Court File No.: CV-18-598657-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

DONALD DAL BIANCO

Applicant

- and -

DEEM MANAGEMENT SERVICES LIMITED and THE UPTOWN INC.

Respondents

APPLICATION UNDER Section 243(1) of the *Bankruptcy and Insolvency Act* and Section 101 of the *Courts of Justice Act*

RECEIVER'S BRIEF OF AUTHORITIES

(motion for directions regarding the third mortgage and other relief, returnable November 21, 2019)

October 30, 2019

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TO: THE SERVICE LIST

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TAB 1

Royal Bank of Canada *Appellant*

v.

North American Life Assurance Company and Balvir Singh Ramgotra *Respondents*

INDEXED AS: ROYAL BANK OF CANADA *v.* NORTH AMERICAN LIFE ASSURANCE CO.

File No.: 24316.

1995: November 8; 1996: February 22.

Present: La Forest, L'Heureux-Dubé, Sopinka, Gonthier, McLachlin, Iacobucci and Major JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR SASKATCHEWAN

Bankruptcy — Settlement of funds — RRSP transferred in good faith to RRIF (insurance annuity) for benefit of third party — Settlements made up to five years prior to bankruptcy void against trustee in bankruptcy if interest of settlor in property did not pass on settlement — RRIFs normally exempt from claims of bankrupt's creditors — Bankruptcy declared within five years of transfer — Whether transfer to RRIF a settlement — If so, whether or not settlement void against trustee in bankruptcy — If so, whether or not funds in RRIF available to satisfy claims of creditors notwithstanding exempt status of RRIF — Bankruptcy and Insolvency Act, R.S.C., 1985, c. B-3, ss. 67, 91 — The Saskatchewan Insurance Act, R.S.S. 1978, c. S-26, ss. 2(kk), 158.

In June 1990, respondent Ramgotra transferred the funds from his RRSPs into a RRIF managed by respondent insurance company. His wife was designated beneficiary under the RRIF and payments began that August. Circumstances related to relocation of respondent's medical practice led him to make an assignment into bankruptcy in February 1992. On his absolute discharge from bankruptcy in January 1993, his only assets were his clothing and household contents, and the RRIF. While the RRSPs would have been subject to his creditors' claims, the RRIF constituted a life insurance annuity and was therefore exempt from their claims on the basis of s. 67(1)(*b*) (property divisible among creditors on bankruptcy does not include property exempt from seizure under provincial law) of the *Bankruptcy and*

Banque Royale du Canada *Appelante*

c.

La Nord-Américaine, compagnie d'assurance-vie et Balvir Singh Ramgotra *Intimés*

RÉPERTORIÉ: BANQUE ROYALE DU CANADA *c.* NORD-AMÉRICAINE, CIE D'ASSURANCE-VIE

N° du greffe: 24316.

1995: 8 novembre; 1996: 22 février.

Présents: Les juges La Forest, L'Heureux-Dubé, Sopinka, Gonthier, McLachlin, Iacobucci et Major.

EN APPEL DE LA COUR D'APPEL DE LA SASKATCHEWAN

Faillite — Disposition de fonds — REER transférés de bonne foi dans un FERR (rente d'assurance) au profit d'un tiers — Inopposabilité au syndic des dispositions faites au cours des cinq ans qui précèdent la faillite si les intérêts du disposant dans les biens n'ont pas cessé lorsque fut faite la disposition — FERR normalement à l'abri des réclamations des créanciers de la faillite — Cession de biens dans les cinq ans du transfert — Le transfert dans le FERR est-il une disposition? — Dans l'affirmative, la disposition est-elle inopposable au syndic? — Si oui, les fonds du FERR peuvent-ils servir à régler les réclamations des créanciers en dépit de l'exemption dont bénéficie le FERR? — Loi sur la faillite et l'insolvabilité, L.R.C. (1985), ch. B-3, art. 67, 91 — The Saskatchewan Insurance Act, R.S.S. 1978, ch. S-26, art. 2kk), 158.

En juin 1990, l'intimé Ramgotra a transféré les fonds de ses REER dans un FERR géré par la compagnie d'assurance intimée. Son épouse a été désignée bénéficiaire du FERR et les paiements ont commencé en août de la même année. Par suite d'événements liés à l'exercice de sa profession de médecin, l'intimé a fait cession de ses biens en février 1992. Lorsqu'il a obtenu sa libération absolue, en janvier 1993, il n'a conservé pour tous biens que ses vêtements, le contenu de sa maison et le FERR. Alors que les REER auraient été touchés par les réclamations de ses créanciers, le FERR, parce qu'il constituait une rente d'assurance-vie, était à l'abri de leurs réclamations par l'effet conjugué de l'al. 67(1)*b*) (les biens constituant le patrimoine attribué aux créanciers ne comprennent pas les biens qui sont exempts de saisie

Insolvency Act (*BIA*), when read in conjunction with ss. 2(kk)(vii) (life insurance includes annuities) and 158(2) (life insurance money and contract is exempt from seisure where a spouse is designated beneficiary) of *The Saskatchewan Insurance Act*. The trustee in bankruptcy applied for a declaration that the transfer of the RRSP funds into the RRIF was void, pursuant to s. 91(2) of the *BIA*, which declares, in part, that "settlements" made one to five years prior to bankruptcy are void against the trustee if "the interest of the settlor in the property did not pass" upon settlement. The trustee's application was dismissed at trial because the transfer of the RRSP funds into the RRIF had been made in good faith and not for the purpose of defeating the claims of his creditors. Appellant's appeal to the Saskatchewan Court of Appeal was dismissed. The issues here were: (1) whether the transaction was a settlement within the meaning of s. 91 *BIA*; (2) if so, whether the settlement was void against the trustee in bankruptcy under the second branch of s. 91(2); and, (3) if so, whether the funds in the RRIF were available to satisfy the claims of the creditors despite the RRIF's exempt status under s. 67(1)(*b*).

Held: The appeal should be dismissed.

When respondent Ramgotra transferred the funds from his two RRSPs into an RRIF designating his wife as beneficiary, the funds became exempt from execution or seizure by reason of s. 67(1)(*b*) *BIA*, when read in conjunction with ss. 2(kk)(vii) and 158(2) of *The Saskatchewan Insurance Act*. Even if the beneficiary designation was a settlement within s. 91 *BIA*, and was void against the trustee in bankruptcy pursuant to the second branch of s. 91(2), the RRIF remained exempt from the claims of respondent Ramgotra's creditors and, in particular, the appellant.

Jurisprudential consensus has emerged that the designation of a beneficiary under a life insurance policy constitutes a s. 91 settlement. Respondent Ramgotra effected a settlement triggering s. 91.

Sections 67(1)(*b*) and 91 *BIA* are not in conflict. The two provisions can be reconciled by giving effect to their distinct terms, and by recognizing their distinct roles in bankruptcy. Section 91 dictates that certain settled property will fall back into the estate of the bankrupt in the possession of the trustee, while s. 67 is

sous le régime de lois provinciales) de la *Loi sur la faillite et l'insolvabilité* (*LFI*) ainsi que du sous-al. 2kk)(vii) (assurance-vie s'entend également d'une rente) et du par. 158(2) (les sommes assurées et le contrat d'assurance-vie sont exempts de saisie lorsque le conjoint est désigné bénéficiaire) de *The Saskatchewan Insurance Act*. Le syndic a demandé un jugement déclaratoire portant que, en vertu du par. 91(2) *LFI*, le transfert des fonds des REER dans le FERR était nul. Ce paragraphe énonce notamment que sont inopposables au syndic les «dispositions» de biens faites au cours des cinq ans qui précèdent la faillite si «les intérêts du disposant dans ces biens n'ont pas cessé» lorsque fut faite la disposition. Au procès, la demande du syndic a été rejetée pour le motif que l'intimé avait agi de bonne foi en transférant les fonds des REER dans le FERR et non dans le but de frustrer les réclamations de ses créanciers. L'appel à la Cour d'appel de la Saskatchewan interjeté par l'appelante a lui aussi été rejeté. Les questions en litige sont les suivantes: (1) L'opération est-elle une disposition au sens de l'art. 91 *LFI*? (2) Dans l'affirmative, la disposition est-elle inopposable au syndic en vertu du second volet du par. 91(2)? (3) Si oui, les fonds du FERR peuvent-ils servir à régler les réclamations des créanciers en dépit de l'exemption dont bénéficie le FERR en vertu de l'al. 67(1)*b*)?

Arrêt: Le pourvoi est rejeté.

Lorsque l'intimé Ramgotra a transféré les fonds de ses deux REER dans un FERR dont son épouse a été désignée bénéficiaire, ces sommes sont devenues exemptes d'exécution ou de saisie par l'effet conjugué de l'al. 67(1)*b*) *LFI* ainsi que du sous-al. 2kk)(vii) et du par. 158(2) de *The Saskatchewan Insurance Act*. Même si la désignation d'un bénéficiaire était une disposition au sens de l'art. 91 *LFI*, et qu'elle était inopposable au syndic conformément au second volet du par. 91(2) *LFI*, le FERR est demeuré à l'abri des réclamations des créanciers de l'intimé Ramgotra et, en particulier, de celle de l'appelante.

Il s'est établi, dans la jurisprudence, un consensus que la désignation d'un bénéficiaire aux termes d'une police d'assurance constitue une disposition au sens de l'art. 91. L'intimé Ramgotra a fait une disposition qui a déclenché l'application de l'art. 91.

Il n'y a pas incompatibilité entre l'al. 67(1)*b*) et l'art. 91 *LFI*. Il est possible de concilier les deux articles en donnant effet à leur texte respectif et en reconnaissant les rôles distincts qu'ils jouent en matière de faillite. Alors que l'art. 91 indique que certains biens ayant fait l'objet d'une disposition reviennent dans le patrimoine

directed at the exercise of administrative powers over the estate by the trustee. Where a settlement is void against the trustee under s. 91, then in normal circumstances, the trustee is empowered to administer the settled asset and use it to satisfy the claims of creditors. However, in the special case where the asset is exempt under s. 67(1)(*b*), then the trustee is prohibited from exercising his or her distribution powers because the asset is not subject to division among creditors.

Respondent Ramgotra's property interest in the RRIF passed to and vested in the trustee in bankruptcy by operation of s. 71(2) *BIA*. The future contingent interest of the designated beneficiary under the RRIF was not captured by s. 71(2), since it had been settled on the designated beneficiary prior to bankruptcy. The trustee in bankruptcy could apply to have this settlement set aside under s. 91(2) *BIA*.

The effect of s. 91 is to render certain settlements void against the trustee in bankruptcy. A life insurance policy, however, is rendered exempt under s. 67(1)(*b*) by the designation of a beneficiary and this status continues so long as the designation is "in effect" according to s. 158(2) of *The Saskatchewan Insurance Act*. The fact that a beneficiary designation is void against the trustee under federal legislation does not necessarily result in its no longer having effect *vis-à-vis* the claims of creditors under the provincial legislation which s. 67(1)(*b*) incorporates.

It was not necessary to decide whether respondent Ramgotra effected a void settlement under the second branch of s. 91(2) when he designated his wife as beneficiary of his RRIF. Even if the settlement were void against the trustee in bankruptcy, that would not allow the trustee to use the funds in the RRIF to satisfy the claims of creditors such as the appellant bank. The RRIF is an exempt asset pursuant to the provincial legislation incorporated into s. 67(1)(*b*): it is not property which is divisible among creditors. Given this, even if Mrs. Ramgotra's future contingent interest in the RRIF had passed into the possession of the trustee through the application of s. 91(2), the RRIF was property "incapable of realization" by the trustee pursuant to s. 40(1) *BIA*. Therefore, the trustee was obliged to return it to respondent Ramgotra prior to applying for his discharge. Regardless of whether or not respondent Ramgotra's settlement was void against the trustee, the

du failli en la possession du syndic, l'art. 67 porte sur les pouvoirs de nature administrative exercés par ce dernier sur le patrimoine. Lorsque, en vertu de l'art. 91, une disposition est inopposable au syndic, celui-ci est, dans des circonstances normales, habilité à administrer le bien ayant fait l'objet de la disposition et à l'appliquer au règlement des réclamations des créanciers. Cependant, dans les cas particuliers où il s'agit d'un bien exempt en vertu de l'al. 67(1)*b*), le syndic ne peut alors exercer ses pouvoirs de distribution car le bien ne fait pas partie du patrimoine attribué aux créanciers.

L'intérêt de propriété de l'intimé Ramgotra dans le FERR est passé et a été dévolu au syndic en application du par. 71(2) *LFI*. L'intérêt futur et éventuel de la bénéficiaire désignée aux termes du FERR n'est pas tombé dans le champ d'application du par. 71(2), puisque la disposition de ce bien en faveur de la bénéficiaire désignée avait eu lieu avant la faillite. Il était loisible au syndic de demander l'annulation de cette disposition en vertu du par. 91(2) *LFI*.

L'article 91 a pour effet de rendre certaines dispositions inopposables au syndic. Toutefois, lorsqu'il s'agit d'une police d'assurance-vie, c'est la désignation d'un bénéficiaire qui la rend exempte en vertu de l'al. 67(1)*b*). Aux termes du par. 158(2) de *The Saskatchewan Insurance Act*, la police d'assurance-vie conserve sa qualité de bien exempt tant que la désignation est «en vigueur». Le fait qu'une désignation de bénéficiaire soit inopposable au syndic en vertu de la loi fédérale n'a pas nécessairement pour effet de rendre cette désignation inopérante à l'égard des réclamations des créanciers sous le régime des lois provinciales pertinentes incorporées par l'al. 67(1)*b*).

Il n'est pas nécessaire de décider si l'intimé Ramgotra a fait une disposition inopposable visée par le second volet du par. 91(2) lorsqu'il a désigné son épouse à titre de bénéficiaire de son FERR. Même si la disposition était inopposable au syndic, cela n'autorisait pas ce dernier à utiliser les fonds du FERR pour régler les réclamations des créanciers telle la banque appelante. Le FERR est un bien exempt aux termes des lois provinciales incorporées par l'al. 67(1)*b*), c'est-à-dire qu'il ne fait pas partie des biens constituant le patrimoine attribué aux créanciers. Pour cette raison, même si l'intérêt futur et éventuel de M^me^ Ramgotra dans le FERR était passé en la possession du syndic par l'application du par. 91(2), le FERR était un bien «non réalisable» par le syndic aux termes du par. 40(1) *LFI*. Par conséquent, le syndic était tenu, avant de demander sa libération, de retourner ce bien à l'intimé Ramgotra. Peu importe que la disposition faite par l'intimé Ramgotra soit ou non

exempt status of the RRIF is an absolute bar to the appellant's claim.

Whether a settlor has acted in good faith or for the purpose of defeating creditors is not relevant to the question of whether a settlement has been made within s. 91. In contrast, however, a settlor's intention is highly relevant where a settlement is being challenged under provincial fraud legislation. It was not necessary to determine if a life insurance beneficiary designation can be set aside as a fraudulent conveyance of property. The provincial fraud provisions are clearly remedial in nature and should be given the fair, large and liberal construction and interpretation that best ensures the attainment of their objects. There is a strong case for concluding that a life insurance beneficiary designation is both a "juridical act" and a "disposition" or "conveyance" of "property".

The *Statute of Elizabeth*, assuming without deciding that it remains in force, would allow creditors to challenge fraudulent conveyances, including life insurance beneficiary designations, without having to prove that, at the time of the conveyance, the debtor was insolvent, was unable to pay his or her debts in full, or knew that he or she was on the eve of insolvency.

Cases Cited

Applied: *Re Bozanich*, [1942] S.C.R. 130; **considered**: *Re Wozniuk* (1987), 76 A.R. 42; *Re Geraci* (1970), 14 C.B.R. (N.S.) 253, rev'g (1969), 13 C.B.R. (N.S.) 86; *Re Sykes* (1993), 18 C.B.R. (3d) 148; *Re Pearson* (1977), 23 C.B.R. (N.S.) 44; *Nicholson v. Milne* (1989), 74 C.B.R. (N.S.) 263; **disapproved**: *Wilson v. Doane Raymond Ltd.* (1988), 69 C.B.R. (N.S.) 156; *Re Yewdale* (1995), 30 C.B.R. (3d) 194; **referred to**: *Royal Bank v. Oliver* (1992), 11 C.B.R. (3d) 82; *In re Lowndes; Ex parte Trustee* (1887), 18 Q.B.D. 677; *Shrager v. March*, [1908] A.C. 402; *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453; *M.N.R. v. Anthony* (1995), 124 D.L.R. (4th) 575; *Re Malloy* (1983), 48 C.B.R. (N.S.) 308; *Alberta Treasury Branches v. Guimond* (1987), 70 C.B.R. (N.S.) 125; *Camgoz (Trustee of) v. Sun Life Assurance Co. of Canada* (1988), 70 C.B.R. (N.S.) 131, aff'd (1988), 72 C.B.R. (N.S.) 319; *Klassen (Trustee of) v. Great West Life Assurance Co.* (1990), 1 C.B.R. (3d) 263; *Re Douyon* (1982), 134 D.L.R. (3d) 324; *Re MacDonald*

inopposable au syndic, la qualité de bien exempt du FERR est un obstacle insurmontable à la réclamation de l'appelante.

La question de savoir si un disposant a agi de bonne foi ou dans le but de frustrer ses créanciers n'est pas pertinente pour déterminer s'il y a eu disposition au sens de l'art. 91. En revanche, l'intention du disposant est éminemment pertinente lorsqu'une disposition est contestée en vertu des lois provinciales en matière de fraude. Il n'est pas nécessaire de déterminer s'il est possible de faire annuler, en tant que transfert frauduleux de biens, la désignation d'un bénéficiaire d'une assurance-vie. Les dispositions législatives provinciales en matière de fraude visent manifestement à créer un recours, et elles devraient donc recevoir une interprétation équitable, large et libérale qui favorise la réalisation de leur objet. Il y a de bonnes raisons de conclure que la désignation d'un bénéficiaire d'une assurance-vie est à la fois un «acte juridique» et une «aliénation» ou un «transfert» de «biens».

À supposer — sans en décider — que le *Statute of Elizabeth* soit toujours en vigueur, ce texte permettrait aux créanciers de contester des transferts frauduleux, y compris la désignation du bénéficiaire d'une assurance-vie, sans avoir à prouver que, au moment où ceux-ci ont été effectués, le débiteur était insolvable ou incapable de payer la totalité de ses dettes, ou encore qu'il se savait sur le point d'être insolvable.

