76(1)(m)(ii) — considered

s. 76(4) — considered

s. 76(6) — considered

ss. 84-88 — referred to

s. 84(1) — considered

s. 85 — considered

s. 85(3) — considered

s. 86 — considered

s. 86(3) — considered

s. 134 — considered

s. 134(3) — considered

Construction Lien Act, R.S.O. 1990, c. C.30

Generally — referred to

Land Titles Act, R.S.O. 1990, c. L.5

s. 93(3) — considered

Words and phrases considered:

equitable lien

An equitable lien is a form of equitable charge upon property until certain claims are satisfied.

An equitable lien is an unregistered interest [in land].

MOTION by condominium corporation granting it priority over mortgage held by applicants on certain units in condominium.

***L.A. Pattillo J.*:**

Introduction

1 Metro Toronto Condominium Corporation No. 1037 ("MTCC 1037") brings this motion seeking priority over a mortgage held by the applicants' Trez Capital Limited Partnership ("Trez") and Computershare Trust Company of Canada ("Computershare") on certain units in MTCC 1037 (the "Mortgage").

2 Specifically, MTCC 1037 seeks an order granting it an equitable mortgage over the units in question on account of arrears of common expense fees owing on the units and granting it priority over the Mortgage. In the alternative, MTCC 1037 seeks an order reviving its right to a lien against the units in question pursuant to s. 85 and 86 of the *Condominium Act*, 1998, S.O. 1998 (the "Act") and granting it priority over the Mortgage.

3 For the reasons that follow, MTCC 1037's motion is dismissed in its entirety.

Background

4 MTCC 1037 is a commercial condominium, created pursuant to the Act on October 6, 1992. It is comprised of 119 commercial units, 361 parking units and 2 storage units and is located at 18 Wynford Drive, Toronto, Ontario (the "Wynford Property").

5 Trez is a limited partnership that operates as a commercial mortgage lender. Computershare holds the mortgage security as the custodian for Trez on Trez loans.

6 On or about February 7, 2011, Wynford Professional Ltd. ("Wynford") purchased 83 condominium units and 297 parking spaces in MTCC 1039 (the "Wynford Units"). Wynford was controlled by Norma Walton ("Norma") and her husband Ronauld Walton ("Ronauld") (collectively the "Waltons") who, at the time of the events in issue, were both lawyers in good standing with the Law Society of Upper Canada.

7 Upon the purchase of the Wynford Units, Wynford, as the owner of the majority of the units in MTCC 1037, assumed control of its board of directors (the "Board") and management. The Waltons became officers and directors of the Board. Norma was the President and Chairman of the Board and Ronauld was the Secretary. The other directors, who were independent, were Dr. Stanley Bernstein ("Dr. Bernstein"), a business partner of the Waltons, George Habib, the president and Chief Executive of an association which owns units in MTCC 1037 ("Habib") and Jonathan Griffiths, a lawyer who also owns a unit in MTCC 1037. Dr. Bernstein has subsequently denied any knowledge that he was appointed a director.

8 MTCC 1037 also appointed the Rose and Thistle Group Inc. ("Rose and Thistle"), a company controlled by the Waltons, as property manager of the Wynford Property.

9 In or around February 2013, Wynford approached Trez about providing mortgage financing to enable it to refinance the Wynford Units. Trez had a pre-existing business relationship with the Waltons and Rose and Thistle. On February 19, 2013, Trez issued a commitment letter to Wynford agreeing to lend it $9,850,000 (the "Loan") on terms and conditions set out therein (the "Commitment Letter"). The Commitment Letter was agreed to by Wynford.

10 Following due diligence undertaken by both Trez and its lawyers, the Loan was fully advanced to Wynford on March 7, 2013. As security for the Loan, Wynford provided, among other things, a charge/mortgage to Computershare which was registered in Land Titles as a first position on the Wynford Units (the "Mortgage").

11 Prior to closing, Trez received two separate status certificates from MTCC 1037 dated March 6, 2013 (the "Status Certificates") signed by Norma in her capacity as President of MTCC 1037 and a statutory declaration, also dated March 6, 2013, sworn by Norma on behalf of Wynford (the "Statutory Declaration").

12 The Status Certificates were in relation to the condominium units and the parking units respectively and, among other things:

a) stated that Wynford was not in default of payment of common element fees for the Wynford Units;

b) appended a list of all the Wynford Units which clearly stated under the column "Common Expenses Payment" that the Wynford Units were not in default; and

c) stated that the MTCC 1037 reserve fund was in good order.

13 The Statutory Declaration stated, among other things, that:

a) Norma was unaware of any corporation who would have any claim or interest in the Wynford Property that is adverse or inconsistent with Wynford's title to the Wynford Units;

b) there were no special assessments contemplated by MTCC 1037 and there were no legal actions pending or in conflict by or against MTCC 1037;

c) Wynford had complied with all terms, conditions, rules and regulations contained in the respective Condominium Declaration, By-Laws and Regulations since Wynford purchased the Wynford Units; and

d) the representations made to Trez in the Commitment Letter and the other related security arising therefrom was true and accurate.

14 As a result of a dispute which arose between the Waltons and Dr. Bernstein in respect of Rose and Thistle, an order was obtained dated November 5, 2013, appointing a Manager of Wynford and 31 other companies related to Rose and Thistle.

15 In or around December 2013, MTCC 1037's evidence is that the minority directors of the Board learned that the Waltons potentially had been negligent or worse fraudulent and acted in bad faith in their role as directors and officers of MTTC 1037. Subsequently, at a court ordered annual general meeting of MTCC 1037 held on February 13, 2014, the Waltons were removed as directors and a new board of directors was elected.

16 It was at the February 13, 2014 AGM that the MTCC 1037 unit owners say that they learned for the first time that Wynford was in arrears of payment of its common element fees and that no statutory lien for common element fee arrears had been registered against the Wynford Units. MTCC 1037's evidence is that the new board did not learn the exact amount of the arrears until sometime in March 2014.

17 By order dated April 2, 2014, the Wynford Units were removed from the Manager and Collins Barrow Toronto Limited was appointed receiver of Wynford (the "Receiver").

18 In May 2014, the Receiver made payment of Wynford's common element fee arrears to MTCC 1037 for the months of February, March and April 2014. The Receiver then continued to keep Wynford's common element fees current.

19 Wynford's common element fee arrears are $1,284,508.23. Up to March 7, 2013, the date when the Loan was fully advanced and the Mortgage registered, Wynford's arrears were $811,841.34.

20 On March 27, 2015, in contemplation of the sale of the Wynford Units, the Receiver obtained an approval, vesting and distribution order from the court (the "Order"). The Order provided, in part, that $1,284,508.23 was to be held in trust by the Receiver from the proceeds of the sale of the Wynford Units in respect of MTCC 1037's priority claim for common expense arrears and not paid until further order of the court.

21 MTCC 1037 has commenced an action against, among others, the Waltons and have sought, among other things, the following declarations against them: that they acted fraudulently, negligently and in bad faith by failing to pay Wynford's share of its common expenses totaling $1,284,508.23; that they acted fraudulently, negligently and in bad faith by failing, as controlling members of the Board, to lien the Wynford Units for arrears of the common element fees pursuant to s. 86 of the Act; and that they breached s. 37 of the Act by failing to act honestly and in good faith (the "Fraud Action").

22 For the purposes of this motion, MTCC 1037 and Trez/Computershare have agreed to proceed on the presumption that MTCC 1037 will be able to subsequently establish its allegations of fraud, negligence and bad faith against the Waltons in the Fraud Action.

The Issues

23 The issues on this motion, as framed by MTCC 1037, are:

1) Should MTCC 1037 be granted an equitable lien;

2) If MTCC 1037 is granted an equitable lien, does it take priority over the Mortgage; and

3) In the alternative, if an equitable lien is not granted, should MTCC 1037 be granted the right to revive its lien rights with respect to Wynford's common element fee arrears pursuant to ss. 85 and 86 of the Act.

Equitable Lien

24 An equitable lien is a form of equitable charge upon property until certain claims are satisfied. It arises by operation of equity from the relationship of the parties, rather than by any act of theirs: *Snell's Equity*, 32nd edition, General Editor John McGhee (2010, Thomson Reuters) at Ch. 44-004, p. 1146.

25 Equitable liens will be available in circumstances that would give rise to a constructive trust (such as breach of fiduciary obligation and breach of confidence) as well as circumstances outside the fiduciary context such as response to improvements made to land under mistake and in the context of indemnity insurance: Maddaugh and McCamus, *The Law of Restitution*, Looseleaf Edition, at pp. 5-45 and 5-46.

26 MTCC 1037 submits that it is entitled to an equitable lien based on Wynford's unjust enrichment (not having to pay its 2012 and 2013 common expense fees) to MTCC 1037's corresponding detriment.

27 Trez/Computershare submit that MTCC 1037's lien rights are restricted to the provisions of the Act which it has failed to comply with and accordingly, it is not entitled to an equitable lien.

28 Part VI of the Act, sections 84 to 88 deal with common expenses.

29 Section 84(1) of the Act provides that the owners shall contribute to the common expenses in the proportion specified in the declaration.

30 Section 85 of the Act allows a condominium corporation to register a lien against an owner's unit for up to three (3) months of common expense fee arrears. If a certificate of lien is not registered on title during this time period, the lien expires. Once a certificate of lien is registered, s. 85(3) provides that all future unpaid common expense fee arrears are captured under the registered lien.

31 Section 86 of the Act provides that a certificate of lien registered pursuant to s. 85 has priority over all mortgages registered against the unit in question provided that the condominium corporation complies with the notice provision in s. 86(3). That subsection requires that the condominium corporation shall, on or before the day the certificate of lien is registered, give written notice of the lien to everyone whose encumbrance is registered against the title of the unit affected by the lien.

32 I agree with Trez/Computershare's submission. The Act clearly sets out MTCC's right to a lien for common expense arrears. As a result, it is not proper for the court to create an equitable lien in its place. The principle is analogous to case law under similar statutes, such as the *Construction Lien Act*, which have held the court cannot create an equitable lien where a statute has occupied the field by creating a lien for the same purpose. See: *Talbot v. Pawelzik*, [2005] O.J. No. 748 (Ont. S.C.J.) at para. 20 and *Rafat General Contractor Inc. v. 1015734 Ontario Ltd.* (2005), 81 O.R. (3d) 798 (Ont. S.C.J.).

33 The purpose of ss. 85 and 86 of the Act is to safeguard the financial viability of the condominium corporation in a manner that balances the rights of all the stakeholders, including, among others, both the condominium corporation and mortgagees: *Toronto Standard Condominium Corp. No. 1908 v. Stefco Plumbing & Mechanical Contracting Inc.*, 2014 ONCA 696 (Ont. C.A.) at para. 41. To interfere with that balance by granting an equitable lien in circumstances where the statutory lien has expired, regardless of the reason, would be contrary to the purpose of Act.

Priority

34 Even if an equitable lien was available, on the facts of this case, it would not have priority over the Mortgage.

35 Section 93(3) of the *Land Titles Act*, R.S.O. 1990, c. L5 ("LTA") provides that when registered, a charge/mortgage takes priority over all unregistered interests in the land. An equitable lien is an unregistered interest.

36 If the equitable lien arises as of the date of the court order, the Mortgage has priority, having been registered long before. Even if the equitable lien attaches as of the date of the arrears, I agree with Wilton-Siegel J. in *Romspen*

Investment Corp. v. Woods Property Development Inc., 2011 ONSC 3648 (Ont. S.C.J.) at para. 185 (reversed on other grounds, 2011 ONCA 817 (Ont. C.A.)) that there is nothing in the language of s. 93(3) that permits an unregistered equitable lien to override its provisions.

37 Further, and even if the doctrine of actual notice applies, the record establishes and I so find that Trez/ Computershare did not have actual notice of MTCC 1037's equitable lien for common expense arrears. In my view, the record doesn't even establish constructive notice.

38 As noted, prior to advancing the Loan, Trez did extensive due diligence, both by itself and through its lawyers. It had a prior business relationship with the Waltons and Rose and Thistle and had no basis to believe that there were any problems or issues in respect of them, Wynford and MTCC 1037. The Waltons were involved in running a substantial successful real estate business at the time. Further, the fact that the Waltons were in control of Wynford and on MTCC 1037's Board was not unusual or cause for suspicion. They were just two of five directors and given the units that Wynford owned, it was not unusual that the Waltons would be on the Board and hold positions as officers of MTCC 1037. Finally, Trez received both the Status Certificates and the Statutory Declaration, which expressly stated that Wynford was not in default of its common expense fees.

39 Both MTCC 1037 and Trez filed affidavits from condominium experts addressing the issue of Trez's due diligence and, in particular, the effect of the Status Certificates. MTCC 1037 retained Ms. Denise Lash, Chair of the Condominium Corporation Group at Aird & Berlis LLP. Trez retained Ms. Audrey Loeb, head of the Miller Thompson LLP's Condominium Practice Group. Both lawyers are well qualified based on experience to testify in respect of status certificates.

40 Relying on s. 76 of the Act, Ms. Loeb states it is her opinion that it was reasonable for Trez and its counsel to rely on the Status Certificates and that they contained no representations which would raise suspicions on the part of counsel or Trez that would shift the onus to them to "look behind" the Status Certificates.

41 Ms. Lash on the other hand states that there were several issues or potential issues, including significant breaches of the Act, which were clear on the face of the Status Certificates which should have alerted Trez and its counsel to potential issues with the information contained therein and given rise to further inquiry. In particular, Ms. Lash points to the non-arm's length relationships of the Walton to MTCC 1037 and Wynford; the failure to include a reserve fund balance in the Status Certificates within the time period prescribed by s. 76(1)(m)(ii) of the Act; and the failure to include current audited financial statements for MTCC 1037 with the Status Certificates as prescribed by s. 76(2)(i) of the Act.

42 The Act contains detailed provisions to provide information to purchasers and mortgagees of both newly-built condominium units and re-sale units. For re-sale units, s. 76 of the Act provides for status certificates. Section 76(1) provides that the status certificate, which is a prescribed form, must contain a variety of organizational and financial information about both the unit and the corporation as a whole. In particular, s. 76(1)(i) requires a copy of the budget of the corporation for the fiscal year, the last annual audited financial statements and the auditors' report on the statements and s. 76(1)(m)(ii) requires the amount of the reserve fund no earlier than at the end of a month within 90 days of the date of the certificate.

43 Section 76(6) provides:

> The status certificate binds the corporation, as of the date it is given or deemed to be given, with respect to the information that it contains or is deemed to contain, as against a purchaser or mortgagee of a unit who relies on the certificate.

44 In the present case, the Status Certificates specified an amount of the reserve fund as at December 31, 2010, a date some two years before the Status Certificates were issued. Further, the financial statements attached to the Status Certificates were for the year ending December 31, 2010. Ms. Lash states that because these documents were not in

accordance with the Act's requirements for condominium corporations, that it should have raised red flags for Trez and its counsel requiring further inquiry.

45 The issue here is the arrears of common element expense fees. The Status Certificates clearly stated there were no arrears of common element expense fees. Trez and its counsel were entitled to rely on that statement.

46 In my view, the documents provided by the Act to be appended to the status certificate are provided for information purposes only. Section 76(4) of the Act provides that if the status certificate omits material information that it is required to contain, it shall be deemed to include a statement that there is no such information.

47 I do not accept Ms. Lash's evidence that a purchaser is required to go behind the status certificate where the information provided is incomplete or missing and inquire further. The Act is clear that a purchaser or mortgagee is entitled to rely on the information contained in the status certificate.

48 I agree with Ms. Loeb's statement at paragraph 16 of her February 20, 2015 affidavit where she states:

> 16. If the recipient of a status certificate were given the onus of confirming the statements by the condominium corporation by cross-referencing and analyzing the corporation's documents, then the very purpose of the status certificate would be severely diluted. Few, if any, purchasers or mortgagees would take any comfort in the status certificate if they knew that, at some point in the future, they may be held to account for their efforts to cross-check and verify the corporation's representations.

49 In my view, for the reasons stated, I am satisfied that Trez and its lawyers carried out satisfactory due diligence in respect of the Loan. There was nothing in the Status Certificates that should have raised any concerns about MTCC 1037 or its financial situation and in particular Wynford's common expense fees. Trez was entitled to rely on the Status Certificates and particularly the explicit representation that Wynford had no common expense arrears.

50 For the above reasons, I do not consider that MTCC 1037's criticisms of Trez's due diligence are well founded. As between Trez and MTCC 1037, it is the latter, in my view, that was in the better position to have discovered Wynford and the Walton's failure to pay common element fees. It is no answer to say that the minority directors were kept in the dark. As Board members they had a duty to "exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances" (the Act, s. 37(1)(b)). They should not have acceded full control of the Board to the Waltons. Nor should they or the unit holders have acquiesced in the failure to provide up to date financial statements.

Revival of the s. 85 Lien

51 MTCC 1037 seeks, in the alternative, to revive its lien rights under ss. 85 and 86 of the Act pursuant to s. 134 of the Act.

52 Section 134 of the Act provides that an interested party (including a condominium corporation) may make an application to the Superior Court for an order enforcing compliance with, among other things, the Act, a declaration or by-law. Section 134(3) gives the court wide remedial powers including granting relief that is "fair and equitable in the circumstances."

53 In *Sefco*, the Court of Appeal considered the issue of whether a condominium corporation's s. 85 lien rights could be revived pursuant to s. 134 of the Act. The Court held that the s. 85 lien rights could not be revived because to do so was inconsistent with the purpose of the Act and the intention of the legislature.

54 MTCC 1037 submits that *Sefco* can be distinguished on the basis that there was no allegation in that case of fraud, negligence and bad faith. In my view, the presence of fraud, negligence and bad faith is immaterial. Regardless of how the arrears arose, the revival of the lien would clearly upset the balance provided in the Act. Specifically, in this case it would deprive Trez/Computershare of proper and timely notice to enable it to consider all its options.

Conclusion

55 For the above reasons, therefore, MTCC 1037's motion for priority over the Mortgage is dismissed. An order shall issue authorizing the Receiver to pay the monies held in trust pursuant to the Order to Trez/Computershare based on their priority.

56 MTCC 1037 submitted that the issues in the case were novel and that there should be no award of costs. I disagree. Having regard to the decision in *Sefco*, I do not consider that the issues can be characterized as novel. Trez/Computershare was successful on the motion and are entitled to their costs on a partial indemnity scale. Both parties have provided Cost Outlines.

57 Trez/Computershare seeks costs totaling $66,215.58, made up of fees of $42,131.50, disbursements of $16,466.35 and HST. MTCC 1037 seeks costs totaling $28,595.37 made up of fees of $16.149, disbursements of $9,171.50 and HST. Both parties' disbursements were higher than usual due to the expert reports both sides retained.

58 Upon the exchange of Cost Outlines, counsel for Trez/Computershare conceded that his fee was high and submitted that the fee should be the difference between the fee amount claimed by both parties but that the disbursements should remain the same for each party. Counsel for MTCC 1037 had no issue with that position.

59 Having regard to the issues raised and the work done, I am satisfied that a fee of $29,140.25 (the midpoint between the two fees claimed) is fair and reasonable. I am also of the view that the disbursements claimed by Trez/Computershare are also reasonable. Ms. Loeb's fee is somewhat higher than Ms. Lash's but given the reports, I do not consider that to be unreasonable.

60 Accordingly, Trez/Computershare's costs are fixed at $51,535.23 inclusive of disbursements and taxes.

Motion dismissed.

Footnotes

* A corrigendum issued by the court on January 5, 2016 has been incorporated herein.

TAB 8

2012 ONSC 1498
Ontario Superior Court of Justice

R. v. Sankar

2012 CarswellOnt 4183, 2012 ONSC 1498, [2012] O.J. No. 1559, 101 W.C.B. (2d) 64, 21 R.P.R. (5th) 76

Her Majesty the Queen, Applicant and Derek Sankar, Respondent and SNC-Lavalin Profac Inc., A person claiming an interest in property and Picard Foods Ltd., A person claiming an interest in property

Durno J.

Judgment: March 13, 2012 *
Docket: 2144/07

Proceedings: additional reasons at *R. v. Sankar* (2012), 2012 CarswellOnt 8087, 2012 ONSC 3430, [2012] O.J. No. 2920 (Ont. S.C.J.); additional reasons at *R. v. Sankar* (2012), 2012 CarswellOnt 8074, [2012] O.J. No. 2919, 2012 ONSC 3621 (Ont. S.C.J.)

Counsel: Aimee Gauthier, for Applicant / Crown
Derek Sankar, for himself
Kathryn J. Manning, Erin Hoult, for SNC-Lavalin Profac Inc.
Mervin L. Riddell, for Picard Foods Ltd.