Jurisprudence

Arrêt appliqué: *Re Bozanich*, [1942] R.C.S. 130; **arrêts examinés**: *Re Wozniuk* (1987), 76 A.R. 42; *Re Geraci* (1970), 14 C.B.R. (N.S.) 253, inf. (1969), 13 C.B.R. (N.S.) 86; *Re Sykes* (1993), 18 C.B.R. (3d) 148; *Re Pearson* (1977), 23 C.B.R. (N.S.) 44; *Nicholson c. Milne* (1989), 74 C.B.R. (N.S.) 263; **arrêts critiqués**: *Wilson c. Doane Raymond Ltd.* (1988), 69 C.B.R. (N.S.) 156; *Re Yewdale* (1995), 30 C.B.R. (3d) 194; **arrêts mentionnés**: *Royal Bank c. Oliver* (1992), 11 C.B.R. (3d) 82; *In re Lowndes; Ex parte Trustee* (1887), 18 Q.B.D. 677; *Shrager c. March*, [1908] A.C. 402; *Husky Oil Operations Ltd. c. Ministre du Revenu national*, [1995] 3 R.C.S. 453; *M.N.R. c. Anthony* (1995), 124 D.L.R. (4th) 575; *Re Malloy* (1983), 48 C.B.R. (N.S.) 308; *Alberta Treasury Branches c. Guimond* (1987), 70 C.B.R. (N.S.) 125; *Camgoz (Trustee of) c. Sun Life Assurance Co. of Canada* (1988), 70 C.B.R. (N.S.) 131, conf. par (1988), 72 C.B.R. (N.S.) 319; *Klassen (Trustee of) c. Great West Life Assurance Co.* (1990), 1 C.B.R. (3d) 263; *Re Douyon* (1982), 134 D.L.R. (3d) 324; *Re*

(1991), 21 C.B.R. (3d) 211; *Canadian Imperial Bank of Commerce v. Meltzer* (1991), 6 C.B.R. (3d) 1; *Marzetti v. Marzetti*, [1994] 2 S.C.R. 765; *Thompson v. Coulombe* (1984), 54 C.B.R. (N.S.) 254; *Zemlak (Trustee of) v. Zemlak* (1987), 66 C.B.R. (N.S.) 1; *Sovereign General Insurance Co. v. Dale* (1988), 32 B.C.L.R. (2d) 226; *Technurbe Building Construction Ltd. v. McKinley* (1989), 76 C.B.R. (N.S.) 106.

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Bankruptcy Rules, C.R.C. 1978, c. 368, r. 89.
Civil Code of Québec, art. 1631 ("Paulian Action").
Exemptions Act, R.S.S. 1978, c. E-14, s. 2.
Frauds on Creditors Act, R.S.P.E.I. 1988, c. F-15, s. 2.
Fraudulent Conveyance Act, R.S.B.C. 1979, c. 142, s. 1.
Fraudulent Conveyances Act, R.S.M. 1987, c. F160, s. 2.
Fraudulent Conveyances Act, R.S.N. 1990, c. F-24, s. 3.
Fraudulent Conveyances Act, R.S.O. 1990, c. F.29, s. 2.
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Interpretation Act, 1993, S.S. 1993, ch. I-11.1, art. 10.
Loi sur la faillite et l'insolvabilité, L.R.C. (1985), ch. B-3, art. 2 «disposition» [mod. par L.C. 1992, ch. 27, art. 3(2)], 16(3), 17, 18, 19, 24, 30(1)*a*), *b*), *c*), *j*), 40(1), 43(1), 49(1), 67(1) [abr. & rempl. *idem* art. 33], *a*), *b*), *c*), *d*), 68 [*idem* art. 34], 71(2), 72(1), 91(1) [*idem* art. 40], (2), 3*b*), 94, 98(1), 99, 158*a*).
Loi sur les cessions en fraude des droits des créanciers, L.R.O. 1990, ch. F.29, art. 2.
Loi sur les cessions et préférences, L.R.O. 1990, ch. A.33, par. 4(1).
Loi sur les cessions et préférences, S.R.N.-B. 1973, ch. A-16, art. 2.
Loi sur les préférences et les transferts frauduleux, L.R.Y. 1986, ch. 72, art. 2.
Loi sur les transferts frauduleux de biens, L.R.M. 1987, ch. F160, art. 2.
Règles régissant la faillite, C.R.C. 1978, ch. 368, art. 89.

Saskatchewan Insurance Act, R.S.S. 1978, c. S-26, ss. 2(kk)(i), (ii), (iii), (iv), (vii), 158(1), (2).

Saskatchewan Farm Security Act, S.S. 1988-89, ch. S-17.1, art. 65.

Saskatchewan Insurance Act, R.S.S. 1978, ch. S-26, art. 2kk)(i), (ii), (iii), (iv), (vii), 158(1), (2).

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APPEAL from a judgment of the Saskatchewan Court of Appeal (1994), 26 C.B.R. (3d) 1, 120 Sask. R. 277, 68 W.A.C. 277, 115 D.L.R. (4th) 536, [1994] 8 W.W.R. 26, [1994] I.L.R. ¶ 1-3089, dismissing an appeal from a judgment of Baynton J. (1993), 18 C.B.R. (3d) 1, 108 Sask. R. 257. Appeal dismissed.

Robert G. Kennedy and *Ian A. Sutherland*, for the appellant.

Gary A. Meschishnick and *Eric M. Singer*, for the respondent North American Life Assurance Co.

Robert D. Jackson, for the respondent Balvir Singh Ramgotra.

The judgment of the Court was delivered by

GONTHIER J. —

I. Issue

1 This case raises an important and controversial issue concerning the interpretation of ss. 67(1)(*b*)

Doctrine citée

Caplan, Lisa H. Kerbel. Case Comment (1994), 26 C.B.R. (3d) 252.

Cuming, R. C. C. «Section 91 (Settlements) of the Bankruptcy and Insolvency Act: A Mutated Monster» (1995), 25 *Can. Bus. L.J.* 235.

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POURVOI contre un arrêt de la Cour d'appel de la Saskatchewan (1994), 26 C.B.R. (3d) 1, 120 Sask. R. 277, 68 W.A.C. 277, 115 D.L.R. (4th) 536, [1994] 8 W.W.R. 26, [1994] I.L.R. ¶ 1-3089, qui a rejeté l'appel formé contre la décision du juge Baynton (1993), 18 C.B.R. (3d) 1, 108 Sask. R. 257. Pourvoi rejeté.

Robert G. Kennedy et *Ian A. Sutherland*, pour l'appelante.

Gary A. Meschishnick et *Eric M. Singer*, pour l'intimée la Nord-Américaine, compagnie d'assurance-vie.

Robert D. Jackson, pour l'intimé Balvir Singh Ramgotra.

Version française du jugement de la Cour rendu par

LE JUGE GONTHIER —

I. La question en litige

Le présent pourvoi soulève une question importante et controversée relativement à l'interprétation

and 91 of the *Bankruptcy and Insolvency Act*, R.S.C., 1985, c. B-3, as amended (hereinafter "*BIA*"): Where a bankrupt has transferred registered retirement savings plan (RRSP) funds into a registered retirement income fund (RRIF) within the five years preceding bankruptcy, and where the RRIF is exempt from the claims of creditors under provincial legislation incorporated into the *BIA* by s. 67(1)(*b*), may a creditor set aside the transfer as a s. 91 "settlement", and thereby get at the RRIF despite its exempt status?

de l'al. 67(1)*b*) et de l'art. 91 de la *Loi sur la faillite et l'insolvabilité*, L.R.C. (1985), ch. B-3, et ses modifications, (ci-après la «*LFI*»). Voici cette question: Si un failli a transféré des fonds d'un régime enregistré d'épargne-retraite (REER) dans un fonds enregistré de revenu de retraite (FERR) au cours des cinq années précédant la faillite, et que le FERR est exempt des réclamations des créanciers en vertu de mesures législatives provinciales incorporées à la *LFI* par l'al. 67(1)*b*), un créancier peut-il faire annuler ce transfert pour le motif qu'il s'agit d'une «disposition» visée par l'art. 91, et, ainsi, avoir accès au FERR malgré l'exemption dont bénéficie ce bien?

II. Factual Background

The respondent Ramgotra is a medical doctor who practised from 1971 to 1991 in Saskatoon, Saskatchewan. During this period, as a self-employed doctor responsible for his own retirement planning, he built up savings and investments, including two RRSPs. In May 1989, he became an associate at a Saskatoon medical clinic, but his share of the clinic expenses proved higher than expected. As a result, in February 1990, he opened his own practice. Unfortunately, the practice was not as successful as Dr. Ramgotra had hoped, partly because of a slow patient load, but also because Dr. Ramgotra suffers from insulin dependent diabetes and was required to reduce his work hours in response to his medical condition.

In June 1990, at the suggestion of a financial adviser, Dr. Ramgotra transferred the funds from his two RRSPs into an RRIF under which his wife was designated as beneficiary. The RRIF was to provide Dr. Ramgotra with a gross monthly income of $1,066.20, and these payments commenced in August 1990. The respondent North American Life Assurance Company is the financial institution responsible for the management of the RRIF.

Ten months later, in May 1991, Dr. Ramgotra applied for and obtained a position as permanent physician with the Town of Dinsmore, Saskatchewan. He then attempted to negotiate with his landlord in Saskatoon in order to terminate the com-

II. Les faits

L'intimé, Ramgotra, est médecin, et il a exercé sa profession à Saskatoon, en Saskatchewan, de 1971 à 1991. Durant cette période, en tant que travailleur indépendant responsable de la planification financière de sa retraite, il a épargné et fait des placements, notamment en établissant deux REER. En mai 1989, il s'est associé à une clinique médicale de Saskatoon. Toutefois, comme sa part des dépenses de la clinique s'est révélée plus élevée que prévu, il a ouvert son propre cabinet en février 1990. Malheureusement, cette décision a été moins fructueuse qu'il avait espéré, en partie en raison d'une faible clientèle, mais également en raison du fait que, comme il est diabétique et doit être traité à l'insuline, il a dû réduire ses heures de travail.

En juin 1990, à la suggestion d'un conseiller financier, le Dr Ramgotra a transféré les fonds de ses deux REER dans un FERR dont son épouse a été désignée bénéficiaire. Le FERR devait rapporter au Dr Ramgotra un revenu mensuel brut de 1 066,20 $. Ces paiements ont commencé en août 1990. L'autre partie intimée, la Nord-américaine, compagnie d'assurance-vie, est l'institution financière chargée de la gestion du FERR.

Dix mois plus tard, soit en mai 1991, le Dr Ramgotra a postulé avec succès un poste permanent de médecin auprès de la ville de Dinsmore en Saskatchewan. Il a alors tenté de négocier avec le propriétaire de l'immeuble où il avait son cabinet à

mercial lease for his practice there. These negotiations were unsuccessful, and the landlord obtained a judgment against Dr. Ramgotra for approximately $30,000. This event led Dr. Ramgotra to make an assignment into bankruptcy in February 1992. When he received an absolute discharge from bankruptcy in January 1993, the only assets which he retained were his clothing and household contents, and the RRIF.

5 While Dr. Ramgotra's RRSPs would have been subject to the claims of his creditors, the RRIF constituted a life insurance annuity, and was therefore exempt from their claims on the basis of s. 67(1)(*b*) *BIA*, when read in conjunction with ss. 2(kk)(vii) and 158(2) of *The Saskatchewan Insurance Act*, R.S.S. 1978, c. S-26. However, the trustee in bankruptcy applied under r. 89 of the *Bankruptcy Rules*, C.R.C. 1978, c. 368, for a declaration that the transfer of the RRSP funds into the RRIF was void, pursuant to s. 91(2) *BIA*. That provision declares, in part, that "settlements" made one to five years prior to bankruptcy are void against the trustee if "the interest of the settlor in the property did not pass" upon settlement.

6 At trial, the trustee's application was dismissed because Dr. Ramgotra's transfer of the RRSP funds into the RRIF had been made in good faith, and not for the purpose of defeating the claims of his creditors. An appeal to the Saskatchewan Court of Appeal by the appellant Royal Bank, Dr. Ramgotra's major creditor, was also dismissed.

III. Relevant Statutory Provisions

Saskatchewan Insurance Act, R.S.S. 1978, c. S-26:

2. — ...

(kk) "life insurance" means insurance whereby an insurer undertakes to pay insurance money:

(i) on death;

(ii) on the happening of an event or contingency dependent on human life;

Saskatoon la résiliation du bail commercial qui le liait à ce dernier. Les négociations n'ont pas porté fruit et le propriétaire a obtenu, contre le Dr Ramgotra, un jugement d'environ 30 000 $. Cet événement a amené le Dr Ramgotra à faire cession de ses biens au profit de ses créanciers en février 1992. Lorsqu'il a obtenu sa libération absolue, en janvier 1993, il n'a conservé pour tous biens que ses vêtements, le contenu de sa maison et le FERR.

Alors que les REER du Dr Ramgotra auraient été touchés par les réclamations de ses créanciers, le FERR, parce qu'il constituait une rente d'assurance-vie, était à l'abri de leurs réclamations par l'effet conjugué de l'al. 67(1)*b*) *LFI* ainsi que du sous-al. 2kk)(vii) et du par. 158(2) de *The Saskatchewan Insurance Act*, R.S.S. 1978, ch. S-26. Cependant, le syndic a demandé, conformément à l'art. 89 des *Règles régissant la faillite*, C.R.C. 1978, ch. 368, un jugement déclaratoire portant que, en vertu du par. 91(2) *LFI*, le transfert des fonds des REER dans le FERR était nul. Ce paragraphe énonce notamment que sont inopposables au syndic les «dispositions» de biens faites au cours des cinq ans qui précèdent la faillite si «les intérêts du disposant dans ces biens n'ont pas cessé» lorsque fut faite la disposition.

Au procès, la demande du syndic a été rejetée pour le motif que le Dr Ramgotra avait agi de bonne foi en transférant les fonds des REER dans le FERR et non dans le but de frustrer ses créanciers. L'appel à la Cour d'appel de la Saskatchewan interjeté par l'appelante, la Banque Royale, créancier principal du Dr Ramgotra, a lui aussi été rejeté.

III. Les dispositions législatives pertinentes

The Saskatchewan Insurance Act, R.S.S. 1978, ch. S-26:

[TRADUCTION] **2.** — ...

kk) «assurance-vie» Assurance par laquelle un assureur s'engage à verser une somme assurée:

(i) lorsque survient un décès,

(ii) lorsque survient un événement ou une éventualité se rattachant à la vie humaine,

(iii) at a fixed or determinable future time; or

(iv) for a term dependent on human life;

and, without limiting the generality of the foregoing, includes:

. . .

(vii) an undertaking given by an insurer, whether before or after this section comes into force, to provide an annuity or what would be an annuity except that the periodic payments may be unequal in amount;

158. — (1) Where a beneficiary is designated, the insurance money, from the time of the happening of the event upon which the insurance money becomes payable, is not part of the estate of the insured and is not subject to the claims of the creditors of the insured.

(2) While a designation in favour of a spouse, child, grandchild or parent of a person whose life is insured, or any of them, is in effect, the rights and interests of the insured in the insurance money and in the contract are exempt from execution or seizure.

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

67. (1) The property of a bankrupt divisible among his creditors shall not comprise

. . .

(*b*) any property that as against the bankrupt is exempt from execution or seizure under the laws of the province within which the property is situated and within which the bankrupt resides,

91. (1) Any settlement of property, if the settlor becomes bankrupt within one year after the date of the settlement, is void against the trustee.

(2) Any settlement of property, if the settlor becomes bankrupt within five years after the date of the settlement, is void against the trustee if the trustee can prove that the settlor was, at the time of making the settlement, unable to pay all his debts without the aid of the property comprised in the settlement or that the interest of the settlor in the property did not pass on the execution thereof.

(iii) lorsqu'arrive une date ultérieure déterminée ou déterminable,

(iv) pendant une période se rattachant à la vie humaine,

et, sans restreindre la portée générale de ce qui précède, «assurance-vie» s'entend également:

. . .

(vii) d'un engagement conclu par un assureur, avant ou après l'entrée en vigueur du présent article, de verser une rente dont le montant des versements périodiques peut varier;

158. — (1) Lorsqu'un bénéficiaire est désigné, les sommes assurées ne font pas partie de la succession de l'assuré et ne peuvent être réclamées par les créanciers de l'assuré, dès la survenance de l'événement qui rend les sommes assurées exigibles.

(2) Tant qu'est en vigueur la désignation en faveur du conjoint, d'un enfant, d'un petit-enfant ou du père ou de la mère de la personne dont la vie est assurée, ou de l'un d'eux, les droits et les intérêts de l'assuré dans les sommes assurées et dans le contrat sont exempts d'exécution ou de saisie.

Loi sur la faillite et l'insolvabilité, L.R.C. (1985), ch. B-3, et ses modifications:

67. (1) Les biens d'un failli, constituant le patrimoine attribué à ses créanciers, ne comprennent pas les biens suivants:

. . .

b) les biens qui, à l'encontre du failli, sont exempts d'exécution ou de saisie sous le régime de lois de la province dans laquelle sont situés ces biens et où réside le failli,

91. (1) Toute disposition est inopposable au syndic, si le disposant devient failli durant l'année qui suit la date de la disposition.

(2) Si le disposant devient failli au cours des cinq ans qui suivent la date de la disposition, toute disposition de biens est inopposable au syndic, si ce dernier peut prouver que le disposant était, lorsqu'il a fait la disposition, incapable de payer toutes ses dettes sans l'aide des biens compris dans la disposition, ou que les intérêts du disposant dans ces biens n'ont pas cessé lorsque fut faite la disposition.

(3) This section does not extend to any settlement made

. . .

(*b*) in favour of a purchaser or incumbrancer in good faith and for valuable consideration; . . .

IV. Decisions Below

1. *Saskatchewan Court of Queen's Bench* (1993), 18 C.B.R. (3d) 1

7 In his reasons, Baynton J. made two factual findings: (1) Dr. Ramgotra was solvent at the time he transferred the RRSP funds into the RRIF, and (2) the transfer was made in good faith, and not for the purpose of defeating creditors. Because of the former factual finding, the first branch of s. 91(2) *BIA* could not be used by the trustee to void the transfer. However, the second branch of s. 91(2) was still available, and the issue was whether the transfer was a "settlement" in which the interest of the settlor in the property did not pass at the time of settlement.