Subject: Criminal; Contracts; Corporate and Commercial; Property
Related Abridgment Classifications
Criminal law
XVIII Proceeds of crime
XVIII.1 Laundering proceeds of crime
Headnote
Criminal law --- Sentencing — Types of sentence — Forfeiture
Rights of innocent secured creditor — Where Crown seeks forfeiture in favour of victim — Subsequent to commission of certain offences by accused but prior to their discovery by victim, corporation M controlled by accused's spouse and funded inter alia by proceeds of commission of offences entered into realty development contract with non-party P — Contract was not performed and P brought action for damages as against M in breach of contract — Debt of M to P allegedly exceeded $200,000 — Breach of contract action was settled inter alia by M giving P mortgage on certain real property, in face value of $110,000 — Accused subsequently pleaded guilty to and was convicted of fraud and laundering proceeds of crime — With intent to compensate victim of offences charged, Crown sought forfeiture of certain funds held in court and in solicitor's trust account as component of sentence pursuant to s. 462.41 of Criminal Code — Non-party P brought application for declaration of priority and payment out to P in course of forfeiture proceedings — Application granted in part — First step in present proceeding was determination that subject property was offence-related or obtained by crime, and Crown established that in present case — Party seeking priority over Crown forfeiture in s. 462.41 Code proceedings must, after proving bona fides of interest in subject property, "establish . . . that it is appropriate for his or her interest to take priority over the forfeiture order" — This imports discretion, so that finding of debt due and owing from accused does not automatically result in order of priority in favour of creditor — In present case, funds secured by mortgage following settlement of breach of contract action were clearly component of offence-related property, and P established that it was not on notice of any criminal acts of M, spouse as its principal or accused — Accordingly, P, to extent of its secured status only and not to full indebtedness of M to P, was entitled to priority —

Security was limited to face value of mortgage as registered, together with interest and payments on certain municipal services owed pursuant to registered instrument — Remainder of funds, including trust funds, were ordered forfeited to Crown — Victim was entitled to restitution order in amount of $2,800,000.

Table of Authorities

Cases considered by *Durno J.*:

Bank of Montreal v. Smith (2008), 2008 CarswellOnt 3473, 71 R.P.R. (4th) 52 (Ont. S.C.J.) — followed

Bascello v. Bascello (Trustee of) (1997), 48 C.B.R. (3d) 235, 33 O.R. (3d) 30, 146 D.L.R. (4th) 289, 1997 CarswellOnt 892, (sub nom. *Bascello v. Bascello (Bankrupt)*) 31 O.T.C. 14 (Ont. Gen. Div.) — referred to

Canadian Imperial Bank of Commerce v. Rockway Holdings Ltd. (1996), 1996 CarswellOnt 2526, 29 O.R. (3d) 350, 3 R.P.R. (3d) 174, 5 O.T.C. 69 (Ont. Gen. Div.) — considered

Durrani v. Augier (2000), 190 D.L.R. (4th) 183, [2000] O.T.C. 607, 36 R.P.R. (3d) 261, 50 O.R. (3d) 353, 2000 CarswellOnt 2807 (Ont. S.C.J.) — referred to

Lynch v. Segal (2005), 2005 CarswellOnt 8735 (Ont. C.A.) — distinguished

Peterkin v. McFarlane (1885), 13 S.C.R. 677, 1885 CarswellOnt 22 (S.C.C.) — considered

R. v. Briscoe (2010), 483 W.A.C. 86, 477 A.R. 86, 2010 CarswellAlta 589, 400 N.R. 216, 22 Alta. L.R. (5th) 49, [2010] 1 S.C.R. 411, 210 C.R.R. (2d) 150, [2010] 6 W.W.R. 1, 316 D.L.R. (4th) 577, 73 C.R. (6th) 224, 253 C.C.C. (3d) 140, 2010 CarswellAlta 588, 2010 SCC 13 (S.C.C.) — referred to

R. v. Connolly (2007), 2007 NLCA 5, 2007 CarswellNfld 16, (sub nom. *Connolly v. R.*) 262 Nfld. & P.E.I.R. 281, (sub nom. *Connolly v. R.*) 794 A.P.R. 281, 216 C.C.C. (3d) 306, 35 R.F.L. (6th) 29, 275 D.L.R. (4th) 609 (N.L. C.A.) — referred to

R. v. Gagnon (1992), 133 A.R. 348, 1992 CarswellAlta 532 (Alta. Q.B.) — considered

R. v. Klymchuk (2008), 2008 ONCA 854, 2008 CarswellOnt 7624, 244 O.A.C. 208 (Ont. C.A. [In Chambers]) — considered

R. c. Lavigne (2006), 2006 SCC 10, 2006 CarswellQue 2524, 2006 CarswellQue 2525, (sub nom. *R. v. Lavigne*) 206 C.C.C. (3d) 449, 264 D.L.R. (4th) 385, 36 C.R. (6th) 55, (sub nom. *R. v. Lavigne*) 346 N.R. 160, [2006] 1 S.C.R. 392 (S.C.C.) — considered

R. v. Malfara (2006), 211 O.A.C. 200, 2006 CarswellOnt 3164 (Ont. C.A.) — referred to

R. v. Paszczenko (2010), 81 C.R. (6th) 97, 2010 CarswellOnt 6968, 2010 ONCA 615, 272 O.A.C. 27, 100 M.V.R. (5th) 1, 103 O.R. (3d) 424 (Ont. C.A.) — considered

R. v. Poirier (December 20, 1996), Savoie Prov. Ct. J. (N.B. Prov. Ct.) — considered

R. v. Sankar (2010), 270 C.C.C. (3d) 410, 2010 ONSC 6967, 2010 CarswellOnt 9913 (Ont. S.C.J.) — referred to

R. v. Sansregret (1985), 1985 CarswellMan 176, (sub nom. *Sansregret v. R.*) [1985] 1 S.C.R. 570, (sub nom. *Sansregret v. R.*) 58 N.R. 123, (sub nom. *Sansregret v. R.*) 45 C.R. (3d) 193, (sub nom. *Sansregret v. R.*) 17 D.L.R. (4th) 577, (sub nom. *Sansregret v. R.*) [1985] 3 W.W.R. 701, (sub nom. *Sansregret v. R.*) 35 Man. R. (2d) 1, (sub nom. *Sansregret v. R.*) 18 C.C.C. (3d) 223, 1985 CarswellMan 380 (S.C.C.) — referred to

R. c. Transfert Express inc. (2007), (sub nom. *Antillas Communication inc. v. La Reine*) 232 C.C.C. (3d) 553, 2007 CarswellQue 11640, 2007 QCCA 1719 (Que. C.A.) — considered

R. v. Wilson (1993), 1993 CarswellOnt 129, 25 C.R. (4th) 239, (sub nom. *Wilson v. R.*) 15 O.R. (3d) 645, (sub nom. *Wilson v. Canada*) 86 C.C.C. (3d) 464, (sub nom. *Wilson v. R.*) 66 O.A.C. 219 (Ont. C.A.) — considered

R. v. 1431633 Ontario Inc. (2010), 92 C.L.R. (3d) 263, 2010 ONSC 266, 2010 CarswellOnt 161, 250 C.C.C. (3d) 354 (Ont. S.C.J.) — distinguished

R.A. & J. Family Investment Corp. v. Orzech (1999), 27 R.P.R. (3d) 230, 121 O.A.C. 312, 44 O.R. (3d) 385, 1999 CarswellOnt 1829 (Ont. C.A.) — considered

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Romspen Investment Corp. v. 2126921 Ontario Inc. (2010), 2010 ONCA 854, 2010 CarswellOnt 9582 (Ont. C.A.) — distinguished

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Statutes considered:

Courts of Justice Act, R.S.O. 1990, c. C.43

s. 100 — referred to

Criminal Code, R.S.C. 1985, c. C-46

Generally — referred to

s. 462.3(1) [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — considered

s. 462.37 [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — referred to

s. 462.37(1) [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — referred to

s. 462.37(3) [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — considered

s. 462.41 [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — considered

s. 462.41(1) [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — considered

s. 462.41(3) [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — considered

s. 462.42 [en. R.S.C. 1985, c. 42 (4th Supp.), s. 2] — considered

s. 738 — referred to

Crown Attorneys Act, R.S.O. 1990, c. C.49

s. 14.6 [en. 2005, c. 33, s. 3] — referred to

Execution Act, R.S.O. 1990, c. E.24

Generally — referred to

Land Titles Act, R.S.O. 1990, c. L.5

Generally — referred to

s. 78(5) — considered

s. 93 — considered

s. 93(2) — considered

s. 93(4) — considered

Planning Act, R.S.O. 1990, c. P.13

Generally — referred to

s. 50(5)(f) — considered

s. 50(18) — considered

Regulations considered:

Land Titles Act, R.S.O. 1990, c. L.5

Transfer of Functions, R.R.O. 1990, Reg. 693

Generally — referred to

APPLICATION by alleged creditor of accused for priority order in course of forfeiture proceedings following accused's guilty plea to and conviction on charges of fraud and laundering proceeds of crime.

***Durno J.*:**

Introduction

1 Derek Sankar pleaded guilty to defrauding his employer, SNC-Lavalin ProFac Inc. (ProFac), out of 2.8 million dollars and laundering proceeds of crime. As a result of civil proceedings taken by ProFac, roughly $1M is held in court and a lawyer's trust account.

2 During the sentencing hearing the Crown applied to have the funds forfeited to the Crown. This is the third ruling on the Crown's application. The first examined procedure and onus issues. The second determined that the Agreed Statement of Facts upon which Derek Sankar's plea and sentencing were based provided an evidentiary basis upon which I could order forfeiture of the funds to the Crown, subject to any order under s. 462.41. Picard Foods Ltd. (Picard) responded to a notice to a person who appeared to have a valid interest in the property the Crown sought forfeited. Picard says they are a secured creditor and should have $248,699.05 plus interest returned to them. The Crown and ProFac say all the funds should go to ProFac.

3 This ruling examines the issues raised in relation to Picard and the forfeiture order. While a forfeiture order under s. 462.37(1) is made in favour of the Crown, pursuant to s. 14.6 of the *Crown Attorneys Act.*, R.S.O. 1990, c. C.49, the Crown is entitled to use forfeited funds to satisfy the claims of victims of crime. Ms. Gauthier advised that the Crown will provide any forfeited funds to ProFac. In these circumstances, while the Crown is bringing the forfeiture application, the contest in relation to the funds to be forfeited and the amount, if any, that should be returned to Picard is essentially between Picard and ProFac. For that reason, I will refer to the forfeited funds as going to ProFac and not the Crown.

The Law

4 On a Crown s. 462.37 forfeiture application, the onus is on the prosecution to establish on a balance of probabilities:

(1) the property is proceeds of crime; and

(2) the designated offence was committed in relation to the property the Crown seeks forfeited.

R. v. Wilson (1993), 86 C.C.C. (3d) 464 (Ont. C.A.)

5 Having found that the Crown had met its onus, s. 462.41 required the following to occur before a forfeiture order could be made:

Notice

462.41 (1) Before making an order under subsection 462.37(1) ... in relation to any property, a court shall require notice in accordance with subsection (2) to be given to and may hear any person who, in the opinion of the court, appears to have a valid interest in the property.

. . .

Order of restoration of property

Where a court is satisfied that any person, other than

(a) a person who is charged with, or was convicted of, a designated offence, or

(b) a person who acquired title to or a right of possession of that property from a person referred to in paragraph (a) under circumstances that give rise to a reasonable inference that the title or right was transferred for the purpose of avoiding the forfeiture of the property,

> is the lawful owner or is lawfully entitled to possession of any property or any part thereof that would otherwise be forfeited pursuant to subsection 462.37(1) ... and that the person appears innocent of any complicity in an offence referred to in paragraph (a) or of any collusion in relation to such an offence, the court *may* order that the property or part thereof be returned to that person.
>
> (emphasis added)

6 Accordingly, before ordering property that would have been forfeited to the Crown pursuant to s. 462.37 restored to Picard, I must be satisfied that Picard:

> (1) is the lawful owner or is lawfully entitled to possession of any property or any part thereof that would be forfeited pursuant to s. 462.37(1) ...;
>
> (2) appears innocent of any complicity in a designated offence or of any collusion in relation to such an offence;
>
> (3) is not a person charged with, or who was convicted of a designated offence; and
>
> (4) is not a person who acquired title to or a right of possession of that property from a person charged with or convicted of a designated offence under circumstances that give rise to a reasonable inference that the title or right was transferred for the purpose of avoiding the forfeiture of the property.

7 Upon being satisfied on each element, s. 462.41(3) provides that the judge *may* order the property or part thereof be returned to the person claiming an interest. Accordingly, even though the judge is satisfied of the four criteria, whether or not to grant relief from forfeiture is a matter within the court's discretion. *R. v. Wilson*, *supra*; *R. v. Connolly* (2007), 216 C.C.C. (3d) 306 (N.L. C.A.) What is required is a balancing of the relevant considerations. *Wilson*, *supra*, at p. 479. In *Wilson*, *supra*, Justice Doherty's comments in relation to a s. 462.42 application, brought after the sentencing and forfeiture has been ordered, are applicable to s. 462.41 considerations of whether otherwise forfeitable property should be returned:

> ... In exercising the discretion conferred by s. 462.42 the trial judge must decide whether the innocent third party should suffer so that the goal of divesting the offender of his or her ill-gotten gains can be achieved; or whether that goal should be tempered so as to permit vindication of the innocent third party's legitimate interest in the forfeited property.

8 Here, the contest is not between an innocent third party and the offender or the Crown and an innocent third party. Rather, it is between two innocent third parties, one the victim of the offence.

9 In *R. v. 1431633 Ontario Inc.*, 2010 ONSC 266 (Ont. S.C.J.) (*Rona*), Molloy J. held that in addition to the criteria outlined in s. 462.42 the person claiming an interest had to establish:

> 1) that he or she had a valid interest in the property that went beyond the interest of a general creditor; and
>
> 2) the nature and extent of the claim. Accordingly, the last component the person claiming an interest must establish was that it is appropriate for his or her interest to take priority over the forfeiture order.

10 I am persuaded that the same criteria apply at a s. 462.41 hearing.

The Onus on an Application pursuant to s. 462.41

11 In the first ruling [1] on this application at para. 17, I addressed the s. 462.41 onus as follows:

> Once the applicable sections are identified, the onus and burden issues are governed by those sections - s. 462.37 and s. 462.41. The onus is on the Crown on the balance of probabilities to establish 1) the property is proceeds of crime,

> and 2) the designated offence was committed in relation to that property. There is no onus on those claiming an interest. At the end of the evidence, if any, and submissions, the question is whether the Crown has met their onus.

12 Those findings are consistent with *R. v. Gagnon*, [1992] A.J. No. 842 (Alta. Q.B.) where Veit J. found, "Since the Crown brings the motion in which the issue of return of property arises under s. 462.41, the Crown presumably bears the onus in motions under that section." However, in the course of preparing this ruling the Quebec Court of Appeal judgment in *R. c. Transfert Express inc.* (2007), 232 C.C.C. (3d) 553 (Que. C.A.) [hereinafter *Antillas*] came to my attention, at para. 31 the Court held that the onus was on the person claiming an interest.

13 Having regard to *Antillas*, *supra*, the unfolding of the issues as this application has proceeded and the additional cases filed on the hearing, the conclusion I reached regarding the onus in that first ruling requires re-examination.

14 The onus is on the Crown under s. 462.37 on a balance of probabilities. For the purpose of this analysis, there are two routes by which a person with an interest in the property to be forfeited can seek to have their property returned. First, during the sentencing hearing by responding to a notice under s. 462.41. Second, after the sentencing hearing and the property has been ordered forfeited by bringing an application under s. 462.42. Neither route makes any reference to the onus or burden of proof.

15 All of the reported s. 462.42 judgments have held that the onus is on the person seeking relief from forfeiture on a balance of probabilities. *1431633 Ontario Inc.*, *supra*, *Connolly (2007)*, *supra*, at para. 23, and *Villeneuve v. Canada (1999)*, 140 C.C.C. (3d) 364 (Que. C.A.) at p. 574.

16 Does the same onus apply where the issue is being determined under s. 462.41 during the sentencing hearing? There are differences between the two sections. First, under s. 462.41 the person with a potential interest in the property does not bring an application for relief from forfeiture. He or she responds to a notice and may be heard in relation to the issues upon which the judge must be satisfied under s. 462.41. If the property is returned to the person claiming an interest, it is effectively removed from the proceeds of crime that is available to be forfeited to the Crown. Second, under s. 462.42, the person claiming an interest must apply. Generally, a party bringing an application has the burden of proof.

17 Notwithstanding the differences in the sections, I am persuaded that there is an onus on the party responding to a s. 462.41 notice who seeks to have property returned to them for the following reasons. First, the criteria upon which the judge must be satisfied under s. 462.41(3) are within the knowledge of the person claiming an interest. Second, it would be illogical to put the onus on the Crown in relation to the s. 462.41(3) criteria when the Crown seeks forfeiture of all the property. It would put the onus on the party who seeks to defeat the claim of the person claiming an interest. The result of the Crown satisfying the court of the criteria would be to diminish or eliminate completely the property the Crown sought forfeited.

18 While during submissions, I had referred to the onus being either a burden of proof or a "practical evidentiary burden" (*R. v. Paszczenko*, 2010 ONCA 615 (Ont. C.A.)), I am persuaded that there must be a burden on the person responding to a notice to satisfy the court of the four criteria. An evidentiary burden has been described as follows in Sopinka, Lederman and Bryant, *The Law of Evidence in Canada* (Toronto: Buttersworth, 1999) where the authors state, at p. 56:

> The term "evidential burden" means that a party has the responsibility to insure that there is sufficient evidence of the existence or non-existence of a fact or of an issue on the record to pass the threshold test for that particular fact or issue.

19 Imposing only an evidentiary burden does not meet the requirements of s. 462.41, that the judge be "satisfied." That is different than there being evidence to pass a threshold test. With the person claiming an interest seeking the return of his or her property, it is appropriate to impose a civil standard burden of proof on that person.

20 The final onus issue is whether there is an onus to be applied when the s. 462.41(3) "criteria" are met and the judge has to determine whether to exercise his or her discretion. While all counsel agree that it would be the balance of probabilities standard, they differ as to where the onus lies. Mr. Riddell alone submits the onus is on the Crown. The Crown submits that practically it may not make a great deal of difference because the final determination involves the exercise of discretion. ProFac submits the onus is on the person claiming an interest, here Picard.

21 I agree with Ms. Gauthier. If the s. 462.41(3) criteria are established, in determining whether to exercise my discretion, the decision is made on the basis of the equities of the situation. When the decision is based on the equities it is not necessary to assign a burden of proof.

22 In summary,

1. The first step in a Crown's forfeiture application is the Crown establishing the criteria for forfeiture under s. 462.37 on a balance of probabilities.

2. If the Crown meets its onus, notice is given to person(s) who appear to have an interest in the property. If anyone responds to the notice seeking the return of property, the judge may hear them and determine whether the disputed property should be returned to the person with an interest. At this stage there is an onus on the person claiming an interest to establish the criteria noted in s. 462.41 on a balance of probabilities.

3. If the person claiming an interest satisfies the judge with regard to the criteria, the judge has a discretion whether to return the property. In exercising his or her discretion, the sentencing judge must consider all the circumstances and determine whether all, part or none of the property should be returned considering the equities of the situation.

4. Where the judge orders property returned, the remainder of the property, if any, is forfeited to the Crown pursuant to s. 462.37(1).

The Parties

23 *Derek Sankar* was employed by ProFac between November, 1999 and February 26, 2004 as a regional facilities manager for seventeen sites. He was married to *Audrey Holder-Sankar*. By his guilty plea to defrauding ProFac, he admitted that the illegally obtained funds went to Massdan and was used to buy property including 457 and 561 Dundas St. E.

24 *Massdan* was incorporated August 25, 2003, with Audrey Holder-Sankar as the president, secretary and treasurer. Derek Sankar and Audrey Holder-Sankar were the only directors. As of October 20, 2005 Derek Sankar was noted as an "inactive administrator."

25 *Picard* is a corporation incorporated under the laws of Ontario with its head office in Waterford, Ontario. *John Picard* is the President of the family run business that employs roughly 24 people and operates eight retail outlets across Ontario. At the time of their development on Dundas St. E., Hamilton, Picard had four other outlets.

26 While other parties were notified of the forfeiture application, only Audrey Holder-Sankar appeared by counsel for the preliminary rulings. She has withdrawn from the application before the Picard evidence and submissions. While she filed an affidavit on this application, as she has withdrawn and was never cross-examined on the affidavit, it plays no part in the application. In addition, while some of the evidence was based on what Ms. Holder-Sankar told other persons, she was not called as a witness.

The Properties

27 The properties in issue are on the northeast corner of Dundas St. E. and Pamela St. in Hamilton with municipal addresses of 447, 453, 457 and 561 Dundas St. E. While at various times in the evidence and documents the properties

were referred to as being in Hamilton, Waterdown or Flamborough, it is all the same property and will be referred to throughout as in Hamilton.

28 The Property Identification Numbers (PIN) associated with each address are: 447 Dundas St. E. — PIN 17503-00330, 453 Dundas St. E. - PIN 17503-00331, 457 Dundas St. E. - PIN 17503-00332 and PIN 17503-0033 and 561 Dundas St. E. - PIN 17503-0334. In much of the documentation and throughout the evidence the two lots that comprised 457 Dundas St. E. were referred to as Part 1 and Part 2. For ease of reference I will refer to the municipal addresses but when the distinction between the two 457 lots is relevant I will refer to them as 457-Part 1 and 457-Part 2.

29 In 2004, Massdan bought the four adjoining properties. In May, 2005, Picard bought 447 and 453 Dundas St. E. from Massdan for $650,000. Picard's retail store is on the corner lot, 447. The adjoining lot, 453, is vacant.

30 The Massdan 457 Dundas St. E. property has frontage of 150 feet comprised of 24 feet for 457-Part 2 and 126 feet for 457-Part 1. This address was the location of a proposed car wash that will be referred to throughout the reasons.

Chronology

31 Before examining the evidence on the application, it might be helpful outline the events chronologically to place the evidence in context.

1. On February 26, 2004, Derek Sankar was terminated for cause by ProFac for the use of non-approved vendors and exceeding his signing authority.