8 Relying on recent case law establishing that the exchange of non-exempt property for exempt property (i.e., "self-settlement") could constitute a settlement under s. 91 *BIA*, Baynton J. reached the tentative conclusion that the transfer in the case at bar fell within the second branch of s. 91(2) because it was a settlement in which, by definition, the property interest of the settlor did not pass. He refused, however, to declare the settlement void against the trustee in bankruptcy. He referred to his previous decision in *Royal Bank v. Oliver* (1992), 11 C.B.R. (3d) 82 (Sask. Q.B.), where a similar settlement was at issue. In *Oliver*, he decided that a *bona fide* exchange of property should not be a voidable settlement under s. 91(2). He effectively "borrowed" the concept of good faith which appears in s. 91(3)(*b*) *BIA* (but is not appli-

(3) Le présent article ne s'applique pas à une disposition faite:

. . .

b) soit de bonne foi et pour contrepartie valable, en faveur d'un acheteur ou d'un créancier hypothécaire; . . .

IV. Les décisions des juridictions inférieures

1. *La Cour du Banc de la Reine de la Saskatchewan* (1993), 18 C.B.R. (3d) 1

Dans ses motifs, le juge Baynton a tiré deux conclusions de fait: (1) le Dr Ramgotra était solvable au moment où il a transféré les fonds des REER dans le FERR, et (2) le transfert a été effectué de bonne foi et non dans le but de frustrer les créanciers. Vu la première conclusion de fait, le syndic ne pouvait s'appuyer sur le premier volet du par. 91(2) *LFI* pour considérer le transfert inopposable à son endroit. Il pouvait toutefois invoquer le second volet, ce qui soulevait la question de savoir si le transfert était une «disposition» n'ayant pas eu pour effet de faire cesser les intérêts du disposant dans les biens en cause au moment où elle a été faite.

Se fondant sur des décisions récentes établissant que le remplacement de biens non exempts par des biens exempts (c.-à-d. une «disposition à soi-même») pouvait constituer une disposition visée à l'art. 91 *LFI*, le juge Baynton est arrivé à la conclusion préliminaire que, en l'espèce, le transfert relevait du second volet du par. 91(2) puisqu'il s'agissait d'une disposition dans le cadre de laquelle, par définition, les intérêts du disposant dans les biens visés n'avaient pas cessé. Il a toutefois refusé de déclarer la disposition inopposable au syndic, mentionnant à cet effet sa décision antérieure dans *Royal Bank c. Oliver* (1992), 11 C.B.R. (3d) 82 (B.R. Sask.), affaire où il était question d'une disposition analogue. Dans *Oliver*, il a conclu qu'un remplacement de biens fait de bonne foi ne devait pas être considéré comme une disposition inopposable en vertu du par. 91(2). En fait, il a «emprunté» le concept de la bonne foi prévu à l'al. 91(3)*b*) *LFI* (qui ne s'applique cependant pas en cas de disposition à soi-même), et il s'en est servi

cable in the case of self-settlement), and used it to limit the common law definition of settlement.

Since Dr. Ramgotra had acted in good faith, and not for the purpose of defeating creditors, when he transferred his non-exempt RRSP funds into an exempt RRIF, Baynton J. concluded that the transfer was not a settlement which could be set aside under s. 91(2).

2. *Saskatchewan Court of Appeal* (1994), 26 C.B.R. (3d) 1

The Saskatchewan Court of Appeal unanimously dismissed the appellant's appeal. For the court, Jackson J.A. rejected the submission (which had been accepted by Baynton J.) that a settlement had been effected by the transfer of the non-exempt RRSP funds into the exempt RRIF. In her view, settlement within the meaning of the *BIA* involved settlement on a third party; the mere conversion of non-exempt property into exempt property was insufficient.

However, after a review of the jurisprudence on the meaning of settlement, Jackson J.A. concluded that the designation of a beneficiary under an insurance policy could constitute a settlement. Thus, when Dr. Ramgotra designated his wife as beneficiary under the RRIF, he settled a property interest on her. Jackson J.A. characterized this interest as a future contingent property interest.

Jackson J.A. then considered whether such a settlement could be declared void under the second branch of s. 91(2) concerning the passing of property. In her view, the essential issue was whether or not it was necessary to convey, or give up control over, all the interests in a particular piece of property in order for the property passing exception to be met. Jackson J.A. reviewed the case law on this issue, most of which concluded that a settlement in the form of an insurance beneficiary designation does not involve the passing of property because the settlor always maintains property interests in, and control over, the insurance after the designation. However, she preferred to rely on

pour restreindre la définition du terme «disposition» en common law.

Comme le Dr Ramgotra avait agi de bonne foi et non dans le but de frustrer ses créanciers lorsqu'il a transféré les fonds non exempts de son REER dans les fonds exempts du FERR, le juge Baynton a conclu que le transfert n'était pas une disposition pouvant être annulée en vertu du par. 91(2). 9

2. *Le Cour d'appel de la Saskatchewan* (1994), 26 C.B.R. (3d) 1

La Cour d'appel de la Saskatchewan a, à l'unanimité, rejeté l'appel formé par l'appelante. S'exprimant pour la cour, madame le juge Jackson a rejeté l'argument (qu'avait pour sa part accepté le juge Baynton) que le transfert des fonds non exempts du REER dans les fonds exempts du FERR, avait donné lieu à une disposition. À son avis, les dispositions visées par la *LFI* sont celles faites à un tiers; la simple conversion de biens non exempts en biens exempts ne suffit pas. 10

Toutefois, après avoir examiné la jurisprudence portant sur le sens du concept de «disposition», le juge Jackson a conclu que la désignation d'un bénéficiaire dans une police d'assurance pouvait constituer une disposition. En conséquence, lorsque le Dr Ramgotra a désigné son épouse à titre de bénéficiaire du FERR, il a disposé de son intérêt dans le bien en question en faveur de celle-ci. Pour le juge Jackson, il s'agissait d'un intérêt de propriété futur et éventuel. 11

Le juge Jackson s'est ensuite demandée si une telle disposition pouvait être déclarée inopposable en vertu du second volet du par. 91(2) qui concerne le transfert de la propriété des intérêts dans les biens visés. À son avis, il s'agissait essentiellement de déterminer s'il était nécessaire ou non qu'il y ait transfert de tous les intérêts dans un bien donné ou cession du contrôle sur ceux-ci pour que s'applique l'exception fondée sur le transfert de la propriété des intérêts dans les biens visés. Le juge Jackson a examiné la jurisprudence sur cette question et constaté que, dans la plupart de ces décisions, les tribunaux avaient conclu que les dispositions prenant la forme d'une désignation de 12

two early English cases, *In re Lowndes; Ex parte Trustee* (1887), 18 Q.B.D. 677, and *Shrager v. March*, [1908] A.C. 402 (P.C.), for the proposition that property passes if a settlor divests him- or herself of all interest in the property acquired by a third party beneficiary. Thus, the beneficiary designation in the case at bar passed a contingent property interest to Mrs. Ramgotra, and fully divested Dr. Ramgotra of that same property interest. Jackson J.A. held that this was sufficient to meet the property passing requirement of the second branch of s. 91(2), with the result that Dr. Ramgotra's designation of his wife as beneficiary under the RRIF was not void against his trustee in bankruptcy.

13 Jackson J.A.'s conclusion that the property passing requirement had been met was further reinforced by her view that any other conclusion would be contrary to bankruptcy policy and the purpose of RRIFs. She noted that if the designation of a beneficiary under an insurance policy were not found to pass property to the beneficiary, then all insurance beneficiary designations made within five years of bankruptcy would be void against the trustee in bankruptcy by operation of the second branch of s. 91(2), including those made in good faith when the bankrupt was solvent. Jackson J.A. was of the view that s. 91 *BIA* should be interpreted to avoid such an absurd result.

14 Finally, with respect to the *bona fide* test applied by the trial judge, Baynton J., Jackson J.A. stated that it was not necessary for her to adopt his position, but she nevertheless endorsed his analysis of

bénéficiaire d'une assurance n'entraînaient pas le transfert de la propriété des intérêts dans l'assurance, étant donné que, après la désignation, le disposant conserve toujours ses intérêts dans ce bien et son pouvoir de contrôle sur celui-ci. Elle a toutefois préféré se fonder sur deux vieilles décisions anglaises — *In re Lowndes; Ex parte Trustee* (1887), 18 Q.B.D. 677, et *Shrager c. March*, [1908] A.C. 402 (C.P.) — appuyant la thèse qu'il y a transfert de la propriété du bien visé si le disposant se départit de tous ses intérêts dans le bien acquis par un tiers bénéficiaire. Par conséquent, la désignation d'un bénéficiaire en l'espèce a eu pour effet de transférer à M^me^ Ramgotra un intérêt de propriété éventuel et, du même coup, de dépouiller complètement le D^r^ Ramgotra de cet intérêt. Le juge Jackson a conclu que cela suffisait pour satisfaire à la condition relative au transfert de la propriété des intérêts dans les biens visés prévue par le second volet du par. 91(2), de sorte que la désignation par le D^r^ Ramgotra de son épouse à titre de bénéficiaire du FERR n'était pas inopposable au syndic.

Le juge Jackson trouvait aussi un appui à sa conclusion que la condition relative au transfert de la propriété des intérêts dans les biens visés avait été respectée dans le fait que, à son avis, toute autre conclusion serait contraire à la politique en matière de faillite et à l'objet des FERR. Elle a souligné que, si la désignation d'un bénéficiaire en vertu d'une police d'assurance était jugée ne pas opérer transfert de propriété en faveur du bénéficiaire, alors toutes les désignations de bénéficiaires effectuées dans les polices d'assurance au cours des cinq années précédant une faillite seraient inopposables au syndic par l'application du second volet du par. 91(2), y compris celles ayant été faites de bonne foi lorsque le failli était solvable. De l'avis du juge Jackson, il faut interpréter l'art. 91 *LFI* de manière à éviter un résultat aussi absurde.

Enfin, relativement au critère de bonne foi qu'a appliqué le juge Baynton en première instance, le juge Jackson a déclaré qu'elle n'était pas tenue d'adopter la position de ce dernier, mais elle a

the difficulties associated with any interpretation of s. 91 *BIA* which would automatically void legitimate transactions made by solvent debtors. Jackson J.A. agreed with Baynton J. that to attack a beneficiary designation made by a solvent debtor, a trustee in bankruptcy should have to prove some lack of good faith on the part of the debtor. However, she disagreed that the creation of a good faith requirement for self-settlement under s. 91 would be appropriate. Instead, she opined that trustees may rely on other legislation, such as provincial fraud legislation, to attack bad faith self-settlements.

V. Analysis

1. *Introduction*

In my recent decision in *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453, I had the opportunity to review the two fundamental purposes underlying the *BIA*. As I stated there, the first such purpose is to ensure the equitable distribution of a bankrupt debtor's assets among the estate's creditors, while the second is to provide for the financial rehabilitation of insolvent persons (at para. 7). The case at bar demonstrates that these two purposes may come into conflict. The appellant bank, Dr. Ramgotra's principal creditor, wishes to attach his RRIF in order to satisfy its outstanding financial claims against him. Not surprisingly, in light of Dr. Ramgotra's post-bankruptcy financial position, he resists the bank's attempts to seize one of his few remaining assets. He argues that the RRIF, being life insurance under s. 2(kk)(vii) of *The Saskatchewan Insurance Act*, is exempt from execution or seizure by creditors (s. 158(2) of *The Saskatchewan Insurance Act* and s. 67(1)(*b*) *BIA*). In short, the bank seeks an "equitable distribution" of Dr. Ramgotra's assets, while Dr. Ramgotra's "financial rehabilitation" is furthered if he maintains his interest in the RRIF.

néanmoins souscrit à son analyse des difficultés qu'engendrerait toute interprétation de l'art. 91 *LFI* qui aurait pour effet de rendre automatiquement inopposables les opérations légitimes faites par des débiteurs solvables. Le juge Jackson a convenu avec le juge Baynton que, pour contester la désignation d'un bénéficiaire faite par un débiteur solvable, le syndic devrait être tenu d'établir la mauvaise foi de ce dernier. Toutefois, elle ne croyait pas qu'il serait judicieux de créer une exigence de bonne foi pour les dispositions à soi-même visées par l'art. 91. À son avis, les syndics peuvent invoquer d'autres lois, telles les lois provinciales en matière de fraude, pour contester les dispositions à soi-même faites de mauvaise foi.

V. Analyse

1. *Introduction*

Récemment, dans l'arrêt *Husky Oil Operations Ltd. c. Ministre du Revenu national*, [1995] 3 R.C.S. 453, j'ai eu l'occasion d'examiner les deux objectifs fondamentaux qui sous-tendent la *LFI*. Comme je l'ai dit dans cette affaire, le premier de ces objectifs est d'assurer un partage équitable des biens du débiteur failli entre les créanciers, tandis que le second consiste à favoriser la réhabilitation financière de la personne insolvable (au par. 7). Le présent cas montre que ces deux objectifs peuvent entrer en conflit. La banque appelante, qui est le principal créancier du Dr Ramgotra, souhaite saisir le FERR de ce dernier pour obtenir paiement des sommes qu'il lui doit. Il n'est pas étonnant, compte tenu de la situation financière dans laquelle il se trouve à la suite de sa faillite, que le Dr Ramgotra résiste aux tentatives de la banque de saisir un des rares biens qui lui restent. Il prétend que, comme le FERR est une assurance-vie au sens du sous-al. 2kk)(vii) de *The Saskatchewan Insurance Act*, ce bien est exempt d'exécution ou de saisie par les créanciers (par. 158(2) de *The Saskatchewan Insurance Act* et l'al. 67(1)*b*) *LFI*). Bref, la banque demande un «partage équitable» des biens du Dr Ramgotra, alors que le fait de lui laisser ses intérêts dans le FERR favoriserait sa «réhabilitation financière».

16 Since Dr. Ramgotra transferred the funds from his two RRSPs into his exempt RRIF when he was solvent, and not for the purpose of defeating his creditors, one might well wonder how the bank could get around the exempt status of the RRIF — a status which, on its face, constitutes an absolute bar to the bank's claim. In the general context of debtor-creditor relations, the bank would have no expectation at all of attaching Dr. Ramgotra's exempt RRIF. On the facts of this case, Dr. Ramgotra's creditors are not being denied something which they would otherwise have, since the general rule is that they would not be entitled to attach the RRIF unless it had been removed from Dr. Ramgotra's estate through a fraudulent conveyance. Why should Dr. Ramgotra's bankruptcy place creditors like the bank in a better position than they would be in absent the bankruptcy? The bank's position before this Court appears to conflict with the principle that creditors should not gain on bankruptcy any greater access to their debtors' assets than they possessed prior to bankruptcy: *M.N.R. v. Anthony* (1995), 124 D.L.R. (4th) 575 (Nfld. C.A.), at p. 580.

Puisque le Dr Ramgotra était solvable au moment où il a transféré les fonds de ses deux REER dans son FERR exempt, et qu'il ne cherchait pas, par cette mesure, à frustrer ses créanciers, on peut fort bien se demander de quelle façon la banque pouvait contourner l'exemption dont bénéficie le FERR — exemption qui, à première vue, constitue un obstacle insurmontable à la réclamation de la banque. Dans le contexte général des rapports entre débiteurs et créanciers, la banque n'aurait aucun espoir de saisir le FERR exempt du Dr Ramgotra. À la lumière des faits de la présente affaire, les créanciers du Dr Ramgotra ne sont pas privés d'une chose à laquelle ils auraient par ailleurs droit puisque, selon la règle générale, ils ne pouvaient saisir le FERR que si celui-ci avait été soustrait du patrimoine du Dr Ramgotra par suite d'un transfert frauduleux. Pourquoi la faillite du Dr Ramgotra devrait-elle placer des créanciers comme la banque dans une position plus avantageuse qu'ils ne le seraient si ce n'était de la faillite? La thèse avancée par la banque devant notre Cour paraît entrer en conflit avec le principe que les créanciers ne devraient pas, du fait d'une faillite, obtenir des droits plus étendus sur les biens de leurs débiteurs qu'ils n'en possédaient avant la faillite: *M.N.R. c. Anthony* (1995), 124 D.L.R. (4th) 575 (C.A.T.-N.), à la p. 580.

17 Moreover, the policy of exempting life insurance investments and policies from execution or seizure under the *BIA*, where family members are designated as beneficiaries, is sound. Given the importance of insurance in providing for the welfare of dependents upon the death of the insured, an insurance policy may be characterized as a necessity. In Saskatchewan, as in the other provinces, many other necessities are excluded from the property of a bankrupt which is subject to execution or seizure by creditors. Examples include food, fuel, clothing, household items, tools of a trade (*The Exemptions Act*, R.S.S. 1978, c. E-14, s. 2), farm buildings, farming equipment, and livestock (*The Saskatchewan Farm Security Act*, S.S. 1988-89, c. S-17.1, s. 65). One might well characterize exempt property collectively as the "bare minimum" which a bankrupt is entitled to maintain

Qui plus est, le fait, dans la *LFI*, d'exempter des mesures d'exécution ou de saisie les polices et placements d'assurance-vie lorsque des membres de la famille sont désignés bénéficiaires est une politique judicieuse. En effet, vu l'importance de l'assurance pour le bien-être des personnes à charge de l'assuré après son décès, il est possible de qualifier les polices d'assurances de nécessité de la vie. En Saskatchewan, tout comme dans les autres provinces, de nombreux autres biens indispensables sont exclus des biens d'un failli qui peuvent faire l'objet de mesures d'exécution ou de saisie par les créanciers. Parmi les biens ainsi exclus, mentionnons la nourriture, le combustible, les vêtements, les articles ménagers, les outils nécessaires à la pratique d'un métier (*The Exemptions Act*, R.S.S. 1978, ch. E-14, art. 2), les bâtiments et l'équipement agricoles, et le bétail (*The Saskatchewan*

in order to facilitate his or her rehabilitation following bankruptcy.

Farm Security Act, S.S. 1988-89, ch. S-17.1, art. 65). On pourrait fort bien qualifier l'ensemble des biens exempts de «strict minimum» que le failli a le droit de conserver pour faciliter sa réhabilitation après la faillite.