2. On March 18, 2004, Audrey Holder-Sankar purchased 453 and 447 Dundas St. E, Hamilton.

3. On March 18, 2004, Massdan purchased 457 Dundas St. E. Hamilton using funds Derek Sankar had fraudulently obtained from Profac.

4. Massdan began discussions with the municipality regarding a subdivision agreement that was required before Massdan could develop the lots, including a planned carwash. Additional municipal services would have to be installed at Massdan's expense.

5. In early 2005, Derek Sankar's illegal activities were discovered and ProFac commenced civil proceedings against numerous individuals and companies including Derek Sankar, his wife and Massdan.

6. On May 20, 2005, Picard bought 447 and 453 Dundas St. E. from Audrey Holder-Sankar with the intention of opening a retail store at that location. Picard entered discussions with the municipality to obtain site-specific zoning to permit the opening of the store.

7. On June 5, 2005, a *Mareva* injunction and an *Anton Pillar* order were granted in relation the defendants in ProFac's civil suit including Derek Sankar, Audrey Holder-Sankar, and Massdan. Twelve properties were listed in Schedule B to the order. 457-Part 2 was listed; 457-Part 1 was not. Since that date the assets of Derek Sankar, Audrey Holder-Sankar and Massdan have been frozen by virtue of the *Mareva* injunction and civil suit commenced by ProFac.

8. On June 21, 2005, a Certificate of Pending Litigation (CPL) was registered by ProFac on Massdan's lot 457-Part 2. Schedule A to the CPL appears to be the same schedule as was appended to the orders noted in #5 and included 561 Dundas St. E. There was no direct evidence on this application explaining why the CPL was not registered on 457-Part 1 at that time.

9. In early 2006, Picard finalized its discussions with the municipality regarding site-specific zoning only to be told for the first time that the city required the Massdan's subdivision agreement as part of the Picard agreement. In the result, before Picard could proceed with its development, the municipal services for the original four Massdan lots would have to be installed.

10. When inquiries were made regarding the carwash, Massdan told Picard that it was not in a position to proceed with the services at that time.

11. On May 1, 2006, discussions between Picard and Massdan led to a written agreement in which Picard was to complete and pay for all of the municipal services that the city required. The written agreement was secured by a collateral first mortgage in relation to and registered on both of Massdan's lots, 457-Part 1 and 457-Part 2. The mortgage, registered on May 29, 2006, stated the principal amount was $110,000, but also noted that it was for the entire costs of all of the municipal services. Massdan was to repay Picard for the entire costs and 10% interest.

12. Picard was aware of the CPL on the Massdan's lot 457-Part 2 and that there was nothing registered on 457-Part 1.

13. On May 28, 2006, Massdan's counsel advised Picard's counsel that John Picard was fully aware of the CPL and prepared to proceed without its removal.

14. On May 24, 2006 Picard approved the registration of the collateral first mortgage on Massdan's lots 457-Part 1 and 457-Part 2.

15. In August, 2006, Derek Sankar was arrested and charged with fraud and money laundering.

16. On June 21, 2007, Picard advised Massdan that the municipal services had been installed and provided a costs breakdown which totalled $248,699.05, including interest. This was exclusive of $11,233.92 consulting costs that Picard had absorbed. The letter required the funds to be paid by August 1, 2007. The funds were not paid.

17. On September 17, 2007, a ProFac CPL was registered on Massdan's lot 457-Part 1.

18. On November 9, 2007, Picard served Massdan with a Notice of Sale under the mortgage in relation to lots 457-Part 1 and 457-Part 2, requiring the funds be paid by December 17, 2007. The funds were never paid.

19. By Statement of Claim, dated June 24, 2008, Picard sought $248,699.05 plus interest from Massdan. The statement referred to the May 1, 2006 written agreement under which Picard was to install the municipal services for 457-Part 1 and 457-Part 2 owned by Massdan, Massdan's agreement to pay Picard the full amount with interest at the rate of 10% per annum payable on the earlier of one year from the final installation of the services or upon the building permit being issued on the Massdan lands. The statement continued, "The defendant granted security for the payment of the works by the registration of a first mortgage in the principle sum of $110,000 against Massdan lands. The mortgage and agreement were registered on title."

20. On July 23, 2008, Picard obtained a default judgment against Massdan for $268.731.25 plus $1,255.06 costs for a total of $269 986.87. Picard filed executions in relation to Massdan.

21. In 2008, when ProFac was selling 457-Part 1 and 457-Part 2, Picard agreed to discharge its charge and consent to the removal of the writ on the understanding that the proceeds from ProFac's sale of 457 and 561 Dundas St. E. be paid into court without prejudice to either ProFac's or Picard's right to argue priority of their respective claims.

22. In September, 2010 the following amounts were paid into court from the sales; 457 Dundas St. E. — $349,548.35 and 561 Dundas St. E. - $79,753.16 for a total of $429,301.51.

23. The proceeds from the sale of eight properties have been paid into court to the credit of ProFac's civil proceeding. The proceeds from the sale of two properties are held in trust by Massdan's counsel, Paul Lafluer.

The Evidence on the Application

The Picard Evidence

32 *John Picard*, the general manager of Picard, testified the company bought 447 and 453 Dundas St. E. from Massdan on May 20, 2005 for $650,000. It was Picard's intention to develop 447 and to leave 453 vacant.

33 In order to open a retail store, Picard was required to obtain site-specific zoning to permit that type of development and complete a subdivision agreement with the municipality for the installation of sewers, water mains, sidewalks, sodding and restoration to the Dundas St. E. Boulevard.

34 When Picard bought the property Massdan "was in the process" of obtaining permits and approval to build a car wash on 457 Dundas St. E. He believed Ms. Holder-Sankar's plans to start a car wash were well underway; having seen the site plan that included a new mainline sewer on Dundas St. E. In earlier discussions and in the initial offers of purchase and sale, Massdan was required to pursue and complete building the carwash, which would have included any municipal services required. However, the written agreement did not include such a commitment. John Picard said there was an oral agreement to that effect and he regarded it as a binding agreement. To Picard, "it was understood."

35 The Agreement of Purchase and Sale, dated April 22, 2005, included the following clauses in Schedule A:

> 3. Buyer is aware that subject property may or will have a temporary easement for the total site servicing including proposed car wash to the east across the property and agrees to accept this with the very possibility of this happening after the completion date and agrees to co-operate fully with the seller in achieving this.
>
> 4. Buyer agrees to pay the cost from the Picard new building to point of connection in front of his property.

36 In his August 6, 2009 affidavit, John Picard swore that at the time of the purchase "Massdan and Audrey Sankar were in negotiations with the Municipality, with respect to a Subdivision Agreement that included the requirement for a new sewer and water services to develop their properties for a proposed car wash.

37 In a November 17, 2010, affidavit, John Picard said that in May, 2005, when Picard registered its deed of purchase for 447 and 453 Dundas St. E., Picard was aware of the City of Hamilton's existing requirement that Massdan must perform certain works for its property including the installation of main-line sewers and water services, drains, connections, sidewalks, driveway approaches, sodding and restoration of the Dundas St. E. Boulevard.

38 In the same affidavit, he said Dwayne Vogel (Vogel), Massdan's Re/Max real estate agent who also acted for Picard on the transaction, showed him the car wash plans and told Picard the car wash agreement had been in development over the past three years and would be going ahead immediately and concurrently with Picard pursuing its re-zoning. Vogel requested permission for Massdan to have access over Picard's frontage on Dundas St. E. to facilitate Massdan's completion of the required work. Picard agreed on the understanding that such temporary access would occur promptly and at Massdan's expense. There was a clear commitment for Massdan to install and pay for the work. Picard had the third and fourth clauses noted above added to the agreement to facilitate Massdan's work and committing Picard to pay the cost of running the site specific services from Picard's new building to connect with the new services Massdan would be completing.

39 After the sale, Picard applied for site-specific zoning for their property which was granted about one year later, in 2006. During that year, Massdan had done no work on 457 Dundas St. E. that advanced the car wash proposal. For the first time, Picard learned that the municipality insisted the Massdan subdivision agreement be implemented before Picard could proceed with its development. The Picard zoning agreement that the city insisted upon included as Schedule "C," the Massdan agreement for improved services. Without a subdivision agreement, Picard could not proceed with its retail store at 447 Dundas St. E.

40 John Picard approached Audrey Holder-Sankar who told him Massdan could not proceed with the car wash at that time, nor could they do so any time soon. Feeling it was not his place to ask, John Picard never asked Audrey

Holder-Sankar why they were not proceeding with the car wash. At no time, did Picard make any inquiries regarding Massdan's liquidity.

41 Picard said he had had his property for one year, was "ready to go" and had to make a decision. He approached Audrey Holder-Sankar and offered to finance the required municipal services because they would both benefit from their completion. She agreed with his proposal that would include Picard taking a collateral mortgage for the total costs. While his 2009 affidavit referred to Massdan repaying Picard for Massdan's share of the costs, the final agreement was for Massdan to repay Picard the entire costs of installing the municipal services. John Picard regarded Ms. Holder-Sankar's willingness to sign the agreement as indicative of her willingness to repay Picard, noting that one year earlier, Picard paid Massdan $650,000 for the property.

42 When Picard was preparing to finalize the agreement, its lawyer, James Boll (Boll), told them there was "a cloud" on the title to the small lot. John Picard thought the CPL possibly related to an easement concern from when the property was a farm as the former owner's name, Vastes, was mentioned. His dealings were mainly with Massdan's real estate agent, Vogel. In his August 6, 2009 affidavit John Picard said Vogel previously told him that there was a title issue in relation to 457-Part 2. In cross-examination, he said that he knew there was litigation pending in relation to 457-Part 2 and that someone was claiming an interest in the smaller parcel. He had no idea it related to Massdan and never asked that further inquiries be made. He relied on his lawyer and never discussed the "cloud" with Audrey Holder-Sankar. His lawyer said that there was sufficient equity in 457-Part 1, a lot that was not encumbered and had enough value to cover the costs of the work to be completed.

43 Picard said he was unaware of any risk they were assuming. He did not recall if he was told anything about the *Planning Act*, R.S.O. 1990, c.P.13 provisions, although he believed he was told the Picard mortgage had to be on both properties.

44 The Picard-Massdan written agreement was reached on May 1, 2006 before the tendering of the contract to install the municipal services. It provided that Massdan would repay Picard "the total actual cost of the work on the earlier of one year from their final installation or the issuance of a building permit on the Massdan properties." Massdan would pay Picard interest at 10% per year, a rate agreed to by Audrey Holder-Sankar. Further, Massdan would grant Picard a collateral first mortgage for the costs in the principal amount of $110,000, but with a reference to Massdan repaying the total amount. Otherwise, the mortgage included no repayment terms. The collateral mortgage was registered against Massdan's lots 457-Part 1 and 457-Part 2 on May 29, 2006.

45 The city estimated the costs of municipal services would be $100,000 and required a deposit before the work started. The successful bid of $177,000 shocked Picard. During the construction, a boulder on Massdan's property had to be removed at an additional cost of $23,000. By the time the services were completed Picard paid about $204,000 plus "a couple of additional costs." While it was substantially above what he had expected, John Picard said they did not have a lot of choice.

46 Picard paid for all of the work including replacing the sidewalk in front of its properties. When no payments were made on the collateral mortgage after one year, on August 28, 2007, Picard e-mailed Audrey Holder-Sankar asking for "direction immediately" as otherwise he would have to arrange longer term financing if she defaulted on the previously agreed upon terms. On September 4, 2007, Ms. Holder-Sankar replied that she was going through "a litigation which is registered against the property and it also involves all of my assets." She did not expect the process to take so long although they were negotiating a settlement and her lawyer was in the process of presenting an offer. She was hopeful to have a resolution by the end of the year and confirmed her commitment to repay the loan. She added that she needed to get an understanding of how the costs had increased above the original budget.

47 On September 25, 2007, Picard again e-mailed advising the matter had become one of urgency and that Ms. Holder-Sankar must make immediate arrangements to settle the account or it would become a legal matter. Ms. Holder-Sankar replied on September 28 that she did not have the funds although a settlement in her other matter looked positive.

Whether a tentative agreement would be final would be determined the next week. If the settlement was finalized she would have to put some properties up for sale to get the funds and it would take some time for the sales to go through. She offered to meet with Picard to discuss the issue. The record is silent as to whether that meeting ever occurred.

48 On November 9, 2007, Picard sent a Notice of Sale in regards to 457-Part 1 and 457-Part 2, advising that if the funds were not paid by December 17, 2007 the property would be sold. The funds were not repaid and Picard initiated civil proceedings against Massdan. On July 23, 2008, Picard obtained a default judgment on the written agreement for $248,699.01 plus costs. ProFac was not notified of the Notice of Sale or the default judgment. John Picard testified he knew nothing of the ProFac's interest in the property at that time.

49 In the fall of 2008, a real estate agent told John Picard the Massdan property was for sale. He assumed it was pursuant to the power of sale. Upon further investigation, he learned ProFac was selling the property with a sale completion date of November, 2008. However, Picard's mortgage and a writ of seizure were registered against Massdan's property. To permit the sale to be completed, Picard agreed to discharge its mortgage and withdraw its Writ of Seizure and Sale. Picard and ProFac agreed to have the roughly $400,000 net proceeds of the sale paid into court without prejudice Picard pursuing its claim to the funds. John Picard testified the first he learned of ProFac and its judgment was when he was told he had to "sign off" to permit the sale to be completed.

50 James Boll, Picard's lawyer throughout its dealings with Massdan, testified he had been practicing real estate and commercial law for roughly 32 years. He drafted the May 1, 2006 Massdan-Picard agreement as well as the collateral security document. He regarded the primary financial obligation as the agreement, a contract. The mortgage was collateral security for the agreement's financial obligations.

51 Mr. Boll had not previously encountered a CPL. It was uncommon to find one on title. He read the CPL that named roughly 13 persons and 14 companies as defendants, gave notice of a claim of interest in respect of 16 properties, including Massdan's 457-Part 2 and 561 Dundas St. E., and provided contact information for ProFac and their lawyers at Blakes. Mr. Boll did not believe he had shown the CPL to John Picard or asked if he wanted ProFac or Blakes contacted. He probably told Mr. Picard the nature of the CPL and its implications.

52 Section 50(18) of the *Planning Act* provides that no foreclosure or exercise of a power of sale in a mortgage shall have any effect in law without government approval, unless all of the land subject to such mortgage is included in the foreclosure or power of sale. If one owner owned adjacent properties they could not deal with them separately. Here, the mortgage was registered on 457-Parts 1 and 2. However, on 457-Part 2 the CPL was registered before the mortgage so the mortgage was subject to the CPL. Without government approval Picard could not sell 457-Part 1 alone. Accordingly, 457-Part 2, upon which the CPL was registered, had a bearing on what could be done with the 457-Part 1.

53 Mr. Boll did not believe the security was invalid because of the *Planning Act* because they registered the charge on both properties. Lot 457-1 was a valuable piece of unencumbered land. He believed Picard had a valid charge although to enforce the mortgage Picard would have had to sell both lots when 457-Part 2 was subject to the CPL.

54 By a fax dated May 18, 2006, Mr. Boll sent the following message to Massdan's counsel, Paul Lafleur:

> We confirm that we have messaged the draft Mortgage to you for registration. We have enclosed the Application and you should confirm with your client that there is a cloud on title to the subject lands. Perhaps this Application needs to be removed from against your client's lands. Please discuss this matter with your client and advise.

55 The fax transmission sheet contains the following handwritten notation, likely based on something John Picard told Mr. Boll, "some sort of right of way issue."

56 A May 23, 2009 letter from Paul Lafleur to Boll addressed the "cloud on title" as follows:

I have been advised by my client that your client is fully aware of the registration of this Application for Certificate of Pending Litigation and your client is willing to close this transaction subject to this litigation.

57 On May 24, 2009, Picard gave Boll approval to "just proceed ASAP" knowing the mortgage was subject to the CPL on 457-Part 2. There was pressure as Picard was extremely anxious to move forward with their project because of the one year delay in getting site-specific zoning approval. Haste and urgency were Picard's priorities as he wanted to open his business and have his interests secured. It was a very pressured situation. Mr. Boll said they needed to move forward and "didn't have the luxury of time to make all those investigations." There was no need to investigate further because they had good quality security on lot 457-Part 1.

58 On November 9, 2007, Boll sent a letter to Paul Lafleur enclosing the Notice of Sale for 457 Dundas St. E. because $257,013.05 was owing. It was shortly after that that John Picard notified him the property was for sale.

59 *John Towle* (Towle), an engineer originally employed by Massdan and later by Picard, testified he negotiated with the City of Hamilton for a site plan for the four lots purchased by Massdan in 2004. That site plan was never completed. When Picard bought 447 and 453 Dundas St. E., Mr. Towle worked for Picard who later entered into a servicing agreement with the municipality. The work involved municipal service connections to the street line only, none of the work involved the installation of services on private property. The private site services to 447 Dundas St. E. were part of a separate job and were not included in the project costs.

60 Following a standard tendering process, the contract was awarded to Howlett Development and Construction Services Limited on their $177,300 plus G.S.T. bid. While the municipality also prepares an estimate, it does not equate with the actual cost because it is for security purposes only. The actual costs of the project was $204,681.86 plus G.S.T. Mr. Towle agreed that the work benefited both Picard and Massdan. While completing the work, additional costs of $27,381.86 were incurred, largely as a result of encountering the boulder. He later testified that the cost of removing the boulder was $12,000.

61 When a project is substantially completed the municipality issues certificates and then the services are connected. The last certificate was issued April 19, 2010, and was "more or less" the completion date.

62 Mr. Towle was asked by Mr. Riddell about apportioning costs between lot owners. Since Mr. Towle was initially dealing with all three municipal locations, there was no need for apportioning. He did not comment on Mr. Cameracci's opinion that apportioning was standard cost-sharing.

The ProFac Evidence

63 *Angelo Cameracci*, a professional engineer, was retained by ProFac to determine what "services, works, improvements, changes, etc., were made to the Massdan property and the Picard properties, what portion of the municipal services related to the Massdan and Picard properties, and what would be the reasonable costs of the work done to the Massdan property at the time it was done. He testified about the costs of the municipal services that were installed by Picard. His affidavit is exhibit 14.

64 The total actual construction costs, not including taxes and soft costs[2] was $204,681.86 based on the Certificate of Payment No. 3 for the period ending March 15, 2007. All appurtenances and restoration required with the sanitary sewer, water main and sidewalk installation appeared to be included in the certificate. He noted that some of the improvements benefit only one party. For example, the sidewalk and boulevard sodding benefit Picard only as does the private sanitary and water main services to its property. The 55 mm water main service only benefited Massdan's property.

65 In estimating the costs of the municipal services installed, Mr. Cameracci based his calculations on engineering drawings, the Certificate of Payments prepared by John Towle Associates Limited and estimated the quantities and materials provided for the Picard and Massdan properties. Using comparable unit prices received by his office from

three projects tendered in 2006 and 2007, he assigned tendered unit prices to the subject list of estimated quantities and materials. He concluded the total cost would be $157,074.71 with $117,752.10 apportioned to Picard's property and $39,652.40 to Massdan's applying a standard cost-sharing method.

66 The standard industry method of cost sharing employed by developers, consultants and municipalities involved apportioning the cost of the improvements based on the property frontage. The Hamilton "Development Engineering Guidelines and Financial Policy for Development" outlines various city policies including "Cost Sharing for Frontage." Applying this approach he concluded that for the sanitary sewers Picard had 75.2% of the frontage and Massdan 24.8% and for the water mains, Picard had 61.2% and Massdan 38.8%. Each would pay their proportionate share of the particular expense.

67 His affidavit included that in his experience cost sharing is always a consideration in any development as developers incur,

> . . .
>
> costs for services and are prudent in ensuring any improvement benefitting another property or development is collected either at the time the service is established or at some future point in time when the benefitting party requires the service.
>
> Developers want to ensure that they maximize their profit by paying the least amount for their servicing improvements and collecting all costs that benefit other parties from the same servicing improvement.

68 The municipal services were of three types: sanitary sewers, water main lines and roadwork comprised of sidewalks and re-sodding. The sanitary sewer ran along Pamella Street, the western border of 447 Dundas St. E., and in front of the three Dundas St. E. properties, 447, 453 and 457. Three private sanitary service lines ran from the main line to each of the properties, two to Picard's at 447 and 453 Dundas St. E. and one to Massdan's at 457 Dundas St. E. The costs for the Pamela Street segment were higher because the line ran under the roadway while on Dundas St. E. it ran under the boulevard.

69 Dundas St. E. had an existing 300 mm. water main that stopped approximately 12 m. west of Pamela St. The additional services took that water main along the front of the three properties to the western edge of 457 Dundas St. E. As was the case with the sanitary service, each property had a private water service, one for each of Picard's lots and one for Massdan's. The two Picard private lines were standard. In part, the municipal services installed were required for a car wash. The Massdan line was "oversized" (50 mm) to accommodate the proposed car wash. In his apportionment of the costs, he attributed 100% of the costs of the oversized line to Massdan.

70 The sidewalks were estimated to be 1.5 m. wide and run for 133 m. in front of all three properties. However, the "as built" was less than the estimate so that there was no new sidewalk put in front of the Massdan property at 457.

71 Mr. Cameracci testified that after the installation of the municipal services the "serviced lots" would have an increased value.

72 Neither the Crown nor Mr. Sankar called any evidence.

The Positions of the Parties

73 Derek Sankar takes no position in relation to the application. The Crown submits ProFac should receive all the funds. Picard submits it should receive what is owing to them based on their default judgment, plus interest.

74 *Picard* submits that it is a secured creditor on two bases: first, their mortgage was registered on both 457 lots and, second, the execution that was filed in relation to Massdan and its Ontario properties.

75 Mr. Riddell argues Picard did not receive actual notice regarding the details of the CPL and that constructive notice is not recognized under the *Land Titles Act*, R.R.O. 1990, Reg. 693. He submits that ProFac is conducting a collateral attack on Picard's 2009 default judgment and that "if the paper fails" Picard has a constructive trust remedy. Finally, in examining the equities between Picard and ProFac he contends the equities favour Picard who put "good money" into improving the lots and should be entitled to get "good money" back.

76 As to whether Picard received actual notice, Mr. Riddell notes the case involves *Land Titles* so Picard was entitled to rely on the register that showed the largest lot, 457-Part 1, was clear. ProFac's suggestion that Picard should have gone to the court office to make inquiries about the CPL has no merit because the file was sealed so they would have no further information.

77 ProFac, Mr. Riddell submits, had no recourse because they did not register the CPL on 457-Part 1. As regards 457-Part 2, Picard clearly has priority as the CPL was not registered on that parcel until after their mortgage was registered.

78 Picard argues that ProFac's attempt to characterize its failure to register the CPL on 457-Part 1 as an "irregularity" is not based on any evidence. In the absence of any evidence that ProFac intended to register the CPL on both properties, the record is open to the inference that ProFac intended to register the CPL on one parcel only and did so at their own peril.

79 As regards the alleged collateral attack on Picard's default judgment, Mr. Riddell argues ProFac should have moved to set the judgment aside instead of indirectly attacking it in the course of the Crown's application.

80 Picard's arguments related to a constructive trust remedy is outlined in Mr. Riddell's October 8, 2010 letter to Ms. Gauthier. He described Picard's position as claiming priority over the ProFac claims in equity by virtue of Picard's equitable rights, including equitable set-off and equitable lien. Picard gave valuable consideration, in good faith and made lasting, necessary improvements that ProFac, as owner in equity, would have made pursuant to the City's requirements. Picard made the property marketable and should be entitled to equitable claims, including an equitable lien or equitable set-off for the full value of the improvements to the property from the proceeds of sale.

81 Mr. Riddell also argues that it was implicit in the Picard-Massdan written agreement that Massdan would go forward with their car wash plans when the agreement was signed, although it is not specified in the agreement. While Massdan did not go ahead with the car wash, Picard argues the equitable obligation existed before the CPL was registered so as to give Picard priority to the CPL.

82 Further, Mr. Riddell submits that as regards the equities between ProFac and Picard, that Picard clearly has priority. While ProFac is pursuing an equitable claim, Picard also has an equitable claim and one that has priority. If the "paper" fails, Picard has an equitable mortgage or an equitable lien. The equity involves Picard's "clean money," the value received by the land and the equitable charge on the land for the amount expended, regardless of the *Land Titles Act*. Picard was simply Massdan's neighbour, is an innocent third party to the Sankar fraud who had nothing to do with the crime. John Picard is an honest businessman who had no idea he was dealing with property obtained by fraud, not the sort of person the "net of forfeiture" was intended to catch. To permit ProFac to prevail would be to permit Derek Sankar to benefit from his deceit by reducing the funds he owes ProFac.

83 Mr. Riddell argues his client was in a crisis situation as his development of his retail store was thwarted by the municipality's insistence on compliance with the Massdan subdivision agreement. John Picard made a commercial decision with legal advice in deciding to proceed on the basis of the clear title to 457-Part 1. In effect, he would worry about enforcement later. For ProFac to suggest that Picard can still go after Massdan when ProFac has seized all Massdan's assets is to suggest an exercise in futility. A windfall would occur if ProFac received the benefit of two serviced lots to sell without having to repay Picard. Forfeiture proceedings, he argues, should not create more victims.

84 Finally, Mr. Riddell submits that if the proceeds of the sale of 457 Dundas St. E. are insufficient to cover Picard's judgment, that as a judgment creditor with a filed execution, Picard is entitled to payment from funds obtained from other Massdan properties, in particular the sale of 561 Dundas St.

85 *ProFac* submits the issue is the equities between two innocent parties. When examined they lie vastly in ProFac's favour. Sankar stole $2.8 million with only roughly $1 million available in court and in Mr. Lafleur's trust account. The victim of Sankar's fraud is ProFac, the party the forfeiture provisions are intended to protect.

86 Further, Picard has not met their onus under s. 462.41 because Picard has not established it is the lawful owner or lawfully entitled to possession of any portion of the funds in issue. If I were to find Picard is a lawful owner or entitled to possession, ProFac submits I should still not exercise my discretion and return the full amount claimed to Picard.

87 In response to Picard's claim as a secured creditor through their collateral security mortgage with priority, ProFac advances three arguments: First, Picard had actual notice of ProFac's claim, the effect of the CPL, and the *Planning Act* requirements. Second, in response to Picard's claim of entitlement to an equitable lien or set-off for the full value of the municipal services, Picard had actual notice of ProFac's claim and seeks to "exploit a registration irregularity for its own gain." Third, ProFac submits the onus is on Picard to demonstrate it did not have actual notice relying on *R. v. Klymchuk*, 2008 ONCA 854 (Ont. C.A. [In Chambers]) at para. 10.

88 ProFac submits Picard paid for the municipal services without any reasonable expectation of compensation from Massdan. In relation to Picard's claim as a judgment creditor with an execution filed being entitled to payment from funds obtained from other Massdan properties if the proceeds of the 457 sale are insufficient, ProFac argues that judgment creditors are ordinary creditors and consistent with the *Criminal Code* forfeiture provisions are not entitled to relief from forfeiture.

89 The CPL, it is submitted, gave ProFac priority over Picard's claim in relation to both 457-Part 1 and 457-Part 2. Picard had enough information that they should have "asked the right questions." They chose not to do so at their own risk. Their own counsel admitted there was a risk with regards to the enforceability of the mortgage. ProFac suggests I should be skeptical about John Picard's evidence given the inconsistencies between his three affidavits noted earlier in these reasons.

90 ProFac notes that Chapnick J. found that part of the Sankars' contempt was the agreement between Picard and Massdan, encumbrancing the property to ProFac's potential detriment. This is the agreement upon which Picard's claim is based.

91 In relation to the *Planning Act*, ProFac argues that Massdan had two lots that could not be dealt with separately. That is why Picard registered its mortgage on both properties. If the funds are not returned to Picard, they still has a valid judgment against Massdan that Picard can enforce.

92 ProFac argues they have gone to great expense to pursue the funds fraudulently taken from them including obtaining *Anton Pillar* orders, *Mareva* Injunctions and assisting the prosecution in the criminal proceedings against Mr. Sankar. It is Picard who has benefited from the municipal services as they needed the work completed before they could open their store. ProFac received no benefit from the services.

93 In addition, ProFac presents a 'value added' argument. The value of Picard's property was increased because the lots were fully serviced. While there was no direct evidence on this issue, it is a logical inference that the property value increased by some unspecified amount.

94 As regards Picard's claim to equitable relief, ProFac argues Picard cannot succeed on an unjust enrichment claim as the three elements of an unjust enrichment (an enrichment, a corresponding deprivation and an absence of any juristic reason for the enrichment) are not established. Unlike the situation in *Rona*, *infra* the ultimate recipient of the funds

here is the victim, ProFac, not the Crown. Accordingly, Picard must show it conferred a benefit on ProFac, that Picard suffered a loss, and that ProFac's retention of the benefit would be unjust. On the first and third branches Picard's claim fails.

95 ProFac denies their opposition to the return of funds to Picard is a collateral attack on Picard's judgment against Massdan. That was a breach of contract judgment. They also reject Picard's windfall argument. It was ProFac that lost $2.8 million and has little hope of recovering all the funds illegally obtained by Sankar. What Picard wants is to have their judgment paid and they wind up with serviced lands.

96 ProFac argues that the Picard default judgment is in relation to a contract and not land. Accordingly, Picard is a general creditor and not entitled to collect from proceeds of crime. Picard's interest in Massdan's assets is as a general creditor.

97 Profac also notes s. 93 of the *Land Titles Act* that requires the amount of the charge to be specified in the charge. Here, the amount is $110,000 although there is a reference to the total costs of the municipal services. Having a blank amount in the charge makes the charge invalid or at least only enforceable for up to $110,000.

98 Finally, in relation to Picard's claim that the funds from the sale of 561 Dundas St. should be available to Picard if the funds from the sale of 457 Dundas are insufficient to cover Picard's judgment, ProFac submits that judgment creditors are ordinary creditors and are not entitled to have funds returned.

99 *The Crown* supports ProFac's position and argues Picard's conduct after learning of the CPL was somewhat akin to someone who is "willfully blind" in criminal proceedings. That doctrine imputes knowledge to an accused whose suspicion is aroused to the point that he or she realizes the need for further inquiries, but deliberately chooses not to make those inquiries. *R. v. Sansregret*, [1985] 1 S.C.R. 570 (S.C.C.).

100 Ms. Gauthier submits this is not a civil proceeding. Rather, it is a criminal sentencing hearing involving the forfeiture of illegally obtained funds. It has already been determined that illegally obtained funds were used by Massdan to buy their Dundas St. E. properties. It is in the public interest to send a message that crime does not pay and that illegally obtained gains will be returned to the party from whom they were taken. The Crown points out ProFac did everything it could to preserve and secure the properties. For its part, Picard did nothing to notify ProFac of its mortgage.

101 In relation to the CPL, Ms. Gauthier submits that a key to this application is how I characterize Picard's conduct noting there was no evidence where Picard got the idea that the CPL related to an easement issue. John Picard made what he no doubt honestly felt was a prudent business decision when he was pressed for time. However, he knew the risks he ran by not checking out the details of the CPL. To give Picard all the money sought would be to give Picard a windfall — two fully serviced lots. Boll knew that the mortgage had to be registered on both parts of Massdan's property which leads to the inescapable conclusion that Picard had to know both lots had to be dealt with together. If he did not know...he was wilfully blind.

102 Ms. Gauthier also submits Picard was being less than candid in his affidavits about whether there was a verbal agreement with Massdan before the May, 2006, agreement. He said he thought the car wash was well under way yet the site plan was dated 2004. When Picard bought its property in May, 2005, no work had been done on the car wash. Further, there was nothing that obligated Massdan to do the work.

Analysis

103 Fraud is a designated offence as defined in s. 462.3(1). Derek Sankar's illegally obtained funds were used by Massdan to buy 457 and 561 Dundas St. E. The properties were proceeds of crime within the meaning of s. 462.3(1). In relation to 457 Dundas St. E., Picard agreed to remove its mortgage and writ of execution to permit ProFac to sell the property with the funds held pending the determination of the conflicting claims to the funds. In relation to 561 Dundas St. E., it has also been sold by ProFac and the funds paid into court. The funds from both sales are subject to

forfeiture as "property acquired in exchange for or by conversion of the original property." *R. c. Lavigne*, 2006 SCC 10 (S.C.C.) at para. 13.

104 I must be satisfied of the four s. 462.41(3) criteria before I determine whether to exercise my discretion and order funds returned to Picard. Three are not in dispute:

1) Picard is not a person charged with or convicted of a designated offence,

2) Picard is not a person who acquired title to or possession of the property from Sankar who was convicted of a designated offence under circumstances that give rise to a reasonable inference the title was transferred for the purpose of avoiding forfeiture of property, and

3) Picard appears innocent of any complicity in relation to Derek Sankar's fraud.

105 What remains to be determined are the following:

1) Is Picard the lawful owner or lawfully entitled to possession of any of the funds being held?

2) If the answer to the first question is 'yes,' should I exercise my discretion and order funds returned to Picard?

106 To answer those questions requires: an assessment of the evidence, findings of fact including whether Picard was a secured creditor and if so to what extent, the amount that is "recoverable" on the mortgage, the amount that is "recoverable" on the basis of Picard's civil judgment based on breach of contract, whether the proceeds from the sale of 561 Dundas St. E. are available should those from the sale of 457 Dundas St. E. be insufficient to satisfy the order for the return of property to Picard, and if funds are to be returned to Picard whether it should be the total amount sought or a lesser amount and how that would be calculated.

Findings of Fact

107 With the exceptions noted later in the reasons, in general, I found the witnesses to be credible and reliable. No one was intent on misleading the court. Each witness gave his evidence in a straightforward manner, was internally consistent within their testimony and was not shaken in cross-examination. I have to take into consideration that the events to which those who were involved in the transactions testified occurred several years earlier. Reconstructing events and thought processes that occurred years earlier can be challenging even with notes or other records.

108 Concerns were raised regarding inconsistencies within John Picard's affidavits and his trial evidence. There were inconsistencies. However, I do not find that they materially impacted on his credibility or reliability. He impressed me as an honest witness who regrettably put too much faith in the word of a person he barely knew, Audrey Holder-Sankar. His determination to open his store and, no doubt, frustration from the delays were the driving forces behind decisions that did not reflect appropriate detached reflection. Poor or careless decisions, however, do not reflect on credibility or reliability.

109 Having regard to all the evidence, I am persuaded that John Picard probably believed the car wash plan was progressing at the time they purchased the property. That information probably came from Audrey Holder-Sankar and/or Dwayne Vogel. Otherwise there was no reason to include clauses "3" and "4" in the schedule to the Offer of Purchase and Sale. I appreciate that clause "3" states the property "may or will have a temporary easement for the total site servicing" and not that it will, but clause "4" specifies that Picard will pay the costs of connecting the services from its new building to the services in front of the Picard property.

110 I accept John Picard's evidence that there were at least discussions during the negotiations preceding Picard's purchase of 447 and 453 Dundas St. E. with Massdan, if not previous offers that included the Massdan's commitment to proceed with the car wash. However, that the commitment did not appear in the accepted offer, is telling against Picard because it could be indicative of Massdans' lack of commitment or financial ability to fulfil the obligation. No doubt

with the wisdom of hindsight, it should have been included. While there is no direct evidence why it was not in the final offer of purchase and sale, it is a reasonable inference that Massdan would not agree to its inclusion. After watching and hearing John Picard's evidence, I find that he was likely prepared to accept Audrey Holder-Sankar's and/or Dwayne Vogel's word and not insist on it being in the offer. While he no doubt placed too much faith in what he was told, I find his evidence in this area is probably accurate.

111 With regards to the registration of the CPL on 457-Part 2 only, unlike some of the authorities relied upon by counsel, there is no explanation on this record why the CPL was not registered on 457-Part 1. It was not simply a "one off" because the *Mareva* injunction and *Anton Piller* orders had a schedule attached that also listed only 457-Part 2. However, in ProFac's Amended Statement of Claim issued on June 14, 2005, ProFac claimed an interest in properties listed in Schedule "A" that included both 457-Part 1 and 457-Part 2. While ProFac argued it was an "irregularity" and relied on a case where the omission was on oversight or error, on this record, I am unable to conclude why the CPL was registered as it was. I am not prepared to draw the inference it was an oversight or an irregularity. I simply do not know why the CPL was not registered on both lots.

112 When Picard finally obtained its site-specific zoning after what must have been a very frustrating and infuriating year, there is overwhelming evidence that Picard was extremely anxious to proceed with its development. Picard paid $650,000 for the property but had yet to earn a nickel of profit. John Picard's frustration and anxiety led him to once again naively and perhaps carelessly accept Audrey Holder-Sankar's word and to act with haste to Picard's ultimate detriment.

113 As regards John Picard's reaction to the CPL, the evidence is inconsistent. He testified that he was uncertain where he got the information that it related to a right-of-way but in an earlier affidavit said the information came from Vogel. I do not find he was deliberately "forgetful." Perhaps it was the passage of time that accounted for his failure to recall the source of the information. In all the circumstances, I accept that at some point he was told there was a right-of-way dispute and that he may very well have been told that it originated from the farm owners who owned the property before Massdan. At its highest, his information could be described as sketchy.

114 From John Picard and James Boll's evidence it is clear that they discussed the CPL and at least Mr. Boll read it. The CPL named Massdan, Derek Sankar and Audrey Holder-Sankar as defendants, and noted that in the proceeding an interest in the lands, including 457 Dundas St. E., Hamilton, Ontario Part 2 was in issue. Picard knew that a decision had to be made about the CPL. Indeed, Mr. Boll wrote to Massdan's counsel, Paul Lafluer, suggesting the CPL "application" be removed. Roughly a week later, Paul Lafleur wrote saying in effect that there was no necessity to remove it because Mr. Picard "knew all about it" and was prepared to proceed with it on title. John Picard probably believed the CPL had something to do with a right-of-way and that someone was claiming an interest in 457-Part 2. With the benefit of legal advice John Picard was prepared to proceed notwithstanding the CPL and his minimal understanding of what it involved.

115 I find that to a large extent, that decision was based on legal advice that the title to 457-Part 1 was clear. That lot was the larger of the two lots with a value that would more than cover the anticipated costs of the municipal services. Based on John Picard's and James Boll's evidence, I find that they discussed the implications of the *Planning Act*'s prohibition on dealing with one of two adjoining properties owned by the same person. Registering the mortgage on both 457-Part 1 and 457-Part 2, recognized the prohibition. Relying on the *Land Tittles* register, Picard's interests in 457-Part 1 were unencumbered and in 457-Part 2, Picard's interest was subrogated by the CPL.

116 The *Planning Act* did not *completely* handcuff Picard. First, while it may have been unlikely both 457 lots could be purchased with 457-Part 2 subject to the CPL, that possibility existed. This case provides an example of a businessman who was prepared to deal with property subject to a CPL.

117 Second, while I accept ProFac's submission that none of the statutory exceptions existed so as to permit Picard to deal with only 457-Part 1, that is not the end of the matter. Sections 50(5)(f) and (18) of the *Planning Act* authorize a council or its delegate, the Committee of Adjustments, to consent to an owner dealing with one of two adjoining

properties. Picard could have applied for permission to deal with only 457-Part 1. Whether such an application would have been granted cannot be predicted.

118 Third, in appropriate circumstances, a court can issue a vesting order despite contravening the *Planning Act*. See: *724597 Ontario Inc. v. Merol Power Corp.*, [2005] O.J. No. 4832 (Ont. S.C.J.) at paras. 13 and 14 and s. 100 of the *Courts of Justice Act*, R.S.O. 1990, Chap. C.43.

119 I accept Mr. Boll's evidence and Mr. Riddell's submission regarding Mr. Picard's attitude when he learned for the first time, that the municipality linked his development to the previously negotiated, but never completed, Massdan's subdivision agreement and that the car wash was not going ahead in the foreseeable future. A crisis had developed for Picard. In the previous year Picard had spent $650,000 acquiring land for a new retail outlet and endured considerable frustration dealing with the municipality to get the site-specific zoning. Once that was finally achieved, a new hurdle had been placed in the way of the development. John Picard's message was clear: as soon as possible make the arrangements with Massdan so the municipal services were installed. Haste was the key motivation for the instructions Mr. Boll fulfilled.

120 What I do not accept as reasonable, is James Boll's evidence that Picard did not have the luxury of time to investigate the CPL. The negotiations regarding the agreement and collateral mortgage did not start one morning at nine o'clock and finish by noon that same day. The exchange of letters between Boll and Paul Lafleur about removing the CPL was on May 18, 2006 to Paul Lafleur and Mr. Lafleur's response was on May 23, 2006. There was ample time within which to make inquiries had it been anything close to a priority.

121 The reason no further inquires were directed by John Picard were his priorities, haste and his naïve and careless reliance on Audrey Holder-Sankar's and/or Vogel's word regarding the CPL. While I accept his evidence that he thought Audrey Holder-Sankar's agreement to repay Picard meant she was willing and able to do so, when on his own evidence, she was just a neighbour reflects a charitable level of generosity to a person and company about whose finances, honesty and reliability he knew nothing. While Picard had given Massdan $650,000 a year earlier, it was an unrealistic leap of faith that Massdan would repay Picard when John Picard knew nothing had been done on the car wash in a year and Ms. Holder-Sankar said she was not in a position to proceed at that time or in the near future.

122 Finally, as regard's Picard's argument that their priorities pre-date the written agreement with Massdan, I am not persuaded that there was an oral contract that predated the written agreement with regards to Picard paying for all of the municipal services. There is no reference to a binding oral agreement in John Picard's August 8, 2009 affidavit. While I accept that there were likely discussions, I cannot find on any standard that there was an oral agreement that never made its way into the written one. While I do not doubt John Picard's honesty, on this record I cannot find there likely was an oral agreement. Even if there was such an agreement on this record it would be impossible to fix a date upon which it was reached.

Was Picard a secured creditor in relation to 457-Part 1 and 457-Part 2?

123 I find Picard did not receive actual notice of the CPL in relation to 457-Part 1 and that Picard is a secured creditor on the basis of its mortgage with regards to 457-Part 1 and 457-Part 2, although its claim on 457-Part 2 was subrogated to ProFac's because of the CPL. I reach those conclusions for the following reasons.