Thus, the bank's claim before this Court is at odds with the exempt status of the property in question, the policy justification underlying that exempt status, and its own expectations prior to Dr. Ramgotra's bankruptcy as to what it would be able to attach. However, the bank is challenging the transaction which transferred the RRSP funds into the RRIF. The bank claims that this transaction was a settlement within the meaning of s. 91 *BIA*, that Dr. Ramgotra's property interest did not pass at the time of the settlement, and that the settlement is void pursuant to the second branch of s. 91(2) (i.e., the "property passing branch"). According to the bank, the funds at issue are not exempt from execution or seizure because the transaction which rendered them exempt is void.

En conséquence, la réclamation de la banque devant notre Cour est incompatible avec l'exemption dont bénéficie le bien en cause ainsi qu'avec la justification de principe qui sous-tend cette exemption et avec les attentes mêmes qu'avait la banque, avant la faillite du Dr Ramgotra, quant à ce qu'elle pourrait saisir. Il n'en reste pas moins que la banque conteste l'opération par laquelle les fonds des REER ont été transférés dans le FERR. Elle prétend que cette opération était une disposition au sens de l'art. 91 *LFI*, que les intérêts du Dr Ramgotra dans ce bien n'ont pas cessé au moment de la disposition et que celle-ci est inopposable en vertu du second volet du par. 91(2) (le «volet concernant le transfert de la propriété des intérêts dans les biens visés»). Selon la banque, les sommes d'argent en cause ne sont pas exemptes d'exécution ou de saisie, car l'opération qui les a rendues exemptes est nulle.

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The issues raised by the bank are three-fold: (1) is the transaction in the case at bar a settlement within the meaning of s. 91 *BIA*; (2) if so, is the settlement void against the trustee in bankruptcy under the second branch of s. 91(2); and (3) if so, are the funds in the RRIF available to satisfy the claims of Dr. Ramgotra's creditors despite the RRIF's exempt status under s. 67(1)(*b*). These issues are not new. They have been the source of considerable controversy in the lower courts, where four competing approaches have been adopted. I will deal with each of these in turn. However, I should state at the outset that I find none of them to be a satisfactory resolution of the problem presented by the case at bar and similar cases. I prefer an approach which recognizes the distinct roles of ss. 67(1)(*b*) and 91 in bankruptcy, as outlined below.

La banque soulève trois questions: (1) L'opération visée en l'espèce est-elle une disposition au sens de l'art. 91 *LFI*? (2) Dans l'affirmative, la disposition est-elle inopposable au syndic en vertu du second volet du par. 91(2)? (3) Si oui, les fonds du FERR peuvent-ils servir à régler les réclamations des créanciers du Dr Ramgotra en dépit de l'exemption dont bénéficie le FERR en vertu de l'al. 67(1)*b*)? Ces questions ne sont pas nouvelles. Elles sont à l'origine d'une importante controverse au sein des juridictions inférieures, où quatre approches divergentes ont été adoptées. Je vais les examiner à tour de rôle. Je tiens cependant à signaler au départ que, selon moi, aucune de ces approches ne permet de régler de manière satisfaisante le problème que soulèvent la présente espèce et des affaires analogues. Je préfère une approche qui tienne compte des rôles distincts que jouent, en matière de faillite, l'al. 67(1)*b*) et l'art. 91, comme nous le verrons ci-après.

19

2. *The Competing Approaches in the Lower Courts*

(i) The exchange of a non-exempt asset for an exempt asset is a settlement under the *BIA*, and is voidable against the trustee in bankruptcy pursuant to s. 91 where made in the five years preceding bankruptcy (the "*Wilson* approach")

20 The first approach to the problem raised by the case at bar involves the more general issue of whether a self-settlement is caught by s. 91 *BIA*. Such an approach is typified by the decision of the Alberta Court of Appeal in *Wilson v. Doane Raymond Ltd.* (1988), 69 C.B.R. (N.S.) 156. There, the appellant dairy farmers sold their milk quota, a non-exempt asset, and used the proceeds to purchase a condominium, an exempt asset. A month later, they made assignments into bankruptcy. The trustee in bankruptcy sought an order declaring the condominium purchase to be a void settlement of property under s. 69(1) of the *Bankruptcy Act*, R.S.C. 1970, c. B-3, (now s. 91(1)) *BIA*.

21 For the Court of Appeal, Haddad J.A. relied upon the decision of the Alberta Queen's Bench in *Re Wozniuk* (1987), 76 A.R. 42, a case the facts of which are strikingly similar to those of the case at bar. In *Re Wozniuk*, it was held that a self-settlement in which a non-exempt RRSP was exchanged for an exempt life insurance annuity was a settlement within the meaning of the *BIA*. Haddad J.A. agreed with this proposition, adding at p. 159 that "[a] settlement within the scheme of the statute occurs when a disposition of property reduces the bankrupt estate available to the trustee for distribution to creditors". He thus concluded that the appellants' conversion of non-exempt property into exempt property was a void settlement under the *BIA*, since it had the effect of reducing the estate which was available to creditors. It made no difference that the appellants had effected the conversion for the purpose of obtaining a home for themselves, and not for the purpose of defeating creditors.

2. *Les approches divergentes des juridictions inférieures*

(i) La conversion d'un bien non exempt en bien exempt est, sous le régime de la *LFI*, une disposition inopposable au syndic en vertu de l'art. 91 si elle survient au cours des cinq années précédant la faillite (l'«approche *Wilson*»)

La première approche du problème en l'espèce soulève la question plus générale de savoir si les dispositions à soi-même sont visées par l'art. 91 *LFI*. L'illustration typique de cette approche est l'arrêt *Wilson c. Doane Raymond Ltd.* (1988), 69 C.B.R. (N.S.) 156, de la Cour d'appel de l'Alberta. Dans cette affaire, les producteurs laitiers appelants ont vendu leur contingent de lait, bien non exempt, et utilisé le produit de la vente pour acheter un condominium, bien exempt. Un mois plus tard, ils ont fait cession de leurs biens. Le syndic a alors demandé une ordonnance déclarant que l'achat du condominium lui était inopposable, conformément au par. 69(1) de la *Loi sur la faillite*, S.R.C. 1970, ch. B-3 (maintenant le par. 91(1) *LFI*).

S'exprimant pour la Cour d'appel, le juge Haddad s'est appuyé sur la décision de la Cour du Banc de la Reine de l'Alberta dans *Re Wozniuk* (1987), 76 A.R. 42, affaire dont les faits sont étonnamment semblables à ceux de l'espèce. Dans *Re Wozniuk*, il a été jugé qu'une disposition à soi-même dans le cadre de laquelle un REER non exempt a été remplacé par une rente d'assurance-vie exempte était une disposition au sens de la *LFI*. Le juge Haddad a souscrit à cette proposition, ajoutant, à la p. 159, qu'il y a [TRADUCTION] «disposition au sens de la loi lorsque l'opération en cause réduit le patrimoine du failli à distribuer aux créanciers par le syndic». Il a par conséquent conclu que la conversion par les appelants d'un bien non exempt en bien exempt était une disposition inopposable aux termes de la *LFI*, puisqu'elle avait pour effet de réduire le patrimoine disponible pour les créanciers. Le fait que les appelants avaient effectué la conversion afin de se procurer un logement et non dans le but de frustrer leurs créanciers ne changeait rien à la situation.

The principle flowing from *Wilson* and *Wozniuk*, namely that the exchange of a non-exempt asset for an exempt asset is a settlement under the *BIA*, and is voidable under s. 91, has been adopted in numerous cases: *Re Malloy* (1983), 48 C.B.R. (N.S.) 308 (Ont. S.C.); *Alberta Treasury Branches v. Guimond* (1987), 70 C.B.R. (N.S.) 125 (Alta. Q.B.); *Camgoz (Trustee of) v. Sun Life Assurance Co. of Canada* (1988), 70 C.B.R. (N.S.) 131 (Sask. Q.B.), aff'd (1988), 72 C.B.R. (N.S.) 319 (Sask. C.A.); *Klassen (Trustee of) v. Great West Life Assurance Co.* (1990), 1 C.B.R. (3d) 263 (Sask. Q.B.). Moreover, this principle was adopted by the trial judge, Baynton J., in the case at bar, and in his earlier decision in *Oliver*, *supra*.

Le principe qui découle des affaires *Wilson* et *Wozniuk*, à savoir que le remplacement d'un bien non exempt par un bien exempt est une disposition au sens de la *LFI* et inopposable aux termes de l'art. 91, a été adopté dans de nombreuses décisions: *Re Malloy* (1983), 48 C.B.R. (N.S.) 308 (C.S. Ont.); *Alberta Treasury Branches c. Guimond* (1987), 70 C.B.R. (N.S.) 125 (B.R. Alb.); *Camgoz (Trustee of) c. Sun Life Assurance Co. of Canada* (1988), 70 C.B.R. (N.S.) 131 (B.R. Sask.), conf. par (1988), 72 C.B.R. (N.S.) 319 (C.A. Sask.); *Klassen (Trustee of) c. Great West Life Assurance Co.* (1990), 1 C.B.R. (3d) 263 (B.R. Sask.). En outre, ce principe a été adopté par le juge Baynton dans le présent cas, en première instance, ainsi que dans sa décision antérieure dans *Oliver*, précité. 22

The approach which found favour with the Alberta Court of Appeal in *Wilson* was rejected, I think properly, by the Saskatchewan Court of Appeal in the case at bar. In my view, it is incorrect to conclude that a person may settle property on him- or herself. This is confirmed by the traditional judicial understanding of "settlement", as stated by this Court in *In re Bozanich*, [1942] S.C.R. 130. Rinfret J. described "settlement" as follows at pp. 138-39:

L'approche qu'a privilégiée la Cour d'appel de l'Alberta dans l'arrêt *Wilson* a été rejetée, avec raison selon moi, par la Cour d'appel de la Saskatchewan dans l'affaire qui nous intéresse. Je suis d'avis qu'il est erroné de conclure qu'une personne peut disposer de biens en faveur d'elle-même. Cette opinion est d'ailleurs confirmée par l'interprétation traditionnelle du mot «disposition» par les tribunaux, qu'a exprimée notre Cour dans *In re Bozanich*, [1942] R.C.S. 130. Le juge Rinfret a décrit ce mot ainsi, aux pp. 138 et 139: 23

> Without attempting to give a definition of the word — and more particularly of that word as used in section 60 — it seems to me sufficient for the purpose of interpreting the section to adopt a passage of Cave J., in the case of *In re Player; Ex parte Harvey* (1885), 15 Q.B.D. 682, at 686-687:
>
> > One must look at the whole of the language of the section in applying that definition, and consider what is meant by "settlement". Although "settlement", by the 3rd subsection, "shall for the purposes of this section include any conveyance or transfer of property", yet I think the view of my brother Mathew is well founded, and that a settlement in the ordinary sense of the word is intended. The transaction must be in the nature of a settlement, though it may be effected by a conveyance or transfer. The end and purpose of the thing must be a settlement, that is, a disposition of property to be held for the enjoyment of some other person. [Emphasis added.]

> [TRADUCTION] Sans tenter de définir le mot — et plus particulièrement tel qu'il est utilisé à l'art. 60 — il me semble suffisant, pour interpréter cet article, d'adopter le passage suivant des motifs du juge Cave dans l'affaire *In re Player; Ex parte Harvey* (1885), 15 Q.B.D. 682, aux pp. 686 et 687:
>
> > Il faut, dans l'application de cette définition, examiner l'ensemble du libellé de l'article et se demander ce qu'on entend par «disposition». Même si, aux termes du paragraphe 3, «disposition» s'entend également, pour l'application du présent article, de tout transport ou transfert de propriété», je demeure d'avis que l'opinion de mon collègue Mathew est bien fondée et que ce mot est utilisé dans son sens ordinaire. L'opération en cause doit tenir de la nature d'une disposition, même si elle peut être effectuée par voie de transport ou de transfert. L'opération doit avoir pour finalité et pour objet une disposition, c'est-à-dire l'aliénation d'un bien qui sera détenu pour le bénéfice d'une autre personne. [Je souligne.]

Rinfret J. then added, at p. 141:

> The Act, as broad as it is, allows of a clear distinction between settlements though effected by a conveyance or transfer of property and conveyances or transfers of property not in the nature of a settlement.

24 There is no room in the definition of settlement adopted by this Court in *Re Bozanich* for a "settlement onto oneself", since the settlement must involve the transfer of property to be held for the enjoyment of another person. It would seem that the lower courts have departed from this aspect of *Re Bozanich*, and have held that a self-settlement is a settlement under the *BIA*, because the exchange of non-exempt property for exempt property is one convenient means of defeating creditors. As the court reasoned in *Re Wozniuk* at p. 62, a bankrupt should not be able to "bootstrap himself" out of s. 91 "by taking non-exempt property and converting it into property which would be exempt".

25 Although the court in *Wilson* thought that excluding self-settlements from s. 91 *BIA* would allow for considerable abuse, it seems to me that the contrary conclusion is more problematic. If creditors may attach self-settled property by attacking the self-settlement under s. 91 *BIA*, notwithstanding the exempt status of the property, then the result follows that such property is attachable in all cases where the self-settlement occurred in the five years preceding bankruptcy, including those cases where the bankrupt was solvent and acting in good faith at the time of the impugned transaction. In his article, "Section 91 (Settlements) of the Bankruptcy and Insolvency Act: A Mutated Monster" (1995), 25 *Can. Bus. L.J.* 235, Professor Cuming strongly criticized the judicial extension of the concept of settlement to include self-settlement as "patently unreasonable", at p. 235, and "a dramatic mutation", at p. 238. He added, at p. 242:

Le juge Rinfret a ajouté ceci, à la p. 141:

> [TRADUCTION] La Loi, aussi générale qu'elle soit, permet d'établir une distinction nette entre les dispositions, même celles effectuées par voie de transport ou de transfert de propriété, et les transports ou transferts de propriété qui ne tiennent pas de la nature d'une disposition.

La définition de disposition adoptée par notre Cour dans *Re Bozanich* ne laisse aucune place aux «dispositions à soi-même», puisqu'il doit y avoir transfert d'un bien qui sera détenu pour le bénéfice d'une autre personne. Il semble que les juridictions inférieures se soient écartées de cet aspect de l'arrêt *Re Bozanich* et aient conclu qu'une disposition à soi-même est une disposition visée par la *LFI* parce que la conversion de biens non exempts en biens exempts est un moyen pratique de frustrer les créanciers. Suivant le raisonnement de la cour dans *Re Wozniuk*, à la p. 62, un failli ne devrait pas avoir la possibilité de «se soustraire par lui-même» à l'application de l'art. 91 [TRADUCTION] «en convertissant des biens non exempts en biens qui seraient exempts».

Bien que, dans *Wilson*, la cour ait estimé que le fait d'exclure les dispositions à soi-même du champ d'application de l'art. 91 *LFI* ouvrirait la porte à de graves abus, il me semble que la solution contraire pose davantage de problèmes. En effet, si on permet aux créanciers de saisir, en vertu de l'art. 91 *LFI*, des biens ayant fait l'objet d'une disposition à soi-même, même dans les cas où il s'agit de biens exempts, il s'ensuit que ces biens sont saisissables chaque fois que la disposition à soi-même est survenue au cours des cinq années qui précèdent la faillite, y compris dans les cas où le failli était solvable et a agi de bonne foi au moment de l'opération contestée. Dans son article intitulé «Section 91 (Settlements) of the Bankruptcy and Insolvency Act: A Mutated Monster» (1995), 25 *Can. Bus. L.J.* 235, le professeur Cuming a vivement critiqué l'élargissement, par les tribunaux, du concept de disposition pour y inclure les dispositions à soi-même, qualifiant cette interprétation de [TRADUCTION] «manifestement déraisonnable» à la p. 235 et de «mutation dramatique», à la p. 238. Il a ajouté ceci à la p. 242:

The problem of injustice arises when this expanded interpretation of the concept of settlement is combined with another Canadian-made adjunct to s. 91: that, in both such situations, the interest of the settlor does not pass on execution of the transfers, thereby bringing them within the third arm of s. 91. The logic of this reasoning appears to be as follows: the transfer of the property to the debtor is a settlement and the interest of the settlor did not pass on execution since, by definition, he retained or ended up with the interest or its equivalent.

This approach alone, while unable to withstand close technical scrutiny, would not be a source of injustice if the property has not been converted into exempt property as a result of the unexecuted transaction. The "settled" property is divisible among the bankrupt settlor's creditors. The potential for injustice arises in situations where the "settlement" involves conversion of property from non-exempt to exempt property. [Emphasis added.]

I agree that there is considerable potential for injustice if the *Wilson* approach to self-settlement is adopted. The situation is quite different in the case of settlements on third parties, not only because in such cases the property of the settlor may well have passed, but also because of s. 91(3)(*b*). That provision states that a "settlement made . . . in favour of a purchaser or incumbrancer in good faith and for valuable consideration" is not void against the trustee in bankruptcy, thus providing a *bona fide* exception to s. 91(1) and (2). However, the provision is not available in the case of self-settlement because, (1) there is no "purchaser or incumbrancer", and (2) there is no exchange of "valuable consideration". The Act therefore affords no protection to self-settlors like Dr. Ramgotra, who have acted in good faith. This anomaly is a persuasive indication that Parliament did not intend s. 91 to apply to self-settlement.

Further to this, I think that the inclusion of self-settlements within s. 91 is contrary to the purpose

[TRADUCTION] La question du risque d'injustice se soulève lorsque cette interprétation élargie du concept de disposition est conjuguée à un autre ajout à l'art. 91, de création canadienne celle-là: c'est-à-dire le fait que dans les deux situations susmentionnées les intérêts du disposant ne cessent pas lorsque le transfert est effectué, de sorte que celui-ci tombe alors sous le coup du troisième volet de l'art. 91. La logique de ce raisonnement paraît être la suivante: le transfert des biens en cause au débiteur est une disposition et les intérêts du disposant dans ces biens n'ont pas cessé lorsque fut faite la disposition puisque, par définition, ce dernier a conservé les intérêts ou leur équivalent, ou ceux-ci se sont retrouvés entre ses mains.

Même si elle ne saurait résister à un examen formel serré, cette approche ne constituerait pas à elle seule une source d'injustice si les biens en cause n'ont pas été convertis en biens exempts du fait de l'opération non réalisée. Les biens «dont il a été disposé» font partie du patrimoine attribué aux créanciers du disposant failli. Le risque d'injustice naît lorsque la «disposition» emporte la conversion de biens non exempts en biens exempts. [Je souligne.]