124 First, dealing with whether Picard had "actual notice," I accept ProFac's submission that the onus is on Picard to establish they did not get actual notice. Section 78(5) of the *Land Titles Act* states:

> Subject to any entry to the contrary in the register and subject to this *Act*, instruments registered in respect of or affecting the same estate or interest in the same parcel of registered land as between themselves rank according to the order in which they are entered in the register and not according to the order in which they were created, and, despite any express, implied or constructive notice, are entitled to priority according to the time of registration

125 As s. 78(5) does refer to actual notice, the notice doctrine still applies in Ontario. *Romspen Investment Corp. v. 2126921 Ontario Inc.*, 2010 ONCA 854 (Ont. C.A.) at para. 1, affirming 2010 ONSC 317 (Ont. S.C.J.). "Actual notice" has been defined to mean actual knowledge of the very fact required to be established, which is "knowledge not presumed as in the case of constructive notice, but shown to be actually brought home to the party to be charged with it." *Peterkin v. McFarlane* (1885), 13 S.C.R. 677 (S.C.C.) at p. 694. More recently, this Court has examined the issue in *Canadian Imperial Bank of Commerce v. Rockway Holdings Ltd.* (1996), 29 O.R. (3d) 350 (Ont. Gen. Div.); *Durrani v. Augier* (2000), 50 O.R. (3d) 353 (Ont. S.C.J.) and *Bank of Montreal v. Smith* (2008), 71 R.P.R. (4th) 52 (Ont. S.C.J.).

119 In *Canadian Imperial Bank of Commerce*, *supra*, relied upon by ProFac, Salhany J. held at para. 13:

> My review of the authorities leads me to the conclusion that the term "actual notice" means actual notice (as opposed to constructive notice) of the nature of the prior agreement and its legal effect. There is no requirement that there be actual notice of the precise terms of the agreement, such as the amount of the consideration passing between the parties or the term of the agreement. The test, in my view, is whether the registered instrument holder is in receipt of such information as would cause a reasonable person to make inquiries as to the terms and legal implications of the prior instrument.

126 *In Durrani*, *supra*, Epstein J., as she then was, found at para. 62:

> Thus, a person has actual notice if he or she is aware of the existence of a legal right. It is not necessary that the person have knowledge of the precise details of that legal right. In circumstances that involve the transfer of title, a purchaser does not need to have actual knowledge of the particular person who is in fact the true owner or holder of title of the property. It is sufficient for actual notice that the purchaser is aware that the person with whom they are dealing as the vendor does not have a legitimate claim to the title. This follows, since the logical inference to draw from the knowledge that the vendor with whom the purchaser is dealing does not have a legitimate right to the title is that someone else is, in fact, the true owner.

127 Finally, in *Bank of Montreal*, Murray J. held at para 53:

> I do not read these cases as authority for the proposition that constructive notice is sufficient to protect an unregistered prior interest in land under the *Land Titles Act*. Quite the contrary, a subsequent encumbrance must have actual notice of the nature of the prior agreement and its legal effect before being bound by a prior unregistered instrument. ...

128 Applying those definitions, I am not persuaded Picard had actual notice. Picard likely had constructive, but not actual notice. The CPL was only registered on 457-Part 2. It was registered under the *Land Titles* system that "embodies the principle that the register is a mirror of the state of the title." *R.A. & J. Family Investment Corp. v. Orzech*, [1999] O.J. No. 2249 (Ont. C.A.) at para. 15. It is designed to let the public look at the register and rely upon it. Lot 457-Part 1, the larger property was clear. John Picard believed, albeit wrongly and carelessly, the CPL dealt with a right-of-way issue.

129 No doubt, the prudent course would have been for Picard's lawyer to make inquiries, inquiries that he had time to make. However, that does not equate with actual notice. It cannot be said that it has been shown the knowledge was "actually brought home" to Picard, in the words of *Rose*, *supra*. It has to be actual notice of the prior agreement, or here, actual notice of the interest claimed and details of the litigation. Applying Salhany J.'s words in *Canadian Imperial Bank of Commerce*, *supra*, John Picard was in receipt of information that there was pending litigation that I accept he believed was in relation to a right-of-way. I am not persuaded that was "such information as would cause a reasonable person to make inquiries" as to the terms and legal implications of the CPL when the CPL was not registered on 457-Part 1. That he knew there could be enforcement problems because of the *Planning Act*, does not equate with actual knowledge. The mortgage could be, and was, registered against both properties.

130 In regards to 457-Part 1, there is neither evidence nor an inference that Picard was aware that Massdan did not have a legitimate or unencumbered claim to title. In fact, Massdan had clear title to the largest lot. As Murray J. held in *Bank of Montreal, supra*, constructive notice is not sufficient to protect an unregistered prior interest under the *Land Titles Act* without actual notice of the nature of the prior agreement/claim and its legal effect.

131 While ProFac relies on *Romspen Investment Corp. v. 2126921 Ontario Inc.*, 2010 ONCA 854 (Ont. C.A.), affirming 2010 ONSC 317 (Ont. S.C.J.), I find that case is factually distinguishable. In *Romspen Investment Corp., supra*, a first mortgagee's mortgage in relation to a restaurant, motel and parking lot was erroneously registered against the motel and restaurant only. The zoning by-law did not permit the restaurant and motel to operate without the parking lot. This was known to the second mortgagee who registered his mortgage on the parking land that at the time had a clear title because of the lawyer's error. There was no *Planning Act* issue because the parking lands were across the street from the restaurant and motel. The second mortgagee argued that he had priority in relation to the parking lands.

132 The application judge disagreed noting in the background facts that Romspen's "lawyer in error registered the mortgage against only the motel and restaurant lands." Once the error was discovered and before any default on the mortgage, Romspen asked the second mortgagee to allow the registration error to be corrected by postponing his mortgage. A mortgage broker and lawyer both testified that they told the second mortgagee that he held a second mortgage. The mortgage broker testified he told the second mortgagee that Romspen held the first mortgage. A title insurance document given to the second mortgagee showed he held a second mortgage. The application judge found the second mortgagee had actual notice of the first mortgage. There is no similar evidence here of Picard being told and shown documents that 457-Part 1 was subject to the CPL.

133 Turning next to the Crown's argument that Picard was 'willfully blind,' a concept frequently encountered in criminal law, wilful blindness acts as a substitute for actual knowledge, by imputing knowledge to an accused person whose suspicions are sufficiently aroused to the point that he or she sees the need to make further inquiries, but deliberately decides not to do so, because he or she does not want to know the truth, preferring to remain ignorant. Put differently, a finding of wilful blindness involves an affirmative answer to the question: did the accused shut his eyes because he knew or strongly suspected that looking would fix him with knowledge." Wilful blindness is distinct from recklessness. A finding of wilful blindness can only be made where it can *almost* be said that the person actually knew. He suspected the fact and realized its probability. *R. v. Briscoe*, 2010 SCC 13 (S.C.C.) at para. 21, 22 and 23. The question is not whether he or she should have been suspicious, but whether they were in fact suspicious *of the fact. R. v. Malfara*, [2006] O.J. No. 2069 (Ont. C.A.)

134 While this application arises in a sentencing hearing, the case law has repeatedly referred to forfeiture applications as *quasi*-civil. *Connolly, supra.* Wilful blindness is established where it can almost be said that the accused actually knew. What is required on this application is a finding of actual notice or deemed notice, not almost a finding of actual notice.

135 Assuming the concept applies in this proceeding, I would have to find that John Picard directed his mind to the need for further inquiries about whether the CPL related to fraudulent conduct and/or a civil claim for millions of dollars. The person must advert to the risk of what it was, in drug importations, that the gift suitcase was heavy because it contained illegal drugs. There is no basis upon which the requisite conclusion could be reached here.

136 In the alternative, the willful blindness argument might apply to whether there had been a mistake in registering the CPL on only one lot. I would not make that finding on this evidence given John Picard's and Boll's evidence that they were satisfied that 457-Part 1 provided adequate equity to cover the costs of the municipal services. Neither Boll nor Picard adverted to the potential there was a registering error or irregularity. This conclusion is supported in this case by the absence of evidence as to why the CPL was not registered on 457-Part 1.

137 I cannot find that Picard had actual notice. In the result, I find Picard was a secured creditor based on its mortgage in relation to the Massdan lots, clear on 457-Part 1 and encumbered by the CPL on 457-Part 2. Picard was lawfully entitled to a portion of the proceeds of crime as required by s. 462.41(3).

Should the court exercise its discretion and order the return of funds to Picard, and if so, in what amount?

138 Balancing of the equities noted in previous authorities and referenced by all counsel in argument, I will order the return of part of the funds claimed by Picard and decline to grant relief in the full amount sought by the Crown and ProFac for the following reasons.

139 Dealing first with ProFac, they are the victims of the designated offence and lost $2.8M. The forfeiture provisions of the *Criminal Code* were enacted to ensure that crime does not pay for the offender and that illegally obtained property is returned to the victim. ProFac has gone to considerable expense to attempt to locate and freeze the proceeds of crime, a process that has been time consuming and expensive involving numerous court proceedings and I infer many attendances. Had it not been for ProFac's efforts there might have been no funds or a smaller amount from which Picard could claim.

140 I accept that ProFac has co-operated in the police investigation and the prosecution of Derek Sankar. It is a valid consideration that if Picard recovers the total amount of the municipal services for all four lots, that Picard will have benefitted by getting two serviced lots at no costs although that is what Picard bargained for with Massdan. It is also important to note that the provision of the services permitted Picard to proceed with its development. While I appreciated Picard's submission that if all the funds are forfeited, ProFac winds up with two serviced lots, it is difficult to see the victim of a $2.8M fraud from which they might recover about $1M as receiving a windfall as Picard contends.

141 On the other hand, ProFac's handling of the CPL caused the dispute to arise. ProFac provided no explanation why the CPL was not registered on 457-Part 1.

142 As regards Picard, they used their lawfully acquired money to obtain services that to some unspecified extent benefited Massdan as well as Picard. John Picard honestly, albeit carelessly, believed his company would be repaid. To grant total forfeiture to ProFac results in Picard paying for services that increased the value of lots ProFac sold. On this record, that Picard would still have a valid judgment against Massdan, would be faint consolation as Massdan's assets are frozen and it is highly unlikely there will be anything left for Picard to pursue.

143 While Picard is not a direct victim of the designated crime although they can be seen as a "corollary victim" having being duped into signing an agreement Audrey Holder-Sankar had to know was in contempt of court and an agreement she knew she would never fulfill. Picard's dealings with Ms. Holder-Sankar revealed good faith but reckless reliance on the words of someone about whom Picard knew little.

144 On the other hand, Picard's careless reaction to the CPL, while not establishing actual notice, is a very relevant consideration in determining whether to exercise my discretion in favour of Picard for the full amount claimed. In addition, providing all of the services was the only way Picard was going to open its outlet on 447 Dundas St. E.

145 I accept the evidence that some of the services benefitted both Picard and Massdan; some benefited only Picard while others benefitted only Massdan. In regards to the competing "windfall" to the other party arguments of Picard and ProFac, while there is no evidence what amount the value of the lots increased because of the municipal services, it is a reasonable inference that the services added something to the value of the lots although a specific amount cannot and need not be determined. That Picard never asked for or wanted the services applies equally to ProFac.

146 In all these circumstances I am persuaded that it is an appropriate case in which to exercise my discretion and order some funds returned to Picard. I am not persuaded that all of the funds claimed should be returned based on the equities canvassed. The potential unfairness of an "all-or-noting" resolution are minimized if the costs of the services is apportioned in the manner described by Paul Cameracci. I was impressed by his evidence. His testimony that

apportioning costs on the basis of frontage was the standard applied was not contested. Where there are limited funds available and considering the equities, I am persuaded that is the fairest resolution of the issues.

147 Accordingly, the costs of the municipal services should be shared in proportion to the frontage of the lots in a similar manner to that used by Mr. Cameracci in his calculations. However, the first issue to be determined in this area is what were the costs of installing the municipal services. Picard submits the costs are what Picard actually paid, $248,699.05. Based on Mr. Cameracci's evidence, ProFac submits a reasonable total cost is $157,074.71.

148 While I appreciate that I can and have considered Mr. Cameracci's evidence in considering the equities, on this record, I am not prepared to adopt the lower amount. First, there is no suggestion that Picard did not actually pay for the amount they seek. Second, while I do not dispute Mr. Cameracci's methodology, I am not prepared to adopt his figure without a detailed line-by-line examination of the costs compared to his figures. On this record, I am not prepared, to determine the issues that would have to be decided without further input and perhaps expert evidence. The starting point is $248,699.05.

149 I have also taken into consideration that Mr. Cameracci says that it is unclear whether private sanitary sewers for 457 Dundas St. E were installed and issues regarding the figures that were raised in the cross-examination of Mr. Towles.

150 Mr. Cameracci did his calculations in the context of answering the third question posed to him, what was a reasonable cost for the work done on 457 Dundas St. E? His analysis used the costs from three contracts that were proximate in time to the provision of municipal services by Picard. He did not determine what amount of the $248,699.05 would be apportioned to Picard and what amount to Massdan. In order to determine what amount will be returned to Picard before forfeiture a similar analysis is required using the money actually spent by Picard. What must be identified from Picard's costs are: 1) the items that benefitted both Picard and Massdan, 2) the items that benefitted only Picard [3] and 3) the items that benefitted only Massdan.

151 The items that benefitted only Picard will be deducted from the total. The remaining items will be apportioned using the percentages determined by Mr. Cameracci — for the sanitary sewers, the costs will be apportioned 75.2% to Picard and 24.8% to Massdan, for the water main extension, they will be apportioned 61.2% to Picard and 38.8% to Massdan. *If* there are items that benefitted both parties that are not within the sanitary sewer and water main items, they will be apportioned 68% to Picard and 32% to Massdan. Mr. Cameracci did not use these figures and it is unlikely they will be required. They are roughly the mid-point between the two calculations he used and are provided if necessary.

152 While I have reviewed all of the material, without further input from counsel, I am not prepared to do the required calculations. I would hope that counsel could agree upon the items and costs within each area or that there would be an agreement that Mr. Cameracci could provide the calculations. Failing an agreement, counsel will be permitted to submit written submissions on the calculations.

153 In reaching these conclusions, I have considered impact on Mr. Sankar from any order returning property to Picard and the forfeiture order. If all the funds were forfeited to ProFac, the restitution order would be in a smaller amount. That would still leave Picard's judgment of very questionable value against Massdan, Sankar and others. Any funds that went to Picard would increase the restitution order but decrease or remove a civil judgment. The impact of s. 462.37(3) under which an offender may be fined and in default jail imposed, is not a consideration since the Crown will not pursue a fine and do not intend to impose a fine in these circumstances. While there may be some benefits to the offender from this disposition of the proceeds of crime, I remain of the view that it the fairest resolution.

154 Subject to determining the apportionment of the costs, the remaining issues may become academic if the amount returnable to Picard is under $110,000. However, to complete the record, I will address these issues at this time.

What amount can he recovered on the basis of the mortgage?

155 Picard's civil action and judgment against Massdan was based on breach of contract. As Ms. Mouland wrote in her October 30, 2008 letter to Ms. Manning, "The mortgage was put on the property as security for the payment under that contract." Section 93(2) of the *Land Titles Act*, states that a charge securing the payment of money shall state *the amount of the principal sum that it secures*. Subsection (4) states that "a registered charge is .... A security upon the land thereby charged to the extent of the money or money's worth actually advanced or supplied under the charge, *not exceeding the amount for which the charge is expressed to be the security*."

156 This mortgage states the principal is $110,000. In the statements section immediately above the principal the following is noted:

> This charge/mortgage of land is given as collateral security for the payment required to be made by the Chargor to the Chargee, plus interest thereon, pursuant to an Agreement dated May 1, 2006 for the installation of services to the lands described in the Agreement. *Upon payment in* full *of the amount required to be paid pursuant to the Agreement*, the Chargee will execute a Discharge of this Charge. Default under one shall constitute a default under the other.
>
> (emphasis added)

157 ProFac submits that the mortgage is either void because it did not state an amount or was limited to $110,000, the stated amount. Picard submits the clause that specified Massdan would be responsible for the total costs of the municipal services should include the actual costs, that the mortgage complies with s. 93(2).

158 I am not persuaded the mortgage is void. I agree with Mr. Riddell that there might have been an issue at registration of the mortgage but once registered it is valid.

159 I am persuaded the mortgage is limited to "the amount of the principal sum that it secures" and that the funds cannot exceed the amount for which the charge is expressed as security - $110,000 plus interest, costs and any charges expressly set out in the charge. It is essential that a mortgage contains an ascertainable amount so that anyone involved in subsequent dealing with the property is aware of the amount of the prior encumbrance. If Picard is correct, there was no need to include a specific amount secured. All that was required was a reference to whatever amount was owed pursuant to the agreement. However, the mortgage was listed in the register as being for $110,000. Applying Picard's argument referenced earlier with respect to public reliance on the register, the world was notified of a $110,000 mortgage.

What amount can be recovered on the basis of the judgment for breach of contract?

160 The contract between Picard and Massdan specified Massdan was to pay the full amount of the costs. While the agreement referred to Massdan granting security for the payment by execution and registration of a collateral first mortgage in the principal sum of $110,000. The $110,000 limitation noted above does not apply to the judgment. While Picard has a judgment for the total amount spent, the amount above $110,000 is as a general creditor. For the "unsecured" balance of the judgment, Picard cannot obtain funds that are otherwise available for forfeiture.

Are the funds from the sale of 561 Dundas St. E. available to be returned to Picard?

161 Picard submits that having obtained the judgment against Massdan and filing the execution against Massdan, that Picard is a secured creditor. As such, the property ordered returned to Picard can include the proceeds of the sale of 561 Dundas St. E., another property bought by Massdan with proceeds of crime. Picard relies upon *Lynch v. Segal* (2005), [2006] O.J. No. 5014 (Ont. C.A.), a family law case where the Court held that a person taking title by way of a vesting order must take the property subject to pre-existing registered executions or encumbrances.

162 ProFac submits that Picard as a general creditor is without an interest in Massdan's assets beyond that of a general creditor relying on *R. v. Poirier*, [1996] N.B.J. No. 666 (N.B. Prov. Ct.) at para. 62-3, 72 and 77. Further, ProFac contends *Lynch, supra* is distinguishable because it did not involve a CPL. Accordingly, the funds to be returned cannot be from the sale of 561 Dundas St. E. that are held in court for the benefit of ProFac's civil action.

163 I am not persuaded Picard is a secured creditor in relation to Massdan and the proceeds of the sale of 561 Dundas St. E. Picard became a judgment creditor under the *Execution Act*, 1990 R.S.O., c. E.24, not a secured creditor. There is a distinction. See *Bascello v. Bascello (Trustee of)* [1997 CarswellOnt 892 (Ont. Gen. Div.)], 1994 CanLII 7373 at para. 11. In addition, the CPL was on 561 Dundas St. E. prior to the execution. The proceeds from the sale of 561 Dundas St. E. are not available should Picard be entitled to the return of more than $110,000 plus interest and costs.

Conclusions

164 In summary,

(1) The Crown has met the onus under s. 462.37;

(2) Picard has met its onus under s. 462.41;

(3) Picard is a secured creditor on the basis of the mortgage to the stated principal sum of $110,000 and a general creditor in relation to the balance of judgment.

(4) I am prepared to exercise my discretion to return to Picard a percentage of the costs of the municipal services and to allow 10% interest on the amount ordered returned as reflected in the judgment. The costs will be apportioned applying the methodology used by Angelo Cameracci when counsel have provided further input on this issue.

(5) The balance of the funds held in court in the civil action and the funds held by Mr. Lafleur will be forfeited to the Crown.

(6) There will be a restitution order pursuant to s. 738 in the full amount of the fraud, $2.8 million in favour of ProFac.

Order accordingly.

Footnotes

* Additional reasons at *R. v. Sankar* (2012), [2012] O.J. No. 2920, 2012 ONSC 3430, 2012 CarswellOnt 8087 (Ont. S.C.J.); further additional reasons at *R. v. Sankar* (2012), 21 R.P.R. (5th) 139, 2012 ONSC 3621, 2012 CarswellOnt 8074 (Ont. S.C.J.).

1 Now reported at (2010), 270 C.C.C. (3d) 410 (Ont. S.C.J.)

2 Soft costs include maintenance, engineering, inspection and testing.

3 Picard incurred $11,233.92 additional consulting fees that were not included in the claim that resulted in their default judgment. Having regard to James Boll's letter that Picard had "absorbed" that costs, it will not be included in the "common benefit" category.

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TAB 9

2014 ONCA 613
Ontario Court of Appeal

Toronto-Dominion Bank v. Phillips

2014 CarswellOnt 11878, 2014 ONCA 613, 122 O.R. (3d) 181, 17 C.B.R. (6th) 127, 243 A.C.W.S. (3d) 533, 325 O.A.C. 141, 376 D.L.R. (4th) 566, 46 R.P.R. (5th) 163

The Toronto-Dominion Bank, Applicant and Cindy Louise Phillips and Richard Joseph Phillips, Respondents (Appellant and Respondent, respectively)

J. MacFarland, S.E. Pepall, G.R. Strathy JJ.A.

Heard: April 15, 2014
Judgment: August 29, 2014
Docket: CA C58084

Proceedings: reversing *Toronto-Dominion Bank v. Phillips* (2013), 37 R.P.R. (5th) 234, 2013 CarswellOnt 15685, 2013 ONSC 7016, 7 C.B.R. (6th) 142, Gray J. (Ont. S.C.J.)