26 Je conviens que le risque d'injustice est considérable si l'approche *Wilson* concernant les dispositions à soi-même est adoptée. Il en va tout autrement des dispositions faites à des tiers, non seulement parce que, dans de tels cas, il est fort possible que les intérêts du disposant dans les biens en cause aient cessé, mais également en raison de l'al. 91(3)*b*). Aux termes de cet alinéa, une «disposition faite [. . .] de bonne foi et pour contrepartie valable, en faveur d'un acheteur ou d'un créancier hypothécaire» est opposable au syndic. Il s'agit donc d'une exception — fondée sur la bonne foi — aux par. 91(1) et (2). Cependant, l'al. 91(3)*b*) ne peut être invoqué en cas de disposition à soi-même et ce pour les raisons suivantes: (1) il n'y a pas d'«acheteur ou [de] créancier hypothécaire», et (2) il n'y a pas d'échange pour «contrepartie valable». La Loi n'offre donc aucune protection à ceux qui, comme le Dr Ramgotra, se font de bonne foi une disposition à eux-mêmes. Cette anomalie est un indice probant que le législateur n'entendait pas que l'art. 91 s'applique aux dispositions à soi-même.

27 Par ailleurs, j'estime qu'assimiler les dispositions à soi-même aux dispositions visée à l'art. 91

of that provision. As I will explain in greater detail below, s. 91 empowers the trustee in bankruptcy to return property to the bankrupt's estate, where it has been removed from the estate through a settlement by the bankrupt on a third party. Since a self-settlement does not transfer property to a third party, the property remains in the bankrupt's estate and vests in the trustee at the time of the bankruptcy (s. 71(2) *BIA*). What possible role could s. 91 have in that situation? Moreover, the property passing branch of s. 91(2) has traditionally been viewed as providing a means by which the trustee in bankruptcy may challenge *in futuro* settlements by the bankrupt on third party beneficiaries, and thereby avoid future claims by those beneficiaries against the bankrupt's estate. In other words, as Jackson J.A. reasoned in the court below at para. 50, the property passing test catches those transactions by solvent debtors that do not confer an immediate interest. The purpose of the second branch of s. 91(2) would be distorted if creditors could employ it to attach self-settled property, since a self-settlement is qualitatively different from the kinds of dealings at which the property passing test is aimed.

28 Ultimately, I think that the *Wilson* approach to s. 91 fails to strike an appropriate balance between the Act's dual, and sometimes conflicting, purposes of protecting creditors and rehabilitating bankrupts. Even though a self-settlement which creates an exempt asset has the effect of reducing the property available to creditors, one must not lose sight of the fact that the result of the transaction is the acquisition of an asset which is so essential to the bankrupt and his or her dependents that it has been rendered exempt from execution or seizure by provincial legislation incorporated into the Act by s. 67(1)(*b*). To interpret s. 91 *BIA* in a manner which automatically allows creditors to attach exempt property of such an essential character is, in my view, going too far.

est contraire à l'objet de cet article. Comme je l'expliquerai plus en détail plus loin, l'art. 91 habilite le syndic à retourner des biens dans le patrimoine du failli lorsqu'ils en ont été soustraits au moyen d'une disposition faite par le failli en faveur d'un tiers. Puisqu'une disposition à soi-même n'a pas pour effet de transférer les biens visés à un tiers, ces biens demeurent dans le patrimoine du failli et sont dévolus au syndic au moment de la faillite (par. 71(2) *LFI*). Quel rôle l'art. 91 peut-il bien jouer dans un tel cas? Qui plus est, le volet du par. 91(2) qui concerne le transfert de la propriété des intérêts dans les biens visés a traditionnellement été considéré comme offrant au syndic un moyen de contester les dispositions *in futuro* faites par le failli en faveur de tiers bénéficiaires, et ainsi d'éviter que ces bénéficiaires présentent subséquemment des réclamations contre l'actif du failli. En d'autres termes, suivant le raisonnement du juge Jackson, au par. 50 de la décision de la Cour d'appel, le critère du transfert de la propriété des intérêts dans les biens visés s'applique aux opérations effectuées par des débiteurs solvables et qui ne confèrent pas un intérêt immédiat. L'objet du second volet du par. 91(2) serait dénaturé si des créanciers pouvaient l'invoquer pour saisir des biens ayant fait l'objet d'une disposition à soi-même, car une telle disposition est qualitativement différente du genre d'opérations visées par le critère susmentionné.

En définitive, je crois que l'approche *Wilson* concernant l'art. 91 ne permet pas d'établir un juste équilibre entre les deux objectifs, parfois incompatibles, visés par la Loi, c'est-à-dire la protection des créanciers et la réhabilitation des faillis. Même si une disposition à soi-même créant un bien exempt a pour effet de réduire la masse des biens disponibles pour les créanciers, il ne faut pas oublier que le résultat de l'opération est l'acquisition d'un bien si essentiel au failli et aux personnes à sa charge qu'il a été rendu exempt d'exécution ou de saisie par les lois provinciales applicables incorporées dans la Loi par l'al. 67(1)*b*). Interpréter l'art. 91 *LFI* d'une manière qui permette automatiquement aux créanciers de saisir des biens exempts ayant un caractère à ce point essentiel est, à mon avis, aller trop loin.

Thus, I see no reason in this case to depart from the definition of settlement adopted by this Court in *Re Bozanich*, which requires a disposition by the settlor to a third party. To borrow the words of Rinfret J., self-settlement is a transfer of property not in the nature of a settlement.

(ii) *Bona fide* self-settlements are not settlements under s. 91 *BIA* (the "*Oliver* approach")

In light of my rejection of the *Wilson* approach, it is not necessary to deal with the *bona fide* exception developed by Baynton J. in *Oliver*, *supra*, and applied in the case at bar. Suffice it to say that I share Baynton J.'s concerns about the harshness of the legal approach taken in cases like *Wilson*. While I appreciate his solution to the problem, I note that he was bound to follow the *Wilson* view that self-settlements are subject to s. 91, since the Saskatchewan Court of Appeal had accepted this proposition in *Camgoz*, *supra*. As I explain below, I do not think that good faith is relevant to the question of whether a settlement has been made within the meaning of s. 91. I prefer the approach to self-settlement taken by the Saskatchewan Court of Appeal in the instant case.

(iii) The designation of a beneficiary under a life insurance plan is a settlement under the *BIA*, and is voidable against the trustee in bankruptcy pursuant to s. 91 where made in the five years preceding bankruptcy (the "*Geraci* (Court of Appeal) approach")

Although the Court of Appeal in the instant case found that Dr. Ramgotra's exchange of a non-exempt asset for an exempt asset was not, by the fact of the exchange alone, a settlement under s. 91, Jackson J.A. proceeded to hold that when Dr. Ramgotra designated his wife as beneficiary of the RRIF, he effected a s. 91 settlement. This

Par conséquent, je ne vois, en l'espèce, aucune raison de s'écarter de la définition de disposition adoptée par notre Cour dans *Re Bozanich* et qui exige qu'il y ait disposition en faveur d'un tiers par le disposant. Pour emprunter les termes du juge Rinfret, une disposition à soi-même est un transfert de propriété qui ne tient pas de la nature d'une disposition. 29

(ii) Les dispositions de bonne foi à soi-même ne sont pas des dispositions au sens de l'art. 91 *LFI* (l'«approche *Oliver*»)

Comme j'ai rejeté l'approche *Wilson*, il n'est pas nécessaire d'examiner l'exception fondée sur la bonne foi qui a été élaborée dans *Oliver*, précité, par le juge Baynton et appliquée en l'espèce. Qu'il suffise de dire que je partage les préoccupations du juge Baynton relativement à la rigueur de la position juridique adoptée dans des cas tels que l'affaire *Wilson*. Même si je reconnais la valeur de la solution que le juge a apportée au problème, il faut souligner qu'il était tenu de suivre l'opinion, énoncée dans l'arrêt *Wilson*, que les dispositions à soi-même sont visées par l'art. 91, étant donné que la Cour d'appel de la Saskatchewan avait accepté cette proposition dans *Camgoz*, précité. Comme je l'explique plus loin, je ne crois pas que la bonne foi soit un facteur pertinent à l'égard de la question de savoir s'il y a eu disposition au sens de l'art. 91. Je préfère l'approche adoptée par la Cour d'appel de la Saskatchewan dans la présente affaire relativement aux dispositions à soi-même. 30

(iii) La désignation d'un bénéficiaire en vertu d'un régime d'assurance-vie constitue une disposition au sens de la *LFI* et elle est inopposable au syndic, conformément à l'art. 91, lorsqu'elle est faite au cours des cinq années précédant la faillite (l'«approche *Geraci* (Cour d'appel)»)

Bien que, en l'espèce, la Cour d'appel ait statué que le fait que le Dr Ramgotra ait échangé un bien non exempt pour un bien exempt ne constituait pas, du seul fait de l'échange, une disposition au sens de l'art. 91, le juge Jackson a conclu que le Dr Ramgotra a effectué une disposition au sens de l'art. 91 lorsqu'il a désigné son épouse à titre de 31

approach, which is particular to life insurance plans, was based on the decision of the Ontario Court of Appeal in *Re Geraci* (1970), 14 C.B.R. (N.S.) 253. There, at a time when the bankrupt was clearly insolvent, he designated his wife as beneficiary of a life insurance policy with a cash surrender value of $9,000. The effect of the designation was to render the insurance exempt from execution or seizure. The trustee in bankruptcy applied for a declaration that the beneficiary designation was void under the first branch (i.e., the "insolvency branch") of what is now s. 91(2) *BIA*. For the court, Jessup J.A. reasoned at pp. 255-56:

I think there emerges from the authorities a definition of the ordinary meaning of "settlement" that it is a disposition of property to be held, either in original form or in such form that it can be traced, for the enjoyment of some other person; and that the designation of a beneficiary of an insurance policy is such a disposition .... Having regard to the wide ranging affairs to which the Bankruptcy Act applies, I do not think that the word "settlement" in s. 60(1) [now s. 91] of that statute should be given a restricted meaning. The respondent argues that the designation of the wife as beneficiary of the policy was not a disposition of property because she would acquire no property rights in or benefit from the policy, unless and until the prior death of the bankrupt. I think it would be more accurate to say the wife's rights are contingent on the death of her husband. But the definition of property in s. 2(*o*) of the Bankruptcy Act, which is in the widest terms, includes "every description of estate, interest and profit, present or future, vested or *contingent*, in, arising out of, or incident to property" .... Moreover, the circumstance that the wife's contingent interest in the policy may be divested by the designation of a different beneficiary does not derogate from the fact that she has an interest until there is divestiture. [Italics added by Jessup J.A.]

He thus concluded that the beneficiary designation in question, having been made when the bankrupt

bénéficiaire du FERR. Cette approche, qui est particulière aux régimes d'assurance-vie, reposait sur la décision de la Cour d'appel de l'Ontario dans *Re Geraci* (1970), 14 C.B.R. (N.S.) 253. Dans cette affaire, à un moment où le failli en cause était clairement insolvable, ce dernier avait désigné son épouse à titre de bénéficiaire d'une police d'assurance-vie dont la valeur de rachat nette s'élevait à 9 000 $. La désignation avait eu pour effet d'exempter l'assurance des mesures d'exécution ou de saisie. Le syndic a demandé un jugement déclarant que la désignation de la bénéficiaire lui était inopposable en vertu du premier volet (c.-à-d. le «volet de l'insolvabilité») de ce qui est maintenant le par. 91(2) *LFI*. S'exprimant pour la cour, le juge Jessup a fait le raisonnement suivant, aux pp. 255 et 256:

[TRADUCTION] Je suis d'avis qu'il se dégage de la jurisprudence et de la doctrine une définition selon laquelle le mot «disposition», dans son sens ordinaire, s'entend de la disposition d'un bien qui sera détenu — soit dans sa forme originale, soit dans une forme permettant d'en suivre la trace — pour le bénéfice d'une autre personne, et selon laquelle la désignation du bénéficiaire d'une police d'assurance constitue une telle disposition ... Compte tenu du large éventail de situations visées par la Loi sur la faillite, je ne crois pas qu'il convienne de donner un sens restrictif au mot «disposition» figurant au par. 60(1) [maintenant l'art. 91] de cette loi. L'intimé prétend que la désignation de l'épouse à titre de bénéficiaire de la police n'était pas une disposition de biens étant donné que l'épouse n'allait acquérir les droits de propriété sur la police ou profiter des bénéfices découlant de celle-ci que si le failli décédait avant elle. Je crois qu'il serait plus juste de dire que les droits de l'épouse sont subordonnés au décès de son époux. Cependant, la définition du mot biens à l'al. 2*o*) de la Loi sur la faillite, qui est exprimée en termes très généraux, vise notamment «toute espèce de droits, d'intérêts ou de profits, présents ou futurs, acquis ou *éventuels*, dans des biens, ou en provenant ou s'y rattachant». ... De plus, même si l'épouse peut se voir privée de son intérêt éventuel dans la police en cas de désignation d'un bénéficiaire différent, cela ne change rien au fait qu'elle continue d'avoir cet intérêt tant que pareille modification de la désignation ne survient pas. [Les italiques sont du juge Jessup.]

Le juge Jessup a donc conclu que, comme la désignation du bénéficiaire avait été faite à l'époque où

was insolvent, was void against the trustee in bankruptcy.

This reasoning appealed to Jackson J.A., and has been followed by several courts: *Re Douyon* (1982), 134 D.L.R. (3d) 324 (Que. Sup. Ct.); *Re MacDonald* (1991), 21 C.B.R. (3d) 211 (Alta. Q.B.); *Re Yewdale* (1995), 30 C.B.R. (3d) 194 (B.C.S.C.). I too find it persuasive. It is also significant that the *BIA* was amended in 1992 to include a definition of "settlement" as follows:

> **2.** . . .
> "settlement" includes a contract, covenant, transfer, gift and designation of beneficiary in an insurance contract, to the extent that the contract, covenant, transfer, gift or designation is gratuitous or made for merely nominal consideration; [Emphasis added.]

(*Act to Amend the Bankruptcy Act*, S.C. 1992, c. 27, s. 3(2))

This definition was not in force when the circumstances of the instant appeal arose (in fact, between 1949 and 1992, there was no statutory definition of settlement in *BIA*). However, in light of *Geraci* and the cases following it, I think that a jurisprudential consensus has emerged that the designation of a beneficiary under a life insurance policy constitutes a s. 91 settlement. The new statutory definition reflects this consensus. On this basis, I agree with Jackson J.A. that Dr. Ramgotra effected a settlement triggering s. 91.

After concluding that the designation of Mrs. Ramgotra as beneficiary of Dr. Ramgotra's RRIF was a s. 91 settlement, Jackson J.A. turned to the second branch of s. 91(2), and inquired as to whether Dr. Ramgotra's interest in the settled property passed at the time of settlement. The settlement would only be void against the trustee in bankruptcy if Dr. Ramgotra's interest had not passed. This raised the perplexing issue of which "interest" should be considered in relation to the property passing requirement: Dr. Ramgotra's present interest in the RRIF itself, which certainly did

le failli était insolvable, elle était inopposable au syndic.

Ce raisonnement, qui a plu au juge Jackson, a été suivi par de nombreux tribunaux: *Re Douyon* (1982), 134 D.L.R. (3d) 324 (C. sup. Qué.); *Re MacDonald* (1991), 21 C.B.R. (3d) 211 (B.R. Alb.); *Re Yewdale* (1995), 30 C.B.R. (3d) 194 (C.S.C.-B.). Je le trouve moi aussi convaincant. Autre fait significatif, la *LFI* a été modifiée en 1992 afin d'y inclure la définition suivante de «disposition»: 32

> **2** . . .
> «disposition» S'entend notamment des contrats, conventions, transferts, donations et désignations de bénéficiaires aux termes d'une police d'assurance faits à titre gratuit ou pour un apport purement nominal. [Je souligne.]

(*Loi modifiant la Loi sur la faillite*, L.C. 1992, ch. 27, par. 3(2))

Cette définition n'était pas en vigueur lorsque sont survenus les faits ayant donné naissance au présent pourvoi (de fait, entre 1949 et 1992, la *LFI* ne renfermait aucune définition du mot «disposition»). Toutefois, à la lumière de l'arrêt *Geraci* et des décisions qui l'ont suivi, je crois qu'il s'est établi, dans la jurisprudence, un consensus que la désignation d'un bénéficiaire aux termes d'une police d'assurance constitue une disposition au sens de l'art. 91. La nouvelle définition ajoutée à la Loi reflète ce consensus. Pour ce motif, je conviens avec le juge Jackson que le D[r] Ramgotra a fait une disposition qui a déclenché l'application de l'art. 91.

Après avoir conclu que la désignation de M[me] Ramgotra à titre de bénéficiaire du FERR du D[r] Ramgotra était une disposition au sens de l'art. 91, le juge Jackson a appliqué le second volet du par. 91(2) et s'est demandée si les intérêts du D[r] Ramgotra dans le bien dont il avait été disposé avaient cessé lorsque fut faite la disposition. Celle-ci n'était en effet inopposable au syndic que si les intérêts du D[r] Ramgotra n'avaient pas cessé, ce qui soulevait la question complexe de savoir quels sont les «intérêts» qui devaient être pris en considération dans l'application de la condition relative au 33

not pass at the time of settlement, or the future contingent interest which he had obviously passed to Mrs. Ramgotra when she became his beneficiary? (For a general discussion of this controversial issue, see David J. McKee, "Debtor-Creditor Issues Affecting Annuity Contracts" (1993), 12 *Est. & Tr. J.* 247, at pp. 272-78, and Norwood and Weir, *Norwood on Life Insurance Law in Canada* (2nd ed. 1993), at pp. 253-56.)

34 Before this Court, the parties focused their submissions on the property passing issue. This was not surprising, as Jackson J.A. wrote substantial reasons justifying her conclusion that the relevant property interest was the future contingent interest which had passed to Mrs. Ramgotra. Jackson J.A.'s position was in direct conflict with the decision in *Re MacDonald*, *supra*. The difficulty with Jackson J.A.'s position is that it does violence to the distinction which s. 91(2) requires to be made between *in futuro* and immediate transfers of property. The settlement of a contingent and revocable future interest in RRIF funds is an *in futuro* settlement, i.e., the settlor's interest in the property does not pass at the moment of the settlement. If the settlement of a contingent and revocable future interest were considered an immediate transfer of property, as Jackson J.A. proposes, it is difficult to imagine what sort of settlement of future property could not be so described.

35 Since the designation of a beneficiary was an *in futuro* settlement made within the five years prior to Dr. Ramgotra's bankruptcy, it is void against the trustee, pursuant to s. 91(2). However, this does not mean that the RRIF funds may be distributed to the creditors of the estate. For the reasons given below, the exempt status of the life-assured RRIF remains in effect under provincial law so as

transfert de la propriété des intérêts dans les biens visés: s'agissait-il des intérêts actuels du Dr Ramgotra dans le FERR lui-même, qui n'avaient certainement pas cessé lorsque fut faite la disposition, ou des intérêts futurs et éventuels que le Dr Ramgotra avait manifestement transférés à son épouse lorsqu'elle est devenue sa bénéficiaire? (Pour une analyse générale de cette question controversée, voir David J. McKee, «Debtor-Creditor Issues Affecting Annuity Contracts» (1993), 12 *Est. & Tr. J.* 247, aux pp. 272 à 278, et Norwood et Weir, *Norwood on Life Insurance Law in Canada* (2e éd. 1993), aux pp. 253 à 256.)

Devant notre Cour, les parties ont fait porter l'essentiel de leurs arguments sur la question du transfert de la propriété des intérêts dans les biens visés. Cela n'est guère étonnant compte tenu du fait que le juge Jackson a rédigé de longs motifs à l'appui de sa conclusion que l'intérêt de propriété pertinent était l'intérêt futur et éventuel transmis à Mme Ramgotra. La position du juge Jackson allait directement à l'encontre de la décision rendue dans l'affaire *Re MacDonald*, précitée. Le problème que soulève la position du juge Jackson est que sa position fait violence à la distinction qui, en application du par. 91(2), doit être faite entre les transferts immédiats de biens et ceux faits *in futuro*. La disposition d'un intérêt futur éventuel et révocable dans les fonds d'un FERR est une disposition *in futuro*, c.-à-d. une disposition n'ayant pas pour effet, lorsqu'elle est faite, de faire cesser les intérêts du disposant dans le bien en question. Si la disposition d'un intérêt futur éventuel et révocable était considérée comme étant un transfert immédiat de biens, comme le propose le juge Jackson, il est difficile d'imaginer quelle sorte de disposition d'un intérêt futur pourrait échapper à cette description.

Comme la désignation d'une bénéficiaire était une disposition *in futuro* faite au cours des cinq années précédant la faillite du Dr Ramgotra, elle est inopposable au syndic, conformément au par. 91(2). Toutefois, cela ne signifie pas que les fonds du FERR peuvent être attribués aux créanciers de la faillite. Pour les motifs qui suivent, la qualité de bien exempt du FERR comportant une assurance-

to block the creditors' claims. Before explaining why this is so, I will examine the fourth approach to the problem raised in the instant case.

(iv) Where property is exempt from execution or seizure by creditors, pursuant to s. 67(1)(*b*) *BIA*, then its exempt status prevails over the fact that it became exempt as a result of a voidable settlement (the "*Geraci* (trial) approach")

Dr. Ramgotra argued forcefully in his submissions that since his RRIF was an exempt property under *The Saskatchewan Insurance Act*, and since this exemption is incorporated into the *BIA* by s. 67(1)(*b*), then it should be irrelevant that the funds in the RRIF were settled when his wife was designated as the beneficiary. In essence, Dr. Ramgotra urged this Court to hold that the exemption provision of the Act should be given effect regardless of s. 91.

Support for Dr. Ramgotra's submission can be found in the judgment of Houlden J. in the trial decision in *Re Geraci* (1969), 13 C.B.R. (N.S.) 86 (Ont. S.C.) (a judgment later overturned by the Ontario Court of Appeal, as discussed above). Houlden J. began by confirming that the designation of a beneficiary under a life insurance policy is a settlement within the *BIA*. He then observed that by reason of the beneficiary designation, the policy itself was exempt from execution or seizure by creditors pursuant to s. 162(2) of *The Insurance Act*, R.S.O. 1960, c. 190 (re-enacted by S.O. 1961-62, c. 63, s. 4) (now s. 196(2) of the *Insurance Act*, R.S.O. 1990, c. I.8). He construed the effect of the exemption as follows, at pp. 92-93:

. . . I believe on a close examination of s. 162(2) that it is the clear intention of the section to make the policy

vie demeure valide sous le régime des lois provinciales applicables, bloquant ainsi les réclamations des créanciers. Avant d'expliquer pourquoi il en est ainsi, je vais examiner la quatrième approche du problème soulevé par le présent pourvoi.

(iv) Lorsque, conformément à l'al. 67(1)*b*) *LFI*, le bien en cause est exempt d'exécution ou de saisie par les créanciers, sa qualité de bien exempt l'emporte alors sur le fait qu'il a acquis cette qualité par suite d'une disposition inopposable (l'«approche *Geraci* (première instance)»)

Dans son argumentation, le Dr Ramgotra a plaidé avec vigueur que, comme son FERR est un bien exempt sous le régime de *The Saskatchewan Insurance Act* et que cette exemption est incorporée dans la *LFI* par l'al. 67(1)*b*), le fait qu'il y a eu disposition des fonds du FERR au moment de la désignation de son épouse à titre de bénéficiaire ne devrait avoir aucune pertinence. Essentiellement, le Dr Ramgotra exhorte notre Cour de conclure que les dispositions de la Loi qui concernent les exemptions produisent leurs effets malgré l'art. 91.

La prétention du Dr Ramgotra trouve appui dans la décision rendue, en première instance, par le juge Houlden dans *Re Geraci* (1969), 13 C.B.R. (N.S.) 86 (C.S. Ont.) (décision par la suite infirmée par la Cour d'appel de l'Ontario, voir la discussion qui précède). Le juge Houlden a d'abord confirmé que la désignation d'un bénéficiaire aux termes d'une police d'assurance-vie est une disposition au sens de la *LFI*. Il a ensuite souligné que, du fait de cette désignation, la police elle-même était exempte d'exécution ou de saisie par les créanciers conformément au par. 162(2) de *The Insurance Act*, R.S.O. 1960, ch. 190 (réédicté par S.O. 1961-62, ch. 63, art. 4) (maintenant le par. 196(2) de la *Loi sur les assurances*, L.R.O. 1990, ch. I.8). Il a interprété ainsi l'effet de l'exemption, aux pp. 92 et 93:

[TRADUCTION] . . . je crois qu'il ressort d'un examen attentif du par. 162(2) que cette disposition vise claire-

immune from attack by creditors while the wife is designated as beneficiary.

. . .

In my opinion, s. 162(2) has been drafted to provide for the group of persons who were formerly called "preferred beneficiaries". It is now possible to name a person who would formerly have been a preferred beneficiary and at the same time, if the designation is not irrevocable, to retain the right to borrow against, surrender or otherwise deal with the policy, but in my view, the Legislature by the wording of s. 162(2) has made it plain that the policy, while such a designation is in effect, is not to be "exigible for the benefit of (his) creditors": see Mulock C.J.O., in *Royal Bank of Canada v. Dumart*, [1932] O.R. 661 (C.A.).

Houlden J. recognized that some injustice would result from giving precedence to the exempt status of the life insurance policy. For example, an insolvent debtor could convert all his or her assets into cash, purchase a life insurance policy, and render it exempt from seizure by designating a family member as beneficiary. However, he wrote at p. 94:

At the present time, if my interpretation of The Insurance Act is correct, the Legislature had decided that an insurance policy coming within s. 157(1) or s. 162(2) is not available to creditors and, in my opinion, there is good moral justification for this position. Insurance is a very different asset from say a house or an automobile . . . . It is purchased to provide for the dependants of the insured and it is ordinarily paid for in small amounts over the insured's lifetime. I believe there are very good reasons for exempting policies of insurance from seizure . . . .

38 Houlden J.'s reasons in *Geraci* largely repeat the view he expressed in an earlier article, "Life Insurance Contracts in Ontario" (1963), 4 C.B.R. (N.S.) 113, at p. 115:

If a [beneficiary] designation is made in favour of a spouse, child, grandchild or parent of a person whose life is insured, the rights and interests of the insured in

ment à mettre la police d'assurance à l'abri des attaques des créanciers tant que la conjointe en est la bénéficiaire désignée.

. . .

À mon avis, le par. 162(2) a été conçu pour pourvoir aux besoins des personnes qui étaient auparavant appelées «bénéficiaires privilégiés». Il est maintenant possible de désigner une personne qui, auparavant, aurait été un bénéficiaire privilégié, tout en maintenant, si la désignation n'est pas irrévocable, le droit d'emprunter sur la police, de la céder ou de l'aliéner d'une autre façon. Toutefois, je suis d'avis que, en adoptant le libellé du par. 162(2), la législature a clairement indiqué que tant qu'une telle désignation est en vigueur la police n'est pas «exigible pour le bénéfice de (ses) créanciers»: voir le juge en chef Mulock de l'Ontario dans *Royal Bank of Canada c. Dumart*, [1932] O.R. 661 (C.A.).

Le juge Houlden a reconnu que le fait d'accorder la préséance à la qualité de bien exempt de la police d'assurance-vie créerait une certaine injustice. Par exemple, un débiteur insolvable pourrait convertir en argent la totalité de son actif, acheter une police d'assurance-vie et rendre ce bien exempt de saisie en désignant un membre de sa famille à titre de bénéficiaire. Le juge Houlden a cependant écrit ceci, à la p. 94:

[TRADUCTION] À l'heure actuelle, si mon interprétation de *The Insurance Act* est juste, la législature a décidé qu'une police d'assurance visée par le par. 157(1) ou le par. 162(2) ne peut être réclamée par les créanciers; à mon avis, cette position repose sur une excellente justification morale. En effet, l'assurance est un élément d'actif très différent d'une maison ou d'une automobile par exemple . . . L'assuré achète une assurance pour pourvoir aux besoins des personnes à sa charge et, en général, cette assurance est payée au moyen de petits versements faits pendant toute la vie de l'assuré. Je crois qu'il y a de très bonnes raisons de soustraire les polices d'assurance aux saisies . . .

Dans ses motifs dans *Geraci*, le juge Houlden a repris en grande partie l'opinion qu'il avait exprimée dans un article rédigé auparavant et intitulé «Life Insurance Contracts in Ontario» (1963), 4 C.B.R. (N.S.) 113, à la p. 115:

[TRADUCTION] Si une désignation [à titre de bénéficiaire] est faite en faveur d'un conjoint, d'un enfant, d'un petit-enfant ou du père ou de la mère de la per-

the insurance money and in the contract are exempt from execution or seizure (s. 162(2)). Even if the designation of such a beneficiary is not irrevocable, a trustee in bankruptcy cannot deal with such a policy because the rights and interests of the insured are declared to be exempt from execution and seizure and by s. 39(*b*) [now s. 67(1)(*b*)] of the Bankruptcy Act property of a bankrupt does not include property which is exempt from execution or seizure. It would seem that s. 162(2) is drawn with s. 39(*b*) in mind as it uses the identical wording of s. 39(*b*).

sonne assurée, les droits et intérêts de l'assuré dans les sommes assurées et dans le contrat ne peuvent faire l'objet ni d'exécution ni de saisie (par. 162(2)). Même si la désignation de ce bénéficiaire n'est pas irrévocable, le syndic ne peut rien faire à l'égard de cette police parce que les droits et intérêts de l'assuré sont déclarés exempts d'exécution ou de saisie, et que, aux termes de l'al. 39*b*) [maintenant l'al. 67(1)*b*)] de la Loi sur la faillite, les biens d'un failli ne comprennent pas les biens qui sont exempts d'exécution ou de saisie. Il semble que le par. 162(2) ait été rédigé à la lumière de l'al. 39*b*) puisqu'il emploie un libellé identique à celui-ci.

On appeal, Jessup J.A. rejected Houlden J.'s construction of the exemption and settlement provisions of the *BIA*, arguing at p. 258:

If a settlement of property which comes within s. 60(1) [now s. 91(1)] of the Bankruptcy Act, both as to substance and as to time, is none the less to be taken as exempt, by virtue of s. 39(*b*), from the claims of a bankrupt's creditors merely because it would enjoy that exemption under provincial law apart from s. 60(1), the result would be to make s. 60(1) completely nugatory. I cannot conceive that to have been the intent of Parliament. The proper rule of construction is to harmonize all sections of an enactment and this is achieved in the present case by applying s. 39(*b*) in the light of s. 60(1) and not despite s. 60(1). I would, therefore, hold that property settled by a bankrupt within a year before his bankruptcy includes property rendered exempt from execution or seizure, under the laws of the relevant province, as a result of the settlement. [Emphasis added.]

En appel, le juge Jessup a rejeté l'interprétation qu'avait donnée le juge Houlden des articles de la *LFI* concernant les exemptions et les dispositions, faisant valoir les motifs suivants à la p. 258:

[TRADUCTION] Si une disposition de biens entrant dans le champ d'application du par. 60(1) [maintenant le par. 91(1)] de la Loi sur la faillite, et ce tant en ce qui concerne la nature de cette disposition que le moment où elle a été effectuée, doit néanmoins être considérée, en vertu de l'al. 39*b*), comme étant à l'abri des réclamations des créanciers du failli du seul fait qu'elle jouirait de cette exemption sous le régime des lois provinciales indépendamment du par. 60(1), cela aurait pour effet de rendre le par. 60(1) tout à fait inefficace. Je ne peux imaginer que le Parlement ait pu avoir une telle intention. La règle d'interprétation qui s'applique est celle qui veut que l'on interprète en harmonie toutes les dispositions d'un texte de loi, objectif qui est atteint dans la présente affaire si on applique l'al. 39*b*) à la lumière du par. 60(1) et non en dépit de celui-ci. Je conclus par conséquent que les biens dont le failli dispose au cours de l'année qui précède sa faillite comprennent les biens qui, par suite d'une disposition, sont devenus exempts d'exécution ou de saisie sous le régime des lois de la province en cause. [Je souligne.]

Jessup J.A.'s reasoning was expressly rejected in preference to that of Houlden J. by the British Columbia Supreme Court in *Re Sykes* (1993), 18 C.B.R. (3d) 148. Meredith J. noted, at para. 19, that Jessup J.A.'s reasons in *Geraci*

. . . seems . . . to tag onto s. 167(*b*) [*sic*] words such as "unless the disposition of the property referred to amounts to a settlement referred to in s. 91". That comes close to judicial legislation.

Le raisonnement du juge Jessup a été expressément écarté au profit de celui du juge Houlden par la Cour suprême de la Colombie-Britannique dans *Re Sykes* (1993), 18 C.B.R. (3d) 148. Le juge Meredith a souligné, au par. 19, que les motifs du juge Jessup dans *Geraci*

[TRADUCTION] . . . semblent . . . ajouter à l'al. 167*b*) [sic] des mots comme «sauf si la disposition des biens en cause équivaut à une disposition visée à l'art. 91». Cela tient du droit prétorien.

Meredith J. was not prepared to go that route, and instead concluded that the exempt status of the life insurance policy in question was conclusive in that it was not available for seizure by creditors, even though it became exempt as a result of a voidable settlement (see also, *Canadian Imperial Bank of Commerce v. Meltzer* (1991), 6 C.B.R. (3d) 1 (Man. Q.B.), which adopted Houlden J.'s construction of the exemption provisions of the *BIA*).

Le juge Meredith n'était pas disposé à suivre cette voie. Il a plutôt statué que la qualité de bien exempt dont bénéficiait la police d'assurance-vie en question permettait de conclure que les créanciers ne pouvaient la saisir, même si l'exemption résultait d'une disposition inopposable (voir également *Canadian Imperial Bank of Commerce c. Meltzer* (1991), 6 C.B.R. (3d) 1 (B.R. Man.), où la cour a adopté l'interprétation donnée par le juge Houlden des articles de la *LFI* concernant les exemptions).

41 The debate between Houlden J. and Jessup J.A. in *Geraci*, which was taken up by Meredith J. in *Sykes*, was premised on the view that ss. 67(1)(*b*) and 91 *BIA* were in conflict. As Michael J. McCabe stated in his article, "Execution Against an R.R.S.P." (1990), 76 C.B.R. (N.S.) 218, at p. 234:

> The issue, simply stated, is which takes precedence, the exemption provision of s. 67 incorporating the provincial exemptions or the settlement provision of s. 91.

Le débat entre les juges Houlden et Jessup dans *Geraci*, qu'a relancé le juge Meredith dans *Sykes*, prenait pour acquis qu'il y a conflit entre l'al. 67(1)*b*) et l'art. 91 *LFI*. Comme l'a écrit Michael J. McCabe dans son article intitulé «Execution Against an R.R.S.P.» (1990), 76 C.B.R. (N.S.) 218, à la p. 234:

> [TRADUCTION] Exprimée simplement, la question est de savoir lequel, de l'art. 67 qui incorpore les exemptions provinciales, ou de l'art. 91 qui concerne les dispositions, a préséance.

In resolving this issue, both Houlden J. and Jessup J.A. undertook a "lesser of two evils" -type analysis. Houlden J. preferred to give effect to s. 67(1)(*b*) over s. 91, to avoid the result that every designation of a beneficiary under a life insurance policy, made within one year of bankruptcy (or within five years if the designation was made when the debtor was insolvent, or if the property interest of the debtor did not pass when the beneficiary was designated), would be voidable. He thought that instances in which such a designation would be made for the purpose of defeating creditors would be rare, and that "it is better to permit injury to the creditors [in those rare cases] than to inflict the undoubted hardship of the forfeiture of a life's investment" (at p. 94). Jessup J.A. reached the opposite conclusion, because Houlden J.'s interpretation of s. 67(1)(*b*) would render s. 91 "completely nugatory". Nevertheless, Jessup J.A. added, at p. 259:

Pour résoudre cette question, les juges Houlden et Jessup se sont tous deux lancé dans une analyse visant à trouver la solution constituant «le moindre mal». Le juge Houlden a préféré donner préséance à l'al. 67(1)*b*) sur l'art. 91, afin d'éviter que toutes les désignations de bénéficiaires aux termes de polices d'assurance-vie faites au cours de l'année précédant la faillite (ou des cinq années qui précèdent la faillite si la désignation a été faite lorsque le débiteur était insolvable, ou si les intérêts de propriété du débiteur n'ont pas cessé lorsque fut faite la désignation) soient inopposables. Il croyait que les cas où une telle désignation serait faite dans le but de frustrer des créanciers seraient rares et qu'[TRADUCTION] «il est préférable de permettre que les créanciers subissent un préjudice [dans ces rares cas] plutôt que d'infliger l'épreuve indubitable que constitue la perte d'un placement de toute une vie» (à la p. 94). Le juge Jessup a tiré la conclusion contraire, pour le motif que l'interprétation donnée par le juge Houlden de l'al. 67(1)*b*) rendrait l'art. 91 «tout à fait inefficace». Le juge Jessup a néanmoins ajouté ceci, à la p. 259:

It does seem unjust that moneys paid in good faith over a period of years to secure a man's wife and children should be available to his creditors . . . .

He then suggested a legislative amendment to avoid this result.

If I had to choose between the approaches of Houlden J. and Jessup J.A., then I would prefer that of Houlden J. for two reasons. First, I think that Jessup J.A. exaggerated the impact on s. 91 of Houlden J.'s construction, since settlements which change the status of property from non-exempt to exempt are only a portion of the settlements subject to s. 91. Houlden J.'s position certainly does not render s. 91 "completely nugatory", as stated by Jessup J.A. at p. 258. Second, Jessup J.A.'s interpretation of s. 67(1)(*b*) clearly favours the interests of creditors over the rehabilitation interest of the bankrupt settlor. The Act itself provides no indication that this should be so in the circumstances presented by the instant case, or *Geraci*. I do not believe that Parliament intended the funds in exempt life insurance plans to be subject to execution and seizure by creditors, simply on the basis that a settlement occurred when a beneficiary was designated. After all, it is the designation which makes the asset exempt under the provincial legislation incorporated into s. 67(1)(*b*). Are we really to believe that Parliament intended the very act which renders an asset exempt to be the cause of its losing its exempt status? I do not think so. Like Houlden J., I think that it would be preferable to respect the exempt status of a life insurance policy, even where the policy became exempt as a result of a s. 91 settlement.

In any event, I reject the view that ss. 67(1)(*b*) and 91 *BIA* are in conflict, and that the resolution of the case at bar requires me to choose one provision over the other on the basis of policy considerations. In fact, I think that it is possible to rec-

[TRADUCTION] Il semble effectivement injuste de permettre que des sommes d'argent versées de bonne foi pendant des années par un homme pour pourvoir aux besoins de son épouse et de ses enfants soient disponibles pour ses créanciers . . . .

Il a alors proposé une modification à la loi en vue d'éviter pareil résultat.

Si j'avais à choisir entre l'approche du juge Houlden et celle du juge Jessup, j'opterais pour celle du juge Houlden et ce pour deux raisons. Premièrement, je crois que le juge Jessup a exagéré l'impact sur l'art. 91 de l'interprétation du juge Houlden, puisque les dispositions qui ont pour effet de rendre exempt un bien qui ne l'est pas ne forment qu'une partie des dispositions visées par l'art. 91. La position du juge Houlden ne rend certainement pas l'art. 91 «tout à fait inefficace», comme l'a affirmé le juge Jessup, à la p. 258. Deuxièmement, l'interprétation qu'a faite ce dernier de l'al. 67(1)*b*) favorise clairement les intérêts des créanciers plutôt que l'objectif de réhabilitation du disposant failli. La Loi elle-même ne renferme aucune indication qu'il devrait en être ainsi dans les circonstances de l'espèce ou dans celles de l'affaire *Geraci*. Je ne crois pas que le législateur entendait que les sommes se trouvant dans des régimes d'assurance-vie exempts puissent faire l'objet de mesures d'exécution ou de saisie par les créanciers, simplement parce qu'il y a disposition lorsqu'un bénéficiaire est désigné. Après tout, c'est la désignation qui rend le bien exempt sous le régime de la loi provinciale incorporée dans l'al. 67(1)*b*). Devons-nous vraiment croire que le législateur entendait que l'acte même par lequel un bien devient exempt soit en même temps la cause de la perte de cette qualité? Je ne le crois pas. À l'instar du juge Houlden, j'estime qu'il serait préférable de respecter la qualité de bien exempt des polices d'assurance-vie, même lorsqu'elles ont acquis cette qualité par suite d'une disposition visée à l'art. 91.

Quoi qu'il en soit, je ne suis pas d'accord avec l'opinion qu'il y a incompatibilité entre l'al. 67(1)*b*) et l'art. 91 *LFI* et que, pour résoudre la présente affaire, je dois choisir un article au dépens de l'autre en me fondant sur des considérations de

oncile the two provisions by giving effect to their distinct terms, and by recognizing their distinct roles in bankruptcy.

3. *The Preferred Approach to the Problem in the Case at Bar*

(v) Even if a settlement which creates an exempt asset is void **against the trustee in bankruptcy** under s. 91, the exempt status of the asset under provincial law remains in effect to block **the claims of creditors**

44 In reconciling ss. 67(1)(*b*) and 91 *BIA*, it is important to remember that the general scheme through which a bankrupt's estate is divided by the trustee among creditors involves two distinct stages. First, the Act provides that an insolvent person "may make an assignment of all his property for the general benefit of his creditors" (s. 49(1)), or that creditors "may file in court a petition for a receiving order against a debtor" (s. 43(1)). At the time of the assignment or receiving order, the trustee in bankruptcy is obligated to take possession of the assets forming the estate of the bankrupt. Thus, by operation of s. 71(2), the bankrupt's property passes to and vests in the trustee:

71. . . .

(2) On a receiving order being made or an assignment being filed with an official receiver, a bankrupt ceases to have any capacity to dispose of or otherwise deal with his property, which shall, subject to this Act and to the rights of secured creditors, forthwith pass to and vest in the trustee named in the receiving order or assignment, and in any case of change of trustee the property shall pass from trustee to trustee without any conveyance, assignment or transfer.

Section 16(3) *BIA* imposes a duty on the trustee to "take possession of the deeds, books, records and documents and all property of the bankrupt and make an inventory . . . ." Section 158(*a*) imposes a complimentary duty on the bankrupt to inform the trustee of all his or her property which is in his or her possession or control, and to deliver it to the

politique. En fait, je crois qu'il est possible de concilier les deux articles en donnant effet à leur texte respectif et en reconnaissant les rôles distincts qu'ils jouent en matière de faillite.

3. *L'approche privilégiée à l'égard du problème soulevé en l'espèce*

(v) Même si une disposition ayant pour effet de créer un bien exempt est inopposable **au syndic** en vertu de l'art. 91, l'exemption reconnue à ce bien par la loi provinciale demeure valide et écarte **les réclamations des créanciers**

Lorsqu'on réconcilie l'al. 67(1)*b*) et l'art. 91 *LFI*, il est important de se rappeler que le mécanisme général par lequel le patrimoine du failli est partagé par le syndic entre les créanciers comporte deux étapes distinctes. Premièrement, aux termes de la Loi, une personne insolvable «peut faire une cession de tous ses biens au profit de ses créanciers en général» (par. 49(1)), ou les créanciers «peuvent déposer au tribunal une pétition en vue d'une ordonnance de séquestre contre un débiteur» (par. 43(1)). Au moment de la cession ou de l'ordonnance de séquestre, le syndic est tenu de prendre possession des biens qui forment le patrimoine du failli. Ainsi, par l'effet du par. 71(2), les biens du failli passent et sont dévolus au syndic:

71. . . .

(2) Lorsqu'une ordonnance de séquestre est rendue, ou qu'une cession est produite auprès d'un séquestre officiel, un failli cesse d'être habile à céder ou autrement aliéner ses biens qui doivent, sous réserve des autres dispositions de la présente loi et des droits des créanciers garantis, immédiatement passer et être dévolus au syndic nommé dans l'ordonnance de séquestre ou dans la cession, et advenant un changement de syndic, les biens passent de syndic à syndic sans transport, cession, ni transfert quelconque.

Aux termes du par. 16(3) *LFI*, le syndic «prend possession des titres, livres, dossiers et documents, ainsi que tous les biens du failli, et dresse un inventaire . . .» L'alinéa 158*a*) impose de plus au failli, à titre gracieux, l'obligation de révéler et de remettre au syndic tous ses biens qui sont en sa possession ou sous son contrôle. D'autres disposi-

trustee. Other provisions of the Act elaborate upon the powers, duties and functions of the trustee during the property-passing stage of bankruptcy (see, in particular, ss. 17, 18, 19 and 24 *BIA*).

Once the bankrupt's property has passed into the possession of the trustee, the Act provides the trustee with the power to administer the estate. For example, the trustee may, with the permission of the estate inspectors, sell or dispose of assets (s. 30(1)(*a*)), lease real property (s. 30(1)(*b*)), carry on the business of the bankrupt (s. 30(1)(*c*)), or divide certain property among the creditors (s. 30(1)(*j*)). The ultimate purpose of these administrative powers is to manage the estate, in order to provide equitable satisfaction of the creditor's claims. This, then, is the estate-administration stage of bankruptcy, one distinct aspect of which is the distribution of the estate among creditors.

During the property-passing stage of bankruptcy, the trustee is empowered under s. 91 of the Act to set aside certain settlements which have reduced the size of the estate. Thus, s. 91 outlines the circumstances in which a settlement will be voidable at the behest of the trustee in bankruptcy. If a settlement is declared void against the trustee, then the settled property reverts back to the bankrupt's estate, and falls into the possession of the trustee in bankruptcy. Several other provisions of the *BIA* have relevance to the property-passing stage. For example, s. 94 renders certain assignments of book debts void against the trustee; s. 98(1) empowers the trustee to take possession of any money or proceeds from the sale of settled property to a third party, where the original settlement was void; and s. 99 dictates that while property acquired by the bankrupt after the bankruptcy vests in the trustee, it may be transferred by the bankrupt to a good faith purchaser, unless the trustee intervenes in the transaction (in which case the transaction is void against the trustee).

After-acquired property is also dealt with in s. 68, which constitutes a complete code in respect of a bankrupt's salary, wages or other remuneration. The provision stipulates that after-acquired remu-

tions de la Loi précisent les fonctions, pouvoirs et obligations du syndic à l'étape de la passation des biens du failli (voir en particulier les art. 17, 18, 19 et 24 *LFI*).

45 Une fois que les biens du failli sont passés en la possession du syndic, la Loi habilite ce dernier à administrer le patrimoine. Ainsi, avec la permission des inspecteurs, le syndic peut vendre ou aliéner des biens (al. 30(1)*a*)), donner à bail des biens immeubles (al. 30(1)*b*)), continuer le commerce du failli (al. 30(1)*c*)), ou partager certains biens parmi les créanciers (al. 30(1)*j*)). Ces pouvoirs d'administration visent en définitive à faire en sorte que l'actif soit géré de façon à permettre le règlement équitable des réclamations des créanciers. Il s'agit de l'étape de l'administration du patrimoine du failli, dont l'un des aspects est l'attribution de l'actif aux créanciers.

46 Durant l'étape de la passation des biens du failli au syndic, ce dernier est habilité, en vertu de l'art. 91 de la Loi, à annuler certaines dispositions qui ont eu pour effet de réduire la taille du patrimoine. L'article 91 énonce donc les circonstances dans lesquelles une disposition sera annulable à la demande du syndic. Si une disposition est déclarée inopposable au syndic, les biens dont il a été disposé sont retournés au patrimoine du failli et le syndic en prend possession. Plusieurs autres dispositions de la *LFI* s'appliquent à l'étape de la passation des biens au syndic. Par exemple, l'art. 94 rend inopposables au syndic certaines cessions de créances comptables; le par. 98(1) habilite le syndic à prendre possession des sommes d'argent ou autre produit de la vente de biens dont il a été disposé en faveur d'un tiers lorsque la disposition initiale était nulle; et l'art. 99 prévoit que, même si les biens acquis par le failli après la faillite sont dévolus au syndic, ils peuvent néanmoins être transférés par le failli à un acheteur de bonne foi, sauf si le syndic intervient (auquel cas l'opération lui est inopposable).

47 Il est également question des biens acquis après la faillite à l'art. 68, lequel forme un code complet relativement au traitement, salaire ou autre forme de rémunération que reçoit le failli. Aux termes de

neration will not pass to and vest in the trustee unless the trustee intervenes by applying for a court order directing the payment of the remuneration (or a portion of it) to the trustee (*Marzetti v. Marzetti*, [1994] 2 S.C.R. 765, at p. 794). Where the trustee obtains such a court order, then the remuneration which passes into his or her possession is also divisible among creditors, even if it would otherwise be exempt from execution or seizure under provincial law. This is because s. 68 operates "notwithstanding section 67(1)", with the result that a provincial exemption for remuneration which would otherwise be incorporated into s. 67(1)(*b*) is ineffective: *Marzetti*, at pp. 792-93 and 795. I note that Parliament considered it necessary to exclude explicitly after-acquired remuneration from the operation of s. 67(1)(*b*), thereby overriding the exempt status of the remuneration under provincial law, in order to ensure that in those circumstances where such remuneration passed to the trustee, it was also divisible among creditors. This supports the view that absent a specific override of s. 67(1)(*b*), exempt property which passes to and vests in the trustee, whether as a result of ss. 71(2) or 91, will not be divisible among creditors.

cet article, la rémunération reçue après la faillite ne passe et n'est dévolue au syndic que s'il intervient en demandant au tribunal de rendre une ordonnance portant que lui soit payée cette rémunération (ou une partie de celle-ci) (*Marzetti c. Marzetti*, [1994] 2 R.C.S. 765, à la p. 794). Lorsque le syndic obtient une telle ordonnance du tribunal, la rémunération qui passe alors en sa possession fait également partie du patrimoine attribué aux créanciers, même si elle serait par ailleurs exempte d'exécution ou de saisie sous le régime de la loi provinciale applicable. Il en est ainsi parce que l'art. 68 s'applique «[n]onobstant l'article 67(1)», de sorte que l'exemption provinciale applicable à la rémunération et qui serait autrement incorporée à l'al. 67(1)*b*) est inopérante: *Marzetti*, aux pp. 792, 793 et 795. Je souligne que le législateur a jugé nécessaire d'exclure explicitement la rémunération acquise après la faillite du champ d'application de l'al. 67(1)*b*), écartant ainsi la qualité de bien exempt reconnue à la rémunération par les lois provinciales, pour faire en sorte que, dans les cas où cette rémunération passe au syndic, elle soit également attribuée aux créanciers. Cela vient étayer l'opinion voulant que, en l'absence de dérogation expresse à l'al. 67(1)*b*), les biens exempts qui passent et sont dévolus au syndic, par l'application soit du par. 71(2) soit de l'art. 91, ne feront pas partie du patrimoine attribué aux créanciers.

48 Unlike provisions of the Act such as ss. 71(2), 91 or 68, s. 67(1) tells us nothing about the property-passing stage of bankruptcy. Instead, it relates to the estate-administration stage by defining which property in the estate is available to satisfy the claims of creditors. It effectively constitutes a direction to the trustee regarding the disposition of property. Thus, property which is divisible among creditors is defined very broadly in s. 67(1) as:

(*c*) all property wherever situated of the bankrupt at the date of his bankruptcy or that may be acquired by or devolve on him before his discharge, and

(*d*) such powers in or over or in respect of the property as might have been exercised by the bankrupt for his own benefit.

Contrairement à d'autres dispositions de la Loi tels le par. 71(2) et les art. 91 et 68, le par. 67(1) ne vise aucunement l'étape de la passation des biens du failli au syndic. Ce paragraphe porte plutôt sur l'étape de l'administration du patrimoine et précise les biens de l'actif qui sont disponibles pour régler les réclamations des créanciers. Il est en fait une directive au syndic sur la façon de disposer des biens visés. En conséquence, les biens constituant le patrimoine attribué aux créanciers sont décrits en termes très généraux au par. 67(1):

c) tous les biens, où qu'ils soient situés, qui appartiennent au failli à la date de la faillite, ou qu'il peut acquérir ou qui peuvent lui être dévolus avant sa libération;

d) les pouvoirs sur des biens ou à leur égard, qui auraient pu être exercés par le failli pour son propre bénéfice.

However, the trustee is barred from dividing two categories of property among creditors: property held by the bankrupt in trust for another person (s. 67(1)(*a*)), and property rendered exempt from execution or seizure under provincial legislation (s. 67(1)(*b*)). While such property becomes part of the bankrupt's estate in the possession of the trustee, the trustee may not exercise his or her estate distribution powers over it by reason of s. 67.

Thus, it can be seen that ss. 91 and 67 relate to two different stages of bankruptcy. Section 91 dictates that certain settled property will fall back into the estate of the bankrupt in the possession of the trustee, while s. 67 is directed at the exercise of administrative powers over the estate by the trustee. Where a settlement is void against the trustee under s. 91, then in normal circumstances, the trustee is empowered to administer the settled asset, and use it to satisfy the claims of creditors. However, in the special case where the asset is exempt under s. 67(1)(*b*), then the trustee is prohibited from exercising his or her distribution powers because the asset is not subject to division among creditors. This two-stage analysis is similar to the one adopted by Henry J. of the Ontario Supreme Court in *Re Pearson* (1977), 23 C.B.R. (N.S.) 44. That case was concerned with the issue of whether a trustee in bankruptcy could revoke the designation of a beneficiary under a life insurance plan, and substitute the estate as beneficiary. Although the plan itself was exempt from the *BIA*, the trustee sought to defeat the exemption by exercising a "power" under s. 47(*d*) [now s. 67(1)(*d*)]. Henry J. dismissed the trustee's application, and in doing so characterized the effect of the exemption provisions of the Act as follows, at pp. 48-49:

What comes into the hands of the trustee on the occurrence of the bankruptcy are the rights and interests of the insured in the insurance money and in the contract as they stood at the date of the bankruptcy. When that event occurred, those rights and interests were, by s. 170 of The Insurance Act, exempt from execution or seizure. In my opinion, so far as the creditors of the bankrupt are

Cependant, deux catégories de biens ne peuvent être attribués aux créanciers par le syndic: les biens détenus par le failli en fiducie pour toute autre personne (al. 67(1)*a*)), et les biens qui sont exempts d'exécution ou de saisie sous le régime des lois de la province concernée (al. 67(1)*b*)). Même si ces biens deviennent partie du patrimoine du failli en la possession du syndic, ce dernier ne peut, en raison de l'art. 67, exercer sur eux ses pouvoirs d'attribution de l'actif.