Counsel: Gustavo F. Camelino, for Appellant, Cindy Louise Phillips
Michael Odumodu, for Respondent, Richard Joseph Phillips

Subject: Civil Practice and Procedure; Constitutional; Corporate and Commercial; Insolvency; Property

Related Abridgment Classifications

Bankruptcy and insolvency
VI Proposal
VI.9 Consumer proposals
Real property
I Interests in real property
I.3 Co-ownership
I.3.d Termination of co-tenancy
I.3.d.iv Miscellaneous
Real property
VII Mortgages
VII.20 Miscellaneous

Headnote

Bankruptcy and insolvency --- Proposal — Consumer proposals

Creditor bank B ("execution creditor") obtained default judgment against debtors CP and RP, and filed writ of seizure and sale — Bank T ("mortgagee") sold property jointly owned by debtors after default under power of sale, with surplus remaining — CP filed consumer proposal under Bankruptcy and Insolvency Act after default of mortgage but prior to sale — Mortgagee brought application to pay surplus of $52,295 into court, and debtors agreed that $19,324 would be paid out to execution creditor but disputed manner — Application judge held that execution creditor was to be paid before there was any residue owing to debtors, and remaining balance should be split equally between CP and RP, such that each was entitled to $16,108 — CP appealed — Appeal allowed; CP entitled to $25,772 and RP entitled to $6,445 — When CP's proposal was filed and approved, execution creditor's debt was unsecured and its claim against CP was stayed — Section 27 of Mortgages Act could not elevate execution creditor's status as unsecured creditor to achieve priority over CP's other unsecured creditors — It was open to execution creditor to realize joint debt against RP, as any interest of RP was not affected by stay — Debtors consented to order authorizing payment to execution creditor,

which completed execution and severed joint tenancy — Payment to execution creditor could only be from RP's share of surplus — Application judge erred in law in ignoring stay and in not finding severance of joint tenancy.

Real property --- Mortgages — Miscellaneous

Creditor bank B ("execution creditor") obtained default judgment against debtors CP and RP, and filed writ of seizure and sale — Bank T ("mortgagee") sold property jointly owned by debtors after default under power of sale, with surplus remaining — CP filed consumer proposal under Bankruptcy and Insolvency Act after default of mortgage but prior to sale — Mortgagee brought application to pay surplus of $52,295 into court, and debtors agreed that $19,324 would be paid out to execution creditor but disputed manner — Application judge held that execution creditor was to be paid before there was any residue owing to debtors, and remaining balance should be split equally between CP and RP, such that each was entitled to $16,108 — CP appealed — Appeal allowed; CP entitled to $25,772 and RP entitled to $6,445 — When CP's proposal was filed and approved, execution creditor's debt was unsecured and its claim against CP was stayed — Section 27 of Mortgages Act could not elevate execution creditor's status as unsecured creditor to achieve priority over CP's other unsecured creditors — It was open to execution creditor to realize joint debt against RP, as any interest of RP was not affected by stay — Debtors consented to order authorizing payment to execution creditor, which completed execution and severed joint tenancy — Payment to execution creditor could only be from RP's share of surplus — Application judge erred in law in ignoring stay and in not finding severance of joint tenancy.

Real property --- Interests in real property — Co-ownership — Termination of co-tenancy — Miscellaneous

Creditor bank B ("execution creditor") obtained default judgment against debtors CP and RP, and filed writ of seizure and sale — Bank T ("mortgagee") sold property jointly owned by debtors after default under power of sale, with surplus remaining — CP filed consumer proposal under Bankruptcy and Insolvency Act after default of mortgage but prior to sale — Mortgagee brought application to pay surplus of $52,295 into court, and debtors agreed that $19,324 would be paid out to execution creditor but disputed manner — Application judge held that execution creditor was to be paid before there was any residue owing to debtors, and remaining balance should be split equally between CP and RP, such that each was entitled to $16,108 — CP appealed — Appeal allowed; CP entitled to $25,772 and RP entitled to $6,445 — When CP's proposal was filed and approved, execution creditor's debt was unsecured and its claim against CP was stayed — Section 27 of Mortgages Act could not elevate execution creditor's status as unsecured creditor to achieve priority over CP's other unsecured creditors — It was open to execution creditor to realize joint debt against RP, as any interest of RP was not affected by stay — Debtors consented to order authorizing payment to execution creditor, which completed execution and severed joint tenancy — Payment to execution creditor could only be from RP's share of surplus — Application judge erred in law in ignoring stay and in not finding severance of joint tenancy.

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Cases considered by *S.E. Pepall J.A.*:

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Cameron Estate, Re (2011), 10 R.P.R. (5th) 326, 2011 CarswellOnt 12323, 2011 ONSC 6471, (sub nom. *Cameron, Re)* 108 O.R. (3d) 117, 83 C.B.R. (5th) 272, 343 D.L.R. (4th) 370 (Ont. S.C.J.) — referred to

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Ontario Development Corp. v. I.C. Suatac Construction Ltd. (1976), 12 O.R. (2d) 465, 22 C.B.R. (N.S.) 42, 69 D.L.R. (3d) 353, 1976 CarswellOnt 50 (Ont. C.A.) — referred to
Polsak, Re (1978), 1978 CarswellOnt 176, 19 O.R. (2d) 570, 27 C.B.R. (N.S.) 227, 85 D.L.R. (3d) 748 (Ont. H.C.) — distinguished
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Statutes considered:

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s. 50 — considered

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Generally — referred to

Pt. III, Div. I — referred to

Pt. III, Div. II — referred to

s. 66(1) — considered

s. 66.11 "consumer proposal" [en. 1992, c. 27, s. 32(1)] — considered

s. 66.12(3) [en. 1992, c. 27, s. 32(1)] — considered

s. 66.13 [en. 1992, c. 27, s. 32(1)] — referred to

s. 66.28(2)(a) [en. 1992, c. 27, s. 32(1)] — considered

s. 66.4(1) [en. 1992, c. 27, s. 32(1)] — considered

s. 69.2(1) [en. 1992, c. 27, s. 36(1)] — considered

s. 69.2(1)(a) [en. 1992, c. 27, s. 36(1)] — considered

s. 69.2(4) [en. 1992, c. 27, s. 36(1)] — considered

s. 70 — considered

s. 70(1) — considered

Execution Act, R.S.O. 1990, c. E.24
Generally — referred to

s. 1 "execution creditor" — considered

Mortgages Act, R.S.O. 1990, c. M.40
s. 27 — considered

Authorities considered:

Lem, Jeffrey W. and Rosemark Bocska, *Halsbury's Laws of Canada — Real Property*, 1st ed. (Markham, Ont.: LexisNexis Canada, 2012)

APPEAL by debtor from judgment reported at *Toronto-Dominion Bank v. Phillips* (2013), 2013 ONSC 7016, 2013 CarswellOnt 15685, 7 C.B.R. (6th) 142, 37 R.P.R. (5th) 234 (Ont. S.C.J.), dividing surplus funds after sale of property.

***S.E. Pepall J.A.*:**

1 This appeal addresses the interaction between a consumer proposal under s. 66.13 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("the *BIA*"), and a writ of execution registered against joint debtors, one of whom has filed a consumer proposal.

2 The appellant, Cindy Louise Phillips, the consumer debtor who filed the proposal, submits that after payment to the execution creditor, the application judge erred in ordering that the remaining sum of $32,217.64 be distributed equally between her and the respondent, her estranged husband, Richard Joseph Phillips.

3 For the reasons that follow, I agree with the appellant.

A. Facts

(1) Joint Indebtedness

4 The appellant and the respondent were spouses and owned residential property in Guelph, Ontario as joint tenants. In November 2008, they granted a mortgage on the property in the amount of $268,000 to the Toronto-Dominion Bank ("TD").

5 The appellant incurred debt using an overdraft facility on the parties' joint bank account with the Bank of Montreal ("BMO"). On April 6, 2011, BMO obtained a default judgment against the appellant and the respondent in the amount of $32,734.37 plus costs of $1,161.15.

6 On April 13, 2011, BMO filed a writ of seizure and sale with the Sheriff of the County of Wellington (Guelph).

7 The mortgage in favour of TD went into default. On November 5, 2012, TD commenced power of sale proceedings.

8 In December 2012, the appellant and the respondent separated.

(2) Consumer Proposal

9 On February 1, 2013, the appellant filed a Division II consumer proposal pursuant to s. 66.13 of the *BIA*. Hoyes, Michalos & Associates Inc. was appointed as the proposal administrator. Notice of the proposal was provided to the appellant's creditors, including BMO. The proposal contemplated payment of secured creditors and preferred claims and payment of $18,000 over five years for the benefit of unsecured creditors. Property would remain vested in the appellant. The appellant's statement of affairs did not mention any interest in the Guelph property. The appellant stated that at the time she filed her proposal, she was unaware that there would be any equity left in the Guelph property.

10 BMO filed two claims in the proposal proceedings.

11 BMO and the other creditors that participated voted in favour of the proposal. On March 18, 2013, the appellant's proposal was deemed to have been approved by the court. Under the proposal, BMO was entitled to a dividend of $3,682.79.

12 On April 4, 2013, TD sold the property. There was a surplus of $52,295.14 after payment of its mortgage and associated costs.

13 The proposal administrator advised the appellant's creditors of the surplus funds and gave them an opportunity to request a meeting of creditors in order to amend the proposal. No creditor responded.

(3) TD's Court Application

14 TD applied to pay the surplus funds into court less $750 on account of its costs of the application, leaving a surplus of $51,545.14. On the return of the application, the application judge heard submissions from the parties to the application and from BMO. The appellant and the respondent agreed that the sum of $19,327.50 would be paid out of the surplus to the Bank of Montreal, and the application judge so ordered. On payment, BMO withdrew its claim in the proposal proceedings. According to the appellant's oral submissions before this court, the payment to BMO was without prejudice to the positions of the appellant and the respondent on the proper allocation of the remaining balance of $32,217.64.

15 Before the application judge, the respondent argued that after TD and BMO had been paid, the remaining balance of $32,217.64 should be split equally between the appellant and the respondent. In contrast, the appellant argued that, due to the operation of the stay of proceedings imposed by s. 69.2(1) of the *BIA*, 50% of the remaining balance should be paid to her, and BMO's writ should be paid out of the respondent's 50% share. Under this proposed distribution plan, the appellant would receive $25,772.57 and the respondent would receive $6,445.07, which is the balance remaining after payment to the appellant and BMO.

16 The motion judge ordered distribution of the funds in accordance with the scheme proposed by the respondent. Applying s. 27 of the *Mortgages Act*, R.S.O. 1990, c. M.40, and provisions of the *Executions Act*, R.S.O. 1990, c. E.24, he determined that a writ of execution created a right to or an interest in land. As such, BMO was a subsequent encumbrancer within the meaning of s. 27 of the *Mortgages Act* and had to be paid before there was any residue owing to the appellant and the respondent.

B. Grounds of Appeal

17 The appellant submits that the application judge erred in finding that an execution creditor is a subsequent encumbrancer within the meaning of s. 27 of the *Mortgages Act* and erred in respect of BMO's right to enforce its writ against her. It is her position that BMO's claim against her was stayed as a result of s. 69.2(1) of the *BIA*. Accordingly, BMO could only realize against the respondent's share of the residue remaining after payment of the mortgagee, TD. As such, the respondent is entitled to $6,445.07 and the appellant is entitled to $25,772.57.

18 The proposal administrator is funding this appeal on behalf of the appellant, who has agreed that her interest in the surplus will be paid to the administrator to pay its fees and to fund payments due under the proposal. This would include any amendments that may be agreed upon between the appellant and her creditors as a result of the disclosure of the existence of the surplus funds. In the event that there is a balance left over, it would be paid to the appellant.

C. Analysis

(1) Proposals

19 Under the *BIA*, insolvency may be addressed by proposals and by bankruptcy. In general terms, a proposal provides a debtor with an opportunity to restructure debt, whereas bankruptcy provides a mechanism for liquidation of assets.

20 Proposals enable debtors to make arrangements with their creditors, including settlement of debts and extensions of time for payment. They are available under Divisions I and II of Part III of the *BIA*. Division I proposals are available to an insolvent or bankrupt debtor, including a corporation. A Division II proposal, which is at issue in this appeal, is known as a consumer proposal. A consumer proposal is available to an insolvent or bankrupt individual who has indebtedness of not more than $250,000 (or any other prescribed amount) excluding debts secured by the individual's principal residence.

21 Consumer proposals are described in s. 66.11 and following of the *BIA*. A consumer proposal is to be made to the creditors of the debtor generally: s. 66.12(3). A consumer proposal that is accepted, or deemed to have been accepted,

by the creditors, and approved, or deemed to have been approved, by the court, is binding in respect of all unsecured claims: s. 66.28(2)(a).

22 Unlike a bankruptcy where the debtor's property vests in the trustee in bankruptcy, in a proposal property may remain with the debtor. Like a bankruptcy, however, a stay of proceedings is available to a debtor on the filing of a consumer proposal. Section 69.2(1) of the *BIA* states:

> [O]n the filing of a consumer proposal under subsection 66.13(2) or of an amendment to a consumer proposal under subsection 66.37(1) in respect of a consumer debtor, no creditor has any remedy against the debtor or the debtor's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy until
>
> (a) the consumer proposal or the amended consumer proposal, as the case may be, has been withdrawn, refused, annulled or deemed annulled; or
>
> (b) the administrator has been discharged.

23 Section 69.2(4) exempts secured creditors from the stay, although in appropriate circumstances, the court may extend the application of the stay to secured creditors as well.

24 Section 69.2(1) therefore imposes a comprehensive prohibition on remedies against the debtor or the debtor's property once a consumer proposal has been filed. The stay includes a prohibition against the commencement or continuation of any action, execution or other proceeding for the recovery of a claim.

(2) Execution Creditor

25 This appeal also involves a writ of execution held by BMO, the execution creditor.

26 Section 1 of the *Execution Act* defines "execution creditor" as including "a person in whose name or on whose behalf a writ of execution is issued on a judgment, or in whose favour an order has been made for the seizure and sale of personal property, real property or both real property and personal property."

27 In bankruptcy, it has long been established that an execution creditor is not a secured creditor: see *Quebec (Attorney General) v. Bélanger (Trustee of)*, [1928] A.C. 187 (Canada P.C.), at p. 197; *Sklar, Re* (1958), 37 C.B.R. 187 (Sask. C.A.) at p. 194; *Ontario Development Corp. v. I.C. Suatac Construction Ltd.* (1976), 12 O.R. (2d) 465 (Ont. C.A.), at p. 476; and *James Hunter & Associates Inc. v. Citifinancial Inc.* (2007), 40 C.B.R. (5th) 149 (Ont. S.C.J.), at para. 22. Rather, unless the execution has been completed by payment to the creditor, the debt of the execution creditor is treated rateably with other unsecured debt.

28 This jurisprudence relies in part on the need to treat unsecured creditors equally under the bankruptcy regime and on s. 70 of the *BIA* and its predecessor, s. 50 of the *Bankruptcy Act*, R.S.C. 1970, c. B-3. Section 70(1) of the *BIA* is found under the sub-heading *General Provisions* in Part IV of the *BIA*. It states:

> Every bankruptcy order and every assignment made under this Act takes precedence over all judicial or other attachments, garnishments, certificates having the effect of judgments, judgments, certificates of judgment, legal hypothecs of judgment creditors, executions or other process against the property of a bankrupt, except those that have been completely executed by payment to the creditor or the creditor's representative, and except the rights of a secured creditor. [Emphasis added.]

29 This sub-section speaks of the precedence of bankruptcy orders and assignments. Arguably a proposal or an order approving a proposal is not a bankruptcy order or assignment and does not fall within the ambit of that provision. However, s. 66.4(1) of the *BIA* provides that:

> All the provisions of this Act, except Division I of this Part, in so far as they are applicable, apply, with such necessary modifications as the circumstances require, to consumer proposals. [1]

30 In my view, section 66.4(1) directs that certain general provisions of the *BIA*, including s. 70(1), should be read to apply to consumer proposals even though there is no such express reference. Moreover, quite apart from the statutory language, the policy rationale of treating unsecured creditors equally applies to the proposal regime: see *Hancor Inc. v. Systèmes de Drainage Modernes Inc.* (1995), 37 C.B.R. (3d) 117 (Fed. C.A.), at p. 72. In short, I would conclude that the hierarchy reflected in s. 70(1) applies with equal force to consumer proposals.

31 Section 27 of the *Mortgages Act* therefore could not serve to elevate BMO's status to achieve priority over the appellant's other unsecured creditors. The decisions of *National Bank of Canada v. Young*, [2002] O.J. No. 3823 (Ont. S.C.J.) and *Polsak, Re* (1978), 19 O.R. (2d) 570 (Ont. H.C.), do not assist. The former did not engage the provisions of the *BIA*, and the latter involved a secured creditor who clearly took priority over any claim of the mortgagors to residue.

32 At the time the proposal was filed and approved, BMO was an execution creditor and its debt was unsecured. Consistent with this characterization, BMO filed a proof of its unsecured claim in the appellant's proposal proceedings. Its debt was paid only after TD commenced its court application, BMO appeared and made submissions, and the parties consented to payment.

(3) Stay of Proceedings

33 Pursuant to s. 69.2(1)(a), BMO's claim against the appellant was stayed once the proposal was filed. The stay of proceedings is akin to the stay imposed in a bankruptcy, which is designed to prevent creditors from gaining an unfair advantage and to allow for an orderly restructuring or liquidation: see *Cohen, Re* (1948), 29 C.B.R. 111 (Ont. S.C.), at pp. 113-14, aff'd [1948] 4 D.L.R. 808 (Ont. C.A.); *Dilollo, Re*, 2013 ONCA 550, 117 O.R. (3d) 81 (Ont. C.A.), at para. 40.

34 Accordingly, I would find that BMO was precluded from executing any remedy against the appellant or her property by virtue of the operation of the statutory stay of proceedings.

(4) Joint Tenancy

35 Having said the above, the appellant and the respondent held the real property as joint tenants. The judgment and execution in favour of BMO was also joint. As such, it would be open to BMO to realize the joint debt as against the respondent, as any interest of the respondent was unaffected by the stay. As Perell J. noted in *Royal & SunAlliance Insurance Co. v. Muir*, 2011 ONSC 2273, 9 R.P.R. (5th) 104 (Ont. S.C.J.), at para. 23: "Joint tenants have identical undivided interests in the same property. Each joint tenant holds '*totum tenet et nihil tenet*' or '*per mie et per tout*' which means each holds everything and yet holds nothing."

36 The characteristics of a joint tenancy are succinctly described in Jeffrey W. Lem and Rosemark Bocska, *Halsbury's Laws of Canada — Real Property*, 1st ed. (Markham, Ont.: LexisNexis Canada, 2012), at HRP-37:

> There are four essential attributes of a joint tenancy, known as the four unities. A joint tenancy requires:
>
> (1) Unity of Interest — the interest of each joint tenant must be equal in nature, extent and duration;
>
> (2) Unity of title — the interests must arise from the same act or instrument;
>
> (3) Unity of Time — the interests must vest at the same time; and
>
> (4) Unity of possession — the interests must relate to the same piece of property.

> A joint tenancy depends on the continuance of the unity of interest, title and possession. The unity of time of vesting only applies to the original creation of the tenancy and cannot be affected by any subsequent act.

37 The continuance of a joint tenancy depends on the maintenance of the unities of title, interest and possession; a destruction of any of these unities leads to a severance: *Power v. Grace*, [1932] O.R. 357 (Ont. C.A.), at p. 360. Severance of a joint tenancy may occur: through the unilateral action of a joint tenant on his or her own share, such as selling or encumbering it; through a mutual agreement between the co-owners to sever the joint-tenancy; or through any course of dealing sufficient to intimate that the interests of all were mutually treated as constituting a tenancy in common: Lem and Bocska, at HRP-41.

38 Severance also may occur on bankruptcy. This is because the bankrupt's property vests in the trustee in bankruptcy, and the four unities are therefore not maintained: see *Cameron Estate, Re*, 2011 ONSC 6471, 108 O.R. (3d) 117 (Ont. S.C.J.), at fn. 9.

39 Severance by execution is not so straightforward. Lem and Bocska describe such severance, at HRP-42:

> Seizure of property through lawful execution procedures will sever a joint tenancy. However the mere filing of the writ is insufficient; it must be acted upon. Thus, where the sheriff holds a writ of execution against a joint tenant but does not execute it prior to that tenant's death, the surviving joint tenant inherits the property free from the execution.

40 The appellant argues that the joint tenancy in the surplus was severed such that BMO could only recover from the respondent's 50% interest in the surplus. The appellant submits that the joint tenancy was severed in either one of two ways: as a result of BMO's efforts to collect its debt, or as a consequence of her consumer proposal. She particularly relies on *Power*, *supra* and *Muir*, *supra* in support of her position.

41 The respondent counters with the following: there was no severance; the application judge's determination that the joint tenancy was not severed was a finding of fact; and in any event, the parties' interests are subject to an accounting and the equities of the case. He relies in part on *Arnold Bros. Transport Ltd. v. Murphy*, 2013 MBQB 137, 34 R.P.R. (5th) 217 (Man. Q.B.), and on *Sirois v. Breton*, [1967] 2 O.R. 73 (Ont. Co. Ct.) in support of his position.

42 In *Power*, this court determined that while advertisement of a sale was sufficient to constitute a seizure that severed a joint tenancy, the mere filing of a writ of execution with the sheriff was insufficient. In *Maroukis v. Maroukis*, [1984] 2 S.C.R. 137 (S.C.C.), at p. 143, the Supreme Court stated that *Power* "stands for the proposition that, where a writ of *fieri facias* is delivered to the sheriff covering the interest of one joint tenant in real property and no further steps are taken in the execution process, the death of that joint tenant will pass the whole estate to the survivor free of execution."

43 In *Muir*, Perell J. concluded that the execution creditor took sufficient steps to execute the judgment, severing the joint tenancy. The steps included advertising the sale of property by the sheriff. Perell J. stated, at para. 26:

> Severance may occur when an execution creditor takes sufficient steps to execute the judgment against the debtor's interest in the property, although the filing of the writ of execution does not by itself result in a severance.

44 The decision of *Sirois*, relied upon by the respondent, also determined that the mere filing or delivery of a writ to the sheriff was insufficient to effect a severance of a joint tenancy. This is of little assistance on this appeal. Similarly, *Arnold Bros.* is a very different case. The key issues were whether the sale of property by a mortgagee or property division negotiations between separated spouses served to sever the joint tenancy. Neither was found to sever the joint tenancy, and the creditor, who held an execution in the name of only one of the joint tenants, was entitled to be paid from the pool of funds prior to any distribution to the joint tenants.

45 The facts in the case under appeal are quite different and indeed, rather unusual. Here, there could be no execution against the appellant because execution against her was stayed. However, the debt was joint, and BMO therefore was at

liberty to recover its debt against the respondent. The parties to the application and BMO appeared before the application judge and made submissions. The parties consented to, and the application judge granted, an order authorizing payment to BMO. The execution was completed and acted upon. In my view, in these circumstances, the joint tenancy was severed, and the payment to BMO could only be from the respondent's 50% share of the surplus.

46 I am also not persuaded of the respondent's other submissions. In my view, the application judge erred in law in ignoring the stay and in not finding a severance of the joint tenancy. Furthermore, in the face of a proposal, it is not open to the court to effect ostensible equitable readjustments to the allocation of the funds in issue. Lastly, I note that in oral argument, counsel for the appellant acknowledged that the respondent could seek redress under the provisions of the BIA however, I do not propose to address that potential eventuality.

D. Disposition

47 For these reasons, I would allow the appeal.

48 The issues raised were somewhat novel. In these circumstances, I would vacate the $4,500 costs order below in favour of the respondent and order both parties to bear their own costs of both the appeal and the application.

J. MacFarland J.A.:

I agree

G.R. Strathy J.A.:

I agree

Appeal allowed.

Footnotes

1 The counterpart provision for Division I provides to the same effect with necessary modifications: s. 66(1).)

TAB 10

2011 ONCA 34
Ontario Court of Appeal

C.I.F. Furniture Ltd., Re

2011 CarswellOnt 155, 2011 ONCA 34, 17 P.P.S.A.C. (3d) 47, 215 A.C.W.S. (3d) 1002, 273 O.A.C. 172, 348 D.L.R. (4th) 660, 73 C.B.R. (5th) 238

In the Matter of the Proposal of C.I.F. Furniture Limited

John Laskin, Robert P. Armstrong, R.G. Juriansz JJ.A.

Heard: October 28, 2010
Judgment: January 18, 2011
Docket: CA C51633

Proceedings: affirming *C.I.F. Furniture Ltd., Re* (2010), 63 C.B.R. (5th) 141, 2010 CarswellOnt 257, 2010 ONSC 505, 16 P.P.S.A.C. (3d) 9 (Ont. S.C.J. [Commercial List])

Counsel: David R. Byers, Maria Konyukhova, for Appellant, Kari Holdings Inc.
Steven L. Graff, for Respondents, VenGrowth Traditional Industries Fund Inc., VenGrowth II Investment Fund Inc.

Subject: Insolvency; Corporate and Commercial
Related Abridgment Classifications
Bankruptcy and insolvency
X Priorities of claims
X.1 Secured claims
X.1.b Forms of secured interests
X.1.b.xii Miscellaneous
Personal property security
IV Priority of security interest
IV.5 Subordination and postponement
Headnote
Bankruptcy and insolvency --- Priorities of claims — Secured claims — Forms of secured interests — Miscellaneous
Business and purchaser amalgamated — Vendor's holding company K Inc. provided vendor takeback financing secured by registered general security agreement — Bank became senior operating lender, guaranteed by two companies related to purchaser, VGT Inc. and VGI Inc. — VG Inc. provided funding through debentures registered by security interest, and other funding subordinate to K Inc. — Inter-creditor agreement made debenture agreement priority over K Inc.'s interest — Bank financing agreement gave K Inc.'s interest priority over bank, which had priority over VG Inc.'s interest — Business became insolvent and gained Bankruptcy and Insolvency Act protection — Hearing was held regarding priority — Motion judge held that VG Inc.'s security interest ranked in priority to K Inc.'s to extent of principal owing under debenture — VG Inc. did not sign any document ceding priority to K Inc. — Circular priority existed — Motion judge found that inter-creditor agreement subordinated K Inc.'s interest to VG Inc.'s interest, which did not change with agreement with bank — K Inc. appealed — Appeal dismissed — It would have been unreasonable to find that VG Inc. intended complete subordination, by 2008 K Inc.'s financing had already been spent and bank was providing new financing — As VG Inc. had big investment in corporation, it made sense for it to subordinate its interest to bank, but made no sense for it to subordinate its interest to K Inc. — Motion judge was correct in finding that complete subordination would confer windfall on K Inc., going from second to first priority.
Personal property security --- Priority of security interest — Subordination and postponement

Business and purchaser amalgamated — Vendor's holding company K Inc. provided vendor takeback financing secured by registered general security agreement — Bank became senior operating lender, guaranteed by two companies related to purchaser, VGT Inc. and VGI Inc. — VG Inc. provided funding through debentures registered by security interest, and other funding subordinate to K Inc. — Inter-creditor agreement made debenture agreement priority over K Inc.'s interest — Bank financing agreement gave K Inc.'s interest priority over bank, which had priority over VG Inc.'s interest — Business became insolvent and gained Bankruptcy and Insolvency Act protection — Hearing was held regarding priority — Motion judge held that VG Inc.'s security interest ranked in priority to K Inc.'s to extent of principal owing under debenture — Section 38 of Personal Property Security Act states that secured party may subordinate its interest in manner which can be enforced by third party, but only where secured creditor explicitly subordinated its interests against third party — Documentation did not show agreement of subordination between VG Inc. and bank in favour of K Inc. — Inter-creditor agreement could only have impact on determining extent to which money paid to business pursuant to senior debentures should be paid in favour of bank, and did not burden or benefit K — Complete subordination in favour of K Inc. had not occurred — K Inc. appealed — Appeal dismissed — Nothing in 2008 inter-creditor agreement showed intention on VG Inc.'s part to go to bottom of queue.

Table of Authorities

Statutes considered:

Personal Property Security Act, R.S.O. 1990, c. P.10

Generally — referred to

s. 38 — considered

APPEAL by creditor from judgment reported at *C.I.F. Furniture Ltd., Re* (2010), 63 C.B.R. (5th) 141, 2010 CarswellOnt 257, 2010 ONSC 505, 16 P.P.S.A.C. (3d) 9 (Ont. S.C.J. [Commercial List]), finding that creditor's interest had been subordinated.

John Laskin J.A.:

A. Introduction

1 This appeal concerns a priorities dispute between two secured creditors of an insolvent corporation. The insolvent corporation is C.I.F. Furniture Limited. The sale of its assets in a receivership did not generate enough money to satisfy its secured creditors. The two competing secured creditors are Kari Holdings, the holding company of the corporation's founders, Hans and Elizabeth Kamin, and The VenGrowth group of investment funds, which financed the purchase of Kari's shares in 2004.

2 Kari claims priority for a $1 million secured note received as vendor take back financing on the sale of its shares. VenGrowth claims priority for a $4.35 million senior subordinated debenture, used to finance the share purchase.

3 The case turns on whether a theory of complete subordination or a theory of partial subordination should be used to resolve the dispute. Under the complete subordination theory, Kari succeeds; under the partial subordination theory, VenGrowth succeeds.

4 The motion judge, Morawetz J., applied a partial subordination theory and so found in favour of VenGrowth. On its appeal, Kari submits that the motion judge erred in two ways. First, having regard to the factual and contractual matrix, the motion judge erred by not applying a complete subordination theory. Second, the motion judge erred in his application of s. 38 of the *Personal Property Security Act* (PPSA).

5 I agree with Morawetz J.'s reasons, which I have appended to this judgment. I add brief reasons of my own to address the arguments made in this court. I will first briefly review the financing agreements that led to this dispute, then the two competing theories, and finally why I agree with the motion judge and reject Kari's submissions.

B. The Financing Agreements

(i) Background

6 The Kamins started C.I.F. in the 1960s and incorporated their business in 1969. The corporation manufactured and supplied custom laboratory systems for laboratory and educational markets in North America.

7 In 2004, the Kamins retired and sold their shares in Kari. As part of the sale price, Kari took back a $1 million secured note, in turn secured by a general security agreement. The purchase of Kari's shares was financed by VenGrowth funds, which included $4.35 million secured by a senior subordinated debenture.

8 On November 30, 2004 Kari perfected its security interest in the note by registration under the PPSA. Two days later, on December 2, 2004, VenGrowth perfected its security interest in its senior debenture by registering its security interest under the PPSA. However, Kari's priority of registration under the PPSA was superceded by an inter-creditor agreement made at the end of December 2004.

(ii) The inter-creditor agreement, December 31, 2004

9 On December 31, 2004, the Bank of Nova Scotia (C.I.F.'s operating lender), Kari and VenGrowth entered into an inter-creditor agreement. They agreed on the following priorities among them, regardless of the order of registration under the PPSA:

- First, the Bank of Nova Scotia to the extent of its loans to C.I.F. (the bank was paid out in December 2006);
- Second, VenGrowth to the extent of its $4.35 million senior subordinated debenture;
- Third, Kari to the extent of its $1 million secured note;
- Fourth, VenGrowth to the extent of the additional loans it had advanced on the purchase of Kari's shares.

10 Thus, under the inter-creditor agreement, the VenGrowth senior debenture had priority over the Kari note, and the other VenGrowth debt was subordinate to the Kari note. The priority dispute between Kari and VenGrowth arose in 2008 when Comerica Bank agreed to provide secured financing to C.I.F.

(iii) The 2008 financing of C.I.F.

11 In 2008, Comerica Bank agreed to provide secured financing to C.I.F. The financing took the form of a revolving credit facility. To implement the financing, the parties signed several documents of which three are relevant to this appeal: a commitment letter signed by Comerica, a credit agreement between Comerica and C.I.F., and, most important, an inter-creditor agreement between Comerica and VenGrowth.

(a) The commitment letter

12 Comerica committed to provide a revolving credit facility to C.I.F. The commitment letter contains two provisions on which Kari relies in support of its appeal. First, the commitment letter expressly provides that the Kari $1 million note is "to rank ahead of the Bank." This provision reflects Kari's prior registration under the PPSA. Second, the commitment letter also required VenGrowth to provide Comerica with a $1 million guarantee, which would terminate on repayment of the Kari note. VenGrowth delivered this guarantee to Comerica.

(b) The credit agreement between Comerica and C.I.F.

13 Under this agreement, Comerica agreed to loan C.I.F. up to $2.5 million, secured by a general security agreement. Comerica perfected its security interest by registering a financing statement under the PPSA. At April 2009, the balance owing on Comerica's loan was approximately $1.3 million.

14 The credit agreement, like the commitment letter, recognized the Kari $1 million note as a "first priority lien" and Comerica's security interest as a "second priority lien." Moreover, Comerica's obligations under the agreement were conditional on, among other things, delivery to it of the VenGrowth guarantee.

(c) The 2008 inter-creditor agreement between Comerica and VenGrowth

15 Under this agreement, VenGrowth agreed to subordinate its security to Comerica's security.

C. The Dispute and the Two Competing Theories

(i) The dispute

16 The various financing agreements created what has been called a "circularity problem." The problem arises because there is no document in which all three parties -Comerica, Kari and VenGrowth - agreed among themselves on which security interest has priority. Instead, the key agreements were entered into by one or two but not all three parties. The three important agreements are the 2004 inter-creditor agreement to which Comerica was not a party, the 2008 creditor agreement to which neither Kari nor VenGrowth was a party, and the 2008 inter-creditor agreement to which Kari was not a party.

17 Under the 2004 inter-creditor agreement, the VenGrowth $4.35 million senior subordinated debenture has priority over the $1 million Kari note. Under the 2008 creditor agreement (and the 2008 commitment letter) the Kari $1 million note has priority over Comerica's security. Under the 2008 inter-creditor agreement, Comerica's security has priority over VenGrowth's security.

18 In short form, these three agreements provide:

- V ($4.35 million) ranks ahead of K ($1 million) - 2004 inter-creditor agreement
- K ($1 million) ranks ahead of C - 2008 creditor agreement
- C ranks ahead of V - 2008 inter-creditor agreement

19 How then is this priority dispute to be resolved? Both sides accept that it should be resolved by applying either a theory of complete subordination or a theory of partial subordination. The two theories are discussed in the reasons of the motion judge. I will review how the application of each theory affects the priorities among VenGrowth, Kari and Comerica.

(ii) Complete subordination

20 Under complete subordination, VenGrowth gives up its priority to Comerica: in other words, VenGrowth agrees not to assert a claim against the fund generated by the sale of C.I.F.'s assets until Comerica's claim is satisfied. But because Kari's security interest was registered under the PPSA before Comerica's security interest was registered, Comerica's claim cannot be satisfied until Kari's claim is paid. Kari therefore benefits indirectly from the agreement between VenGrowth and Comerica: Kari goes to first priority and VenGrowth falls to last priority. If the theory of complete subordination is applied, the priorities are:

- First, Kari;
- Second, Comerica;
- Third, VenGrowth

(iii) Partial subordination

21 Under partial subordination, VenGrowth gives the benefit of its first priority to Comerica. The amount of VenGrowth's claim - $4.35 million - is set aside out of the fund. That amount is used to satisfy Comerica's claim. If Comerica's claim is less than $4.35 million, it will get all of its claim paid and VenGrowth will get the balance. If Comerica's claim is greater than $4.35 million it will get the entire $4.35 million, but will receive the remainder of its claim only after Kari is paid.

22 Partial subordination has no effect on Kari. It remains in second priority after VenGrowth's first priority to the extent of $4.35 million. While under complete subordination, VenGrowth completely steps aside, under partial subordination VenGrowth steps aside only to the extent of Comerica's claim. Accordingly, if the theory of partial subordination is applied, the priorities are:

- First, Comerica, to a maximum of $4.35 million, and then VenGrowth, to a maximum of $4.35 million less Comerica's claim;
- Second, Kari;
- Third, Comerica for any claim in excess of $4.35 million;
- Fourth, VenGrowth for all of its remaining claims.

D. Discussion

23 The motion judge applied a theory of partial subordination for two main reasons. First, partial subordination produced an equitable result because it meant "Kari is neither burdened nor benefited by the 2008 Inter-Creditor Agreement," whereas complete subordination "would result in a windfall benefit to Kari at the expense of VenGrowth." Second, complete subordination could be justified only if supported by "clear and explicit language," and "such clear and explicit language is not found in the documents": see paras. 50-51 of the motion judge's reasons.

24 I turn to Kari's two submissions.

1. Having regard to the factual and contractual matrix, did the motion judge err by not applying complete subordination?

25 Whether complete or partial subordination should be applied turns on VenGrowth's intention, as disclosed by the various agreements. Do the agreements show that VenGrowth intended to wholly step aside and go to the bottom of the queue, or do they show that VenGrowth intended to step aside only to the extent of Comerica's interest?

26 Kari submits that the agreements, and the factual context in which they were signed, show that VenGrowth intended to go to the bottom of the queue. In making this submission, Kari relies mainly on five contractual provisions: the negative covenant in s. 8.2(b) of the Kari note, repeated in Kari's general security agreement; sections 4(d) and 11 of the 2004 inter-creditor agreement between Kari and VenGrowth; the 2008 credit agreement between Comerica and C.I.F.; the VenGrowth $1 million guarantee; and article 4 of the 2008 inter-creditor agreement between VenGrowth and Comerica. I do not think that singularly or collectively these five contractual provisions support Kari's position.

27 Section 8.2(b) of the Kari note contains a negative covenant precluding C.I.F. from granting additional encumbrances without Kari's consent. Kari says that the 2008 Comerica financing was done without its knowledge and thus breaches s. 8.2(b). Whether the 2008 financing amounts to a breach of this covenant need not be decided on this appeal. The important point is that VenGrowth was not a party to the note or to the financing in 2008. They therefore do not speak to VenGrowth's intentions; nor can they affect its priority position. Kari's corollary argument that VenGrowth arranged the financing is not supported in the record.

28 Sections 4(d) and 11 of the 2004 inter-creditor agreement stipulate that nothing in that agreement shall be construed as conferring any rights on a third party. Comerica is a third party, and therefore Kari argues that these provisions

precluded Comerica from taking the benefit of VenGrowth's priority. In my opinion, these provisions do not assist Kari. The priority given to Comerica was conferred not in this 2004 agreement, but in the 2008 inter-creditor agreement.

29 Nor does the 2008 credit agreement or the commitment letter assist Kari. As VenGrowth was not a party to this agreement, or to the commitment letter, their terms cannot demonstrate any intention on VenGrowth's part to go to the bottom of the queue. These documents do no more than acknowledge that the Kari note ranks ahead of Comerica's security interest. They do not establish any agreement between Kari and VenGrowth or between VenGrowth and Comerica that puts Kari in first priority.

30 Kari's strongest argument rests on the $1 million guarantee given by VenGrowth in connection with the Comerica financing. The guarantee stipulated that it would terminate on payment of the Kari note. Kari contends that this guarantee and its termination provision make no sense under partial subordination. Kari says that Comerica insisted on this guarantee because it did not have a subordination agreement with Kari. Functionally, Kari says that the guarantee puts it in first priority until it is paid.

31 I do not accept Kari's contention. The record is silent on why Comerica insisted on this guarantee. I agree with VenGrowth that banks ask for many pieces of security, some they need and some they may not need, to protect their position. It is just as plausible that Comerica asked for this guarantee because the guarantee made its interest more secure. Perhaps more important, there is no term in the guarantee from which one can say that by giving it VenGrowth intended to entirely cede its priority to Kari.

32 Finally, Kari relies on article 4 of the 2008 inter-creditor agreement between Comerica and VenGrowth. Article 4 states:

> **Priorities of Indebtedness; Subordination of Junior Creditor Indebtedness**
>
> Junior Creditor hereby subordinates, to the extent and in the manner provided in this Agreement, all of its rights of payment of all of the Junior Creditor Indebtedness to the full and final payment of all of the Senior Creditor Indebtedness and the termination of all financing arrangements and commitments between the Debtor, the Guarantor and the Senior Creditor.
>
> [Comerica is the Senior Creditor and VenGrowth is the Junior Creditor.]

33 Kari submits that article 4 means VenGrowth is not to be paid until Comerica is paid in full. However, because Kari's security interest was registered before Comerica's security interest, Comerica cannot be paid until Kari is paid. So, implicitly, by article 4, VenGrowth agreed to step aside completely.

34 Kari's submission does not give effect to the qualifying phrase in article 4, "to the extent and in the manner provided in this Agreement". Other provisions of the agreement show that VenGrowth did not intend to subordinate its entire priority position to Kari. For example, articles 2 and 3 state that no third party - and Kari is a third party under this agreement - may benefit from anything contained in the agreement. Article 7a explicitly recognizes that VenGrowth agrees to step aside only to the extent of Comerica's interest:

> Under any circumstances ... the Collateral shall be applied first to the Senior Creditor Indebtedness until all of the Senior Creditor Indebtedness has been fully and finally paid and all of the financing arrangements and commitments between the Debtor, the Guarantor and Senior Creditor have been terminated, and then to the Junior Creditor Indebtedness.

35 For these reasons, I do not agree that the various contractual provisions on which Kari relies argue for complete subordination. Moreover, there are several compelling reasons to apply partial subordination.

36 First, it would be unreasonable to find that VenGrowth intended complete subordination. By 2008, Kari's financing had already been spent. Comerica was providing new financing to keep the corporation afloat. As VenGrowth had a

big investment in the corporation, it made sense for VenGrowth to subordinate its interest to Comerica's interest. By contrast, it would have made no sense for VenGrowth to subordinate its interest to Kari's interest.

37 Second, as the motion judge pointed out, complete subordination would confer a windfall on Kari. It would go from second to first priority. Partial subordination leaves Kari in second position. It gets exactly what it bargained for in 2004.

38 Third, there is no document where VenGrowth agreed to subordinate its interest to Kari's interest. Thus, to give effect to Kari's position, one would have to infer that VenGrowth intended to go to the bottom of the queue. To draw that inference, one would expect some clear and unequivocal language in one of the documents, or at the very least, an exchange of correspondence between VenGrowth and Kari. Nothing of that sort exists.

39 I would not give effect to Kari's main ground of appeal.

2. Did the Motion Judge Err in His Application of s. 38 of the PPSA?

40 Section 38 of the PPSA states:

> A secured party may, in the security agreement or otherwise, subordinate the secured party's security interest to any other security interest and such subordination is effective according to its terms.

41 Section 38 recognizes that a secured party can, by agreement, subordinate its interest to other security interests in the same collateral, and a third party, not privy to that agreement, can rely on and enforce that subordination.

42 Kari argues that as a third party, it can rely on section 38 to enforce what it claims is the priority given to it by the 2008 credit agreement between Comerica and C.I.F., and the 2008 inter-creditor agreement between Comerica and VenGrowth. This argument simply recasts in the context of s. 38 of the PPSA, the main argument Kari advanced on this appeal, which I have already rejected. The motion judge did not give effect to Kari's argument under s. 38 and I would not do so either.

43 VenGrowth was not a party to the 2008 credit agreement, and therefore the parties to that agreement - Comerica and C.I.F. - could not by themselves subordinate the priority interest of the VenGrowth senior debenture to the Kari note. Further, as I have already discussed, nothing in the 2008 inter-creditor agreement shows an intention on VenGrowth's part to go to the bottom of the queue. I would not give effect to this ground of appeal.