Cela permet donc de constater que les art. 91 et 67 régissent deux étapes différentes de la faillite. Alors que l'art. 91 indique que certains biens ayant fait l'objet d'une disposition reviennent dans le patrimoine du failli en la possession du syndic, l'art. 67 porte sur les pouvoirs de nature administrative exercés par ce dernier sur le patrimoine. Lorsque, en vertu de l'art. 91, une disposition est inopposable au syndic, celui-ci est, dans des circonstances normales, habilité à administrer le bien ayant fait l'objet de la disposition et à l'appliquer au règlement des réclamations des créanciers. Cependant, dans les cas particuliers où il s'agit d'un bien exempt en vertu de l'al. 67(1)*b*), le syndic ne peut alors exercer ses pouvoirs de distribution car le bien ne fait pas partie du patrimoine attribué aux créanciers. Cette analyse à deux volets est semblable à celle adoptée par le juge Henry de la Cour suprême de l'Ontario dans *Re Pearson* (1977), 23 C.B.R. (N.S.) 44. Cette affaire portait sur la question de savoir si un syndic peut révoquer la désignation d'un bénéficiaire faite aux termes d'un régime d'assurance-vie et substituer la faillite à titre de bénéficiaire. Même si le régime lui-même était exempt de l'application de la *LFI*, le syndic a cherché à contourner cette exemption en exerçant un «pouvoir» visé à l'al. 47*d*) [maintenant l'al. 67(1)*d*)]. Le juge Henry a rejeté la demande du syndic, qualifiant ainsi l'effet des dispositions de la Loi relatives aux exemptions, aux pp. 48 et 49:

[TRADUCTION] En cas de faillite, passent dans les mains du syndic, tels qu'ils étaient à la date de la faillite, les droits et intérêts de l'assuré dans les sommes assurées et dans le contrat. Lorsque cet événement s'est produit en l'espèce, les droits et intérêts en question étaient, conformément à l'art. 170 de l'Insurance Act, exempts d'exécution ou de saisie. À mon avis, en ce qui concerne

concerned, that situation crystallized at the time the bankruptcy occurred, and that property by virtue of s. 47(*b*) [now s. 67(1)(*b*)] of the Bankruptcy Act was impressed with its character of not being divisible among the creditors, for all the purposes of the bankruptcy.

I adopt this as a correct statement of the law. Therefore, while an asset which is exempt under provincial law passes into the possession of the trustee at the time of bankruptcy, the exemption itself bars the trustee from dividing the asset among creditors where s. 67(1)(*b*) is operative.

50 Relating this to the circumstances in the case at bar, at the time of Dr. Ramgotra's bankruptcy application, his property interest in the RRIF passed to and vested in the trustee in bankruptcy by operation of s. 71(2) *BIA*. Mrs. Ramgotra's future contingent interest as the designated beneficiary under the RRIF was not captured by s. 71(2), since it had been settled on her prior to bankruptcy. It was open to the trustee in bankruptcy to apply to have this settlement set aside under s. 91(2) *BIA*. As I noted above, the settlement was void under s. 91(2) and, consequently, Mrs. Ramgotra's future contingent interest passed to and vested in the trustee. The trustee in bankruptcy possessed the complete set of property interests associated with the RRIF. But the trustee could not divide the RRIF among creditors because its exempt status under s. 67(1)(*b*) *BIA* continued regardless of s. 91. In other words, the role of s. 91 is to bring settled property back into the estate of the bankrupt in the possession of the trustee. Therefore, while s. 91 could be employed to bring Dr. Ramgotra's RRIF fully into the possession of the trustee in bankruptcy, it has no bearing on the issue of whether or not the RRIF is exempt under s. 67(1)(*b*).

51 The appellant has argued that when a settlement creating an exempt asset has been set aside under s. 91, then the exempt status itself is no longer effective. In other words, the existence of a valid settlement is a logical precondition to the enforce-

les créanciers du failli, cette situation s'est cristallisée au moment où est survenue la faillite, et l'al. 47*b*) [maintenant l'al. 67(1)*b*)] de la Loi sur la faillite a eu pour effet de soustraire ces biens du patrimoine attribué aux créanciers pour tout ce qui concerne la faillite.

Je fais mien cet exposé conforme au droit. Par conséquent, même si au moment de la faillite un bien exempt sous le régime des lois provinciales passe en la possession du syndic, l'exemption elle-même empêche ce dernier de partager le bien entre les créanciers lorsque l'al. 67(1)*b*) s'applique.

Si on applique ce qui précède aux circonstances de l'espèce, au moment où le Dr Ramgotra a présenté sa demande de faillite, son intérêt de propriété dans le FERR est passé et a été dévolu au syndic en application du par. 71(2) *LFI*. L'intérêt futur et éventuel de Mme Ramgotra à titre de bénéficiaire désignée aux termes du FERR n'est pas tombé dans le champ d'application du par. 71(2), puisque la disposition de ce bien en faveur de l'épouse avait eu lieu avant la faillite. Il était loisible au syndic de demander l'annulation de cette disposition en vertu du par. 91(2) *LFI*. Comme je l'ai signalé précédemment, la disposition était inopposable aux termes du par. 91(2), et, en conséquence, l'intérêt futur et éventuel de Mme Ramgotra est passé et a été dévolu au syndic, qui est alors entré en possession de tous les intérêts de propriété rattachés au FERR. Par contre, le syndic ne pouvait partager le FERR entre les créanciers puisque ce bien continuait, malgré l'art. 91, d'être exempt en vertu de l'al. 67(1)*b*) *LFI*. En d'autres termes, l'art. 91 a pour rôle de ramener dans le patrimoine du failli en la possession du syndic les biens ayant fait l'objet d'une disposition. Par conséquent, bien que l'art. 91 puisse être invoqué pour mettre le syndic en pleine possession du FERR du Dr Ramgotra, il n'a aucune incidence sur la question de savoir si le FERR est exempt en vertu de l'al. 67(1)*b*).

L'appelante a fait valoir que, dans les cas où une disposition ayant pour effet de créer un bien exempt est annulée en vertu de l'art. 91, l'exemption elle-même ne vaut plus. En d'autres termes, l'existence d'une disposition valide est une condi-

ability of a s. 67(1)(*b*) exemption. This argument found favour in *Re Yewdale*, *supra*, where Tysoe J. stated at p. 204:

> While s. 67(1)(*b*) does provide an exemption for insurance annuities, it cannot be viewed in isolation. An asset can only be properly exempted under s. 67(1)(*b*) if the transaction creating the asset is valid. If the transaction is void under s. 91 (or any other provision), the exempted asset must be considered to revert to its form prior to the invalid transaction. If its prior form was not an exempted asset, s. 67(1)(*b*) is not applicable.

With respect, I cannot agree. The effect of s. 91 is to render certain settlements void against the trustee in bankruptcy. However, in the case of a life insurance policy, it must be remembered that what renders it exempt under s. 67(1)(*b*) is the designation of a beneficiary. According to s. 158(2) of *The Saskatchewan Insurance Act*, the exempt status of the life insurance policy continues so long as the designation is "in effect". To reach the conclusion of Tysoe J. in *Re Yewdale*, I would have to find that the designation in the case at bar is no longer "in effect" for the purpose of preventing distribution of the funds in the RRIF to Dr. Ramgotra's creditors, because the designation "is void against the trustee". However, I do not think that the fact a beneficiary designation is void against the trustee under federal legislation necessarily results in it no longer having effect vis-à-vis the claims of creditors under the provincial legislation which s. 67(1)(*b*) incorporates. As I stated above, ss. 91 and 67(1)(*b*) are directed at different stages of bankruptcy, and play different roles. Section 91 assists in identifying the property of the bankrupt which comes into the possession of the trustee, whereas s. 67(1)(*b*) is relevant in determining the property in the trustee's possession over which he or she may exercise his or her administrative powers. I therefore prefer a construction of ss. 91 and 67(1)(*b*) which recognizes their distinct roles in bankruptcy, as opposed to a construction which holds one to be a precondition of the other.

tion préalable logique à l'application d'une exemption fondée sur l'al. 67(1)*b*). Cet argument a été accepté dans *Re Yewdale*, précité, où le juge Tysoe a déclaré ceci, à la p. 204:

> [TRADUCTION] Même si l'al. 67(1)*b*) établit une exemption à l'égard des rentes d'assurance, il ne doit pas être analysé isolément. Un bien ne peut bénéficier à juste titre de l'exemption prévue par l'al. 67(1)*b*) que si l'opération créant ce bien est valide. Si cette opération est nulle suivant l'art. 91 (ou tout autre article), le bien exempté doit être considéré comme ayant repris la forme qu'il avait avant l'opération invalide. Si, sous sa forme originale, le bien n'était pas exempt, alors l'al. 67(1)*b*) ne s'applique pas.

En toute déférence, je ne suis pas d'accord. L'article 91 a pour effet de rendre certaines dispositions inopposables au syndic. Toutefois, lorsqu'il s'agit d'une police d'assurance-vie, il faut se rappeler que c'est la désignation d'un bénéficiaire qui la rend exempte en vertu de l'al. 67(1)*b*). Aux termes du par. 158(2) de *The Saskatchewan Insurance Act*, la police d'assurance-vie conserve sa qualité de bien exempt tant que la désignation est «en vigueur». Pour conclure comme l'a fait le juge Tysoe dans *Re Yewdale*, il me faudrait statuer que, parce qu'elle est «inopposable au syndic», la désignation faite en l'espèce n'est plus «en vigueur» et n'a pas pour effet d'empêcher le partage des fonds du FERR entre les créanciers du Dr Ramgotra. Toutefois, je ne crois pas que le fait qu'une désignation de bénéficiaire soit inopposable au syndic en vertu de la loi fédérale a nécessairement pour effet de rendre cette désignation inopérante à l'égard des réclamations des créanciers sous le régime des lois provinciales pertinentes incorporées par l'al. 67(1)*b*). Comme je l'ai dit plus tôt, l'art. 91 et l'al. 67(1)*b*) régissent des étapes différentes de la faillite et jouent des rôles distincts. L'article 91 aide à identifier les biens du failli qui passent en la possession du syndic, alors que l'al. 67(1)*b*) permet de déterminer ceux parmi ces biens sur lesquels le syndic peut exercer ses pouvoirs d'administration. Je préfère donc une interprétation de l'art. 91 et de l'al. 67(1)*b*) reconnaissant le rôle distinct de ces dispositions législatives en matière de faillite à une interprétation faisant de l'une de ces dispositions une condition préalable à l'application de l'autre.

52 Therefore, even though Dr. Ramgotra effected a void settlement under the second branch of s. 91(2) when he designated his wife as beneficiary of his RRIF, that does not allow the trustee to use the funds in the RRIF to satisfy the claims of creditors such as the appellant bank. The RRIF is an exempt asset pursuant to the provincial legislation incorporated into s. 67(1)(*b*), meaning that it is not property which is divisible among creditors. Given this, even though Mrs. Ramgotra's future contingent interest in the RRIF had passed into the possession of the trustee through the application of s. 91(2), the RRIF was property "incapable of realization" by the trustee pursuant to s. 40(1) *BIA*. Therefore, the trustee was obliged to return it to Dr. Ramgotra prior to applying for his discharge: *Thompson v. Coulombe* (1984), 54 C.B.R. (N.S.) 254 (Que. C.A.), at p. 257; *Zemlak (Trustee of) v. Zemlak* (1987), 66 C.B.R. (N.S.) 1 (Sask. C.A.), at pp. 9 and 11. Despite the fact that Dr. Ramgotra's settlement was void against the trustee, the exempt status of the RRIF is an absolute bar to the appellant bank's claim.

Par conséquent, même si le Dr Ramgotra a fait une disposition inopposable visée par le second volet du par. 91(2) lorsqu'il a désigné son épouse à titre de bénéficiaire de son FERR, cela n'autorisait pas le syndic à utiliser les fonds du FERR pour régler les réclamations des créanciers telle la banque appelante. Le FERR est un bien exempt aux termes des lois provinciales incorporées par l'al. 67(1)*b*), c'est-à-dire qu'il ne fait pas partie des biens constituant le patrimoine attribué aux créanciers. Pour cette raison, même si l'intérêt futur et éventuel de Mme Ramgotra dans le FERR était passé en la possession du syndic par l'application du par. 91(2), le FERR était un bien «non réalisable» par le syndic aux termes du par. 40(1) *LFI*. Par conséquent, le syndic était tenu, avant de demander sa libération, de retourner ce bien au Dr Ramgotra: *Thompson c. Coulombe* (1984), 54 C.B.R. (N.S.) 254 (C.A. Qué.), à la p. 257; *Zemlak (Trustee of) c. Zemlak* (1987), 66 C.B.R. (N.S.) 1 (C.A. Sask.), aux pp. 9 et 11. En dépit du fait que la disposition faite par le Dr Ramgotra soit inopposable au syndic, la qualité de bien exempt du FERR est un obstacle insurmontable à la réclamation de la banque appelante.

4. *The Application of Provincial Fraud Legislation*

4. *L'application des lois provinciales en matière de fraude*

53 In the lower courts which have considered the issue presented by the case at bar, considerable concern has been expressed over the fact that the conversion of a non-exempt asset into an exempt asset is a convenient means for a bankrupt to reduce the size of his or her estate available to creditors. Thus, the bankrupt's intention in effecting a transaction, and the impact of the transaction on creditors, have both been important factors directing the jurisprudence related to ss. 91 and 67(1)(*b*) *BIA*. Of course, in the case at bar, Dr. Ramgotra acted in good faith, and not for the purpose of defeating his creditors' claims. One could well imagine more troubling circumstances, however.

Devant les juridictions inférieures qui ont examiné la question soulevée par le présent pourvoi, de vives inquiétudes ont été exprimées à l'égard du fait que la conversion d'un bien non exempt en bien exempt est un moyen commode par lequel un failli peut réduire la taille du patrimoine disponible pour les créanciers. En conséquence, l'intention du failli lorsqu'il effectue l'opération et les conséquences de celle-ci pour les créanciers ont été des facteurs importants dans l'orientation de la jurisprudence relative à l'art. 91 et à l'al. 67(1)*b*) *LFI*. De toute évidence, en l'espèce, le Dr Ramgotra a agi de bonne foi et non dans le but de frustrer les réclamations de ses créanciers. Néanmoins, il serait bien possible d'imaginer des circonstances plus troublantes.

54 In her case comment on the Saskatchewan Court of Appeal decision in the instant case Lisa H. Kerbel Caplan ((1994), 26 C.B.R. (3d) 252),

Dans son commentaire sur la décision de la Cour d'appel de la Saskatchewan dans la présente affaire Lisa H. Kerbel Caplan ((1994), 26 C.B.R.

argues that at common law, the role of intention has focused "on the settlor's intention that the donee hold the settled property in its current form or in a traceable form", and not on the settlor's purpose in making a settlement (at p. 253). Like her, I am of the view that whether a settlor has acted in good faith, or for the purpose of defeating creditors, is not relevant to the question of whether a settlement has been made within s. 91.

In contrast, however, a settlor's intention is highly relevant where a settlement is being challenged under provincial (or territorial) fraud legislation: *Fraudulent Conveyances Act*, R.S.N. 1990, c. F-24, s. 3; *Assignments and Preferences Act*, R.S.N.S. 1989, c. 25, s. 4; *Assignments and Preferences Act*, R.S.N.B. 1973, c. A-16, s. 2; *Frauds on Creditors Act*, R.S.P.E.I. 1988, c. F-15, s. 2; *Civil Code of Québec*, art. 1631 ("Paulian Action"); *Assignments and Preferences Act*, R.S.O. 1990, c. A.33, s. 4(1), and *Fraudulent Conveyances Act*, R.S.O. 1990, c. F.29, s. 2; *The Fraudulent Conveyances Act*, R.S.M. 1987, c. F160, s. 2; *The Fraudulent Preferences Act*, R.S.S. 1978, c. F-21, s. 3; *Fraudulent Preferences Act*, R.S.A. 1980, c. F-18, s. 2; *Fraudulent Conveyance Act*, R.S.B.C. 1979, c. 142, s. 1, and *Fraudulent Preference Act*, R.S.B.C. 1979, c. 143, s. 3; *Fraudulent Preferences and Conveyances Act*, R.S.Y. 1986, c. 72, s. 2. (Note: the Northwest Territories has no legislation on fraudulent conveyances or preferences.) In fact, several lower courts have suggested that bad faith settlements, made for the purpose of defeating creditors, may be set aside under these statutes. Although it is not strictly necessary to decide this issue in the case at bar, since Dr. Ramgotra was found by Baynton J. to have acted in good faith, I am mindful of the need to provide some guidance to bankrupts, trustees, creditors and lower courts.

(3d) 252), prétend que, en common law, pour ce qui est de l'intention, on s'est attaché principalement à [TRADUCTION] «l'intention du disposant que le donataire détienne le bien en question dans sa forme originale ou sous une forme qui permette d'en suivre la trace», et non à l'objectif visé par le disposant lorsqu'il effectue la disposition (à la p. 253). Comme cet auteur, je suis d'avis que la question de savoir si un disposant a agi de bonne foi ou dans le but de frustrer ses créanciers n'est pas pertinente pour déterminer s'il y a eu disposition au sens de l'art. 91.

En revanche, l'intention du disposant est éminemment pertinente lorsqu'une disposition est contestée en vertu des lois provinciales (ou territoriales) en matière de fraude: *Fraudulent Conveyances Act*, R.S.N. 1990, ch. F-24, art. 3; *Assignments and Preferences Act*, R.S.N.S. 1989, ch. 25, art. 4; *Loi sur les cessions et préférences*, S.R.N.-B. 1973, ch. A-16, art. 2; *Frauds on Creditors Act*, R.S.P.E.I. 1988, ch. F-15, art. 2; *Code civil du Québec*, art. 1631 («action en inopposabilité»); *Loi sur les cessions et préférences*, L.R.O. 1990, ch. A.33, par. 4(1), et *Loi sur les cessions en fraude des droits des créanciers*, L.R.O. 1990, ch. F.29, art. 2; *Loi sur les transferts frauduleux de biens*, L.R.M. 1987, ch. F160, art. 2; *The Fraudulent Preferences