E. Conclusion

44 The motion judge was correct in applying the theory of partial subordination to resolve the priority dispute between Kari and VenGrowth. I would therefore dismiss Kari's appeal, with costs fixed in the agreed upon amount of $17,500, inclusive of disbursements and applicable taxes.

Robert P. Armstrong J.A.:

I agree.

R.G. Juriansz J.A.:

I agree.

Appeal dismissed.

Appendix A

CITATION: C.I.F. Furniture Limited (Bankruptcy of), 2010 ONSC 505 **COURT FILE NO.:** 31-1194593 **DATE:** 20100121

SUPERIOR COURT OF JUSTICE - ONTARIO

(COMMERCIAL LIST - BANKRUPTCY AND INSOLVENCY) RE: IN THE MATTER OF THE PROPOSAL OF C.I.F. Furniture Limited, Applicants **BEFORE:** MORAWETZ J.

COUNSEL: Steven L. Graff and Sandra A. Vitorovich, for The VenGrowth Traditional

Industries Fund Inc. and the VenGrowth II Investment Fund Inc.

Paul G. Macdonald and Myriam M. Seers, for Kari Holdings Inc.

Endorsement

[1] This matter involves a priority dispute arising from the sale of assets of C.I.F. Furniture Limited ("CIF") for proceeds that are insufficient to satisfy the security interests of certain secured creditors. The dispute is between Kari Holdings Inc. ("Kari") and The VenGrowth Traditional Industries Fund Inc. ("VenGrowth Traditional") and The VenGrowth II Investment Fund Inc. ("VenGrowth Investment") and together with VenGrowth Traditional, ("VenGrowth").

[2] The parties are in agreement that a secondary issue, namely, whether the VenGrowth Security Interest only covered the principal amount owing to VenGrowth and does not include any payments of interest is moot and consequently need not be determined.

Summary of Facts

[3] CIF carried on business for the manufacture and supply of custom laboratory systems for markets across Canada and the United States.

[4] The business was established in the early 1960's by Mr. Hans J. Kamin and his spouse, Mrs. Elizabeth M. Kamin. In 1969, the Kamins incorporated CIF to continue the business.

[5] Upon retiring in 2004, the Kamins sold CIF to an affiliate of VenGrowth (the "Purchaser") pursuant to a share purchase agreement dated November 23, 2004. On the closing date (December 7, 2004), the Purchaser and CIF amalgamated and continued as CIF. The purchase price was $7,057,060. At the time of closing, VenGrowth indirectly held 53% of the issued and outstanding shares in CIF. At the time of the motion, VenGrowth was CIF's 95% majority shareholder and a substantial secured creditor.

[6] As part of the share purchase, Kari (the holding company of Mr. and Mrs. Kamin) provided the Purchaser with $1,000,000 in vendor take-back ("VTB") financing (the "Kari Note"), secured by a general security agreement dated December 1, 2004 (the "Kari GSA"), for which a financing statement was registered under the *Personal Property Security Act (Ontario)* ("PPSA") on November 30, 2004 (the "Kari Security Interest").

[7] VenGrowth also financed the share purchase by advancing the Purchaser the principal amount of $4,350,000, secured by a senior subordinated debenture dated December 2, 2004 (the "VenGrowth Senior Debenture") for which a financing statement was registered under the PPSA by VenGrowth on December 2, 2004 (the "VenGrowth Security Interest").

[8] VenGrowth also advanced significant additional capital to CIF on a junior and/or subordinated basis to Kari, with certain of these additional advances being made in December 2004 to finance the share purchase.

[9] Following the share purchase, Bank of Nova Scotia ("BNS") agreed to be the operating lender of CIF. All parties funding the share purchase recognized and agreed that BNS was in priority to all other secured creditors. CIF repaid its obligations to BNS in December 2006.

[10] Subsequently, Comerica Bank ("Comerica") became the operating lender. Pursuant to a credit agreement between Comerica and CIF dated November 28, 2008 (the "Comerica Credit Agreement"), Comerica provided CIF with a revolving credit facility to a maximum of $2,500,000. The facility granted pursuant to the Comerica Credit Agreement was secured by a security agreement dated November 28, 2008 (the "Comerica Security"), for which a financing statement was registered under the PPSA on November 13, 2008 (the "Comerica Security Interest").

[11] Both VenGrowth Traditional and VenGrowth Investment guaranteed a portion of the Comerica facility pursuant to the following guarantees (the "VenGrowth Guarantees"):

(a) a guarantee dated November 28, 2008 granted by VenGrowth Traditional in favour of Comerica and limited to $462,571; and

(b) a guarantee dated November 28, 2008 granted by VenGrowth Investment in favour of Comerica limited to $537,429.

[12] VenGrowth submits that the guarantee of VenGrowth Traditional was amended and restated by a guarantee dated April 29, 2009 limited to $601,342 and that the guarantee of VenGrowth Investment was amended and restated by a guarantee also dated April 23, 2009 limited to $698,658.

[13] The PPSA registrations are filed in the following order of priority:

(i) Kari - November 30, 2004;

(ii) VenGrowth - December 2, 2004;

(iii) Comerica - November 13, 2008.

[14] In 2004, CIF, Kari and VenGrowth entered into the following priorities agreements:

(a) an inter-creditor agreement dated December 3, 2004 (the "2004 Inter-Creditor Agreement");

(b) a subordination agreement dated December 7, 2004 (the "2004 Subordination Agreement"); and

(c) separate postponement and subordination agreements in favour of Kari from each of VenGrowth Traditional, VenGrowth Investment, as well as various other CIF creditors, namely, Cinitel Corp., Fallbrook Holdings Limited ("Fallbrook"), Mr. Bruce Andrew, Mr. Stephen Dulong and 1639662 Ontario Inc. ("Holdco").

[15] The 2004 Inter-Creditor Agreement granted the VenGrowth Security Interest, to the extent of the debt under the VenGrowth Senior Debenture, priority over the Kari Security Interest.

[16] Under the 2004 Subordination Agreement, VenGrowth Investment and VenGrowth Traditional agreed to postpone and subordinate their security interests, pursuant to their respective security, to the Kari Security Interest, except that neither of VenGrowth Investment or VenGrowth Traditional postponed or subordinated the VenGrowth Security Interest. As stated by counsel to VenGrowth, "in other words, all advances made by VenGrowth, other than the VenGrowth Senior Debenture, were subordinated to Kari".

[17] Comerica was not a party to the 2004 Inter-Creditor Agreement.

[18] In 2008, CIF secured financing from Comerica. The terms of the financing were set out in a commitment letter dated June 5, 2008 pursuant to which Comerica committed to provide a $2.5 million revolving credit facility to CIF (the "Commitment Letter").

[19] The Commitment Letter expressly states that the Kari Security Interest will rank in priority to the Comerica Security Interest and that the VenGrowth Security Interest will be subordinated to the Comerica Security Interest.

[20] The Comerica Credit Agreement recognizes the Kari Security Interest as a first priority lien and that the Comerica Security Interest as a second priority lien.

[21] The Comerica Credit Agreement included the Kari Note as a "Permitted Debt", the Kari Security Interest as a "Permitted Lien" and required a subordination of the VenGrowth Security Interest but not the Kari Security Interest to the Comerica Security Interest.

[22] VenGrowth was not a party to either the Commitment Letter or the Comerica Credit Agreement.

[23] Also, on November 28, 2008, CIF provided Comerica with the Comerica Security Agreement.

[24] The Comerica Security Interest also provides that each of the VenGrowth Guarantees will terminate upon the payment in full of the Kari Note.

[25] On November 28, 2008, VenGrowth and Comerica entered into an inter-creditor agreement whereby VenGrowth agreed to fully subordinate the VenGrowth Security Interest to the Comerica Security Interest (the "2008 Inter-Creditor Agreement").

[26] Kari did not know about the Comerica Security Interest until CIF served it with motion materials in these proceedings on April 21, 2009.

[27] CIF is insolvent and on April 21, 2009 it filed a Notice of Intention to Make a Proposal under the *Bankruptcy and Insolvency Act* (the "BIA").

[28] On April 29, 2009, A. Farber & Partners Inc. (the "Interim Receiver") was appointed interim receiver of CIF and by order dated May 15, 2009, the Interim Receiver was authorized to market and sell the assets.

[29] There is no inter-creditor agreement to which Comerica, VenGrowth and Kari are all parties that set out the priorities among them. There is no inter-creditor agreement or subordination agreement in which VenGrowth subordinates or postpones the VenGrowth Security Interest to the Kari Security Interest.

[30] Kari and Comerica have not entered into any agreement between themselves which governs the relative priorities of the Kari Security Interest and the Comerica Security Interest.

Analysis

[31] Kari submits that the Kari Security Interest ranks in priority to the Comerica Security Interest and the VenGrowth Security Interest by operation of the Commitment Letter, the Comerica Credit Agreement, the Comerica Security Agreement, the Comerica Security Interest and the 2008 Inter-Creditor Agreement (collectively the "Comerica Agreements") and s. 38 of the PPSA.

[32] Counsel to Kari submits that an objective interpretation of the relevant documents demonstrates that both VenGrowth and Comerica intended that, as a result of the Comerica Agreements, the Kari Security Interest would rank in priority to the Comerica Security Interest and, therefore, the VenGrowth Security Interest. Counsel to Kari submits that this position is supported by the repeated references in the Commitment Letter and the Comerica Credit Agreement to the first priority position of the Kari Security Interest and VenGrowth's voluntary agreement to step out of the priority queue and back in behind Comerica.

[33] There is, in my view, a fundamental weakness in this argument. VenGrowth is not party to either the Commitment Letter or the Comerica Credit Agreement. These are contractual agreements between CIF and Comerica. Although VenGrowth is the substantial controlling shareholder of CIF, this does not mean that the contractual agreements of CIF are agreements that bind VenGrowth. There is no stated intention in any document that establishes that VenGrowth intended to cede its priority position in all respects to the Kari Security Interest.

[34] When read together, the 2004 Inter-Creditor Agreement and the 2008 Inter-Creditor Agreement create a circularity issue as between Kari, VenGrowth and Comerica.

[35] Professor Wood commented on this issue in "*Circular Priorities in Secured Transactions Law*" at pages 7 - 8:

> The real controversy concerns the proper interpretation of the subordination agreement. In the United States, the issue is framed as whether SP1 intended a complete subordination of its claim or only a partial subordination. A **complete subordination** occurs if the subordination agreement is interpreted as an agreement by SP1 not to assert its claim against the collateral until SP3's claim is satisfied. It does not involve an agreement by SP1 to turn over the benefit of its priority to SP3. Rather, it is essentially an agreement by SP1 to step aside and not assert its claim until SP3's claim has been satisfied. On this view, the competition is resolved by giving first priority to SP2, second priority to SP3, and third priority to SP1. SP2 is the indirect beneficiary of the subordination agreement because SP3 cannot satisfy its claim until the claim of SP2 is fully satisfied.
>
> Under the competing **partial subordination theory**, a subordination agreement is interpreted as an agreement under which SP1 agrees to turn over the benefit of its priority to SP3. The priorities are therefore resolved in the following manner. First, the amount of SP1's claim is set aside out of the fund. Second, the fund is used to satisfy SP3's claim. If there is anything left over, it is paid to SP1. Third, SP2's claim is satisfied out of the fund. Fourth, any remaining balance is distributed to SP3 and then to SP1.

[36] The duelling approaches were also the subject of commentary by Professors Cumming, Walsh and Wood in *Personal Property Security Law* where the authors explained as follows:

> The priority competition is resolved by setting aside the amount of SP1's claim. From this fund, SP3's claim is satisfied. If a surplus remains after SP3's claim is satisfied, it is paid over to SP1. SP2's claim would next be satisfied from the remaining funds. If there is anything left, it is then distributed to SP3, then SP1. In other words, the subordination agreement between SP1 and SP3 is effective only as between those parties, and has no effect on the relative priority of SP2.
>
> Most subordination agreements provide for a postponement of the subordinating creditor's claim. Under a "step-aside" agreement, a secured party may instead agree that it will not make a claim in respect of a subordinated debt until the benefiting creditor is paid in full. If this form of agreement is used, there is a greater likelihood that it will have the effect of elevating the priority of an intervening party. In the above scenario, SP1 would renounced its claim until SP3 is paid in full. This would seem to have the effect of placing SP1 at the end of the queue, with the result that SP2 would obtain first priority followed by SP3.

[37] At issue is whether the circularity problem should be resolved in favour of VenGrowth or Kari. A resolution in favour of VenGrowth would require the application of the partial subordination theory. A resolution in favour of Kari would require the application of the complete subordination theory.

[38] In considering which of these two approaches should be applied in these circumstances, in my view, it is necessary to consider the impact of agreements to which VenGrowth, Kari and Comerica are parties.

[39] As a result of the 2004 Inter-Creditor Agreement, the Kari Security Interest is subordinate to the VenGrowth Security Interest. The issue is whether this situation changed as a result of the Comerica Agreements. In my view, it has not.

[40] VenGrowth entered into the 2008 Inter-Creditor Agreement with Comerica, the result of which is that VenGrowth subordinated payment under the VenGrowth Senior Debenture to Comerica. It does not follow that VenGrowth intended that its entire priority position would be subordinated to that of Kari.

[41] The Commitment Letter states that the VTB from Kari in the amount of $1,000,000 is to rank ahead of Comerica. This statement, at most, provides the understanding on the part of Comerica that Kari's interest ranks ahead of Comerica's position, but there is no agreement or acknowledgement by VenGrowth that the Kari Security Interest ranks ahead of the VenGrowth Security Interest.

[42] Further, the Comerica Credit Agreement does not recognize or state that the Kari Security Interest shall constitute a priority claim to the VenGrowth Security Interest.

[43] Section 38 of the PPSA provides that a secured party may, in the security agreement or otherwise, subordinate its security interest to any other security interest and the subordination is effective according to its terms and a third party who is not privy to the security agreement or other agreement which contains the subordination clause can enforce it.

[44] Counsel to VenGrowth submits that s. 38 applies only in instances where the secured creditor itself subordinates, explicitly or implicitly, its security interest vis-à-vis a third party. Counsel cites *Sun Life Assurance Co. of Canada v. Royal Bank*, 37 C.B.R. (4th) 169 in support of this submission. I agree with this position.

[45] In this case, the Commitment Letter and the Comerica Credit Agreement are the documents that Kari submits evidences the intention of VenGrowth to subordinate the VenGrowth Security Interest to the Kari Security Interest. I am in agreement with the submission of counsel to VenGrowth that evidence of an understanding involving Comerica and CIF in respect of the priority between Kari and Comerica does not establish a subordination agreement as between VenGrowth and Comerica in favour of Kari.

[46] The only documents in the Comerica Agreement to which VenGrowth is a party are the 2008 Inter-Creditor and the VenGrowth Guarantees. These documents, do not, in my view, result either clearly or explicitly, in a subordination of the VenGrowth Security Interest to the Kari Security Interest.

[47] Counsel to VenGrowth submits that the effect of the 2008 Inter-Creditor Agreement is to provide that a portion of any fund paid by CIF to VenGrowth under the VenGrowth Senior Debenture would be paid by VenGrowth to Comerica and any funds available for payment by CIF after repayment of the amount owing under the VenGrowth Senior Debenture would be paid to Kari next in satisfaction of the indebtedness under the Kari Note. A proper interpretation is that under the 2008 Inter-Creditor Agreement, any payments received by VenGrowth from CIF pursuant to the VenGrowth Senior Debenture (up to a maximum of the VenGrowth Indebtedness) would be shared as between VenGrowth and Comerica as follows:

> (a) first, payment would be made to Comerica in satisfaction of the Comerica indebtedness; and
>
> (b) secondly, the remaining funds, of the total of the VenGrowth Senior Debenture (inclusive of amounts paid in sub (a)), would be payable to VenGrowth in satisfaction of the VenGrowth indebtedness. The total distributed under both sub (a) and sub (b) would not be greater than the VenGrowth indebtedness.

[48] Counsel to VenGrowth submits that this interpretation is consistent with the analysis set out by Grant Gilmore in *Security Interests in Personal Property*, where he discusses a situation with three creditors, A, B, and C where A and C enter into a subordination agreement, the secured assets are sold and there are insufficient funds to satisfy the claims of all three creditors. The ensuing distribution was explained by Gilmore as follows:

> There is a comforting unanimity, among courts and commentators, on the proper distribution of funds:
>
> 1. Set aside from the fund the amount of A' claim.
>
> 2. Pay the amount set aside to
>
> a) C, to the amount of his claim;
>
> b) A, to the extent of any balance remaining after C's claim is satisfied.
>
> 3. Pay B the amount of the fund remaining after A's claim has been set aside.
>
> 4. If any balance remains in the fund after A's claim has been set aside and B's claim has been satisfied, distribute the balance to
>
> a) C,
>
> b) A.
>
> Thus C, by virtue of the subordination agreement, is paid first, but only to the amount of A's claim, to which B was in any event junior. B receives what he had expected to receive: the fund less A's prior claim. If A's claim is smaller than C's, C will collect the balance of his claim in his own right, only after B has been paid in full. A, the subordinator, receives nothing until B and C have been paid except to the extent that his claim, entitled to first priority, exceeds the amount of C's claim, which under his agreement, is to be paid first.

[49] Counsel to VenGrowth also referenced the decision of the Newfoundland and Labrador Court of Appeal in *Hickman Equipment (1985) Ltd., Re*, 2006 CarswellNfld 245, leave to appeal to Supreme Court of Canada refused, [2006] S.C.C.A. No. 462. Counsel to VenGrowth submitted in their factum as follows:

> 42. The Newfoundland and Labrador Supreme Court was recently asked to decide whether by virtue of a subordination agreement between party A and C: (i) C moved up to stand in the place of A and thereby gains priority over B; or (ii) while A ranks in priority behind C, nonetheless B retains priority over C.
>
> 43. Quoting several texts, including the passage from Gilmore above, and Canadian jurisprudence, the Appellant in Hickman argued that "the ranking of the claims and distribution of proceeds is determined apart from the operation of the subordination agreement" with the subordination agreement applying to determine the extent of the share of the distribution that should be paid to the party in whose favour the subordination was granted. Moreover, a creditor in second position (such as Kari) should not receive the benefit of a subordination agreement to which it is not a party and on which the parties to the subordination agreement intended the second position creditor to rely.
>
> 44. The central proposition of the case of the Appellants in *Hickman* [and the position advanced by VenGrowth herein] was:
>
> > Where a subordination is enforced by the benefiting creditor [RBC] for its benefit, the amount secured by the subordinated security interest simply goes toward satisfying in whole or in part

> two claims as opposed to one: the benefiting creditor's claim [RBC's] and the subordinated creditor's claim [CIBC's]. The benefiting creditor shall receive payment in full of its claim, before the subordinated creditor receives any payment on the subordinated debt. Where there is an intervening security interest [GMAC], the result is equitable, because the intervening creditor will receive what it expected to receive, the fund less the amount secured by the higher ranking subordinated security interest. Otherwise, the intervening creditor receives a windfall and the statutory rights bestowed on the subordinating creditor to subordinate its security interest and the benefiting creditor to enforce the subordination for its benefit are thwarted.

The court, finding the arguments set out by the Appellant persuasive, adopted the Appellant's reasoning.

[50] I am in agreement with the submissions of counsel to VenGrowth. The 2008 Inter-Creditor Agreement can only have an impact on determining the extent to which the monies paid to CIF pursuant to the VenGrowth Senior Debenture should be paid in favour of Comerica. In this manner, Kari is neither burdened nor benefited by the 2008 Inter-Creditor Agreement. On the other hand, the argument put forward by counsel to Kari would result in a windfall benefit to Kari at the expense of VenGrowth. The result preferred by VenGrowth produces, in my view, an equitable result.

[51] It seems to me that the result preferred by Kari, namely, that of a complete subordination, could only be justified if there is clear and explicit language that would result in a complete subordination agreement. Such clear and explicit language is not found in the documents.

Disposition

[52] In this case, in the 2008 Inter-Creditor Agreement, VenGrowth subordinates only to and for the benefit of Comerica, while at the same time preserving its priority position as against third parties. In my view, it is especially telling that s. 2 of the 2008 Inter-Creditor Agreement provides that all agreements and representations are solely for the benefit of the creditors (VenGrowth and Comerica) and that no other parties are intended to be benefited in any way by the 2008 Inter-Creditor Agreement. In the face of such explicit language, it seems to me that it cannot be said that there was the intention on the part of VenGrowth to effect a complete subordination in favour of Kari. Rather, the effect of the 2008 Inter-Creditor Agreement is that, with all the priorities remaining the same, VenGrowth is to set aside a portion of the funds it receives in trust to be paid to Comerica pursuant to the 2008 Inter-Creditor Agreement and that it will not receive its priority payment until Comerica has been paid in full from payments it receives in its position.

[53] In the result, I find that the VenGrowth Security Interest is in priority to the Kari Security Interest to the extent of principal owing under the VenGrowth Senior Debenture. The issue of whether priority extends to interest need not be determined.

[54] VenGrowth is to have its costs of this motion, as agreed, in the amount of $42,500 inclusive of disbursements and GST.

End of Document

IN THE MATTER OF THE PROPOSAL OF 1482241 ONTARIO LIMITED, OF THE CITY OF TORONTO, IN THE PROVINCE OF ONTARIO

Court File No. 31-2303814
Estate No. 31-2303814

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST
(IN BANKRUPTCY AND INSOLVENCY)

Proceedings commenced at Toronto

BRIEF OF AUTHORITIES OF THE PROPOSAL TRUSTEE
(motion returnable March 16, 2018)

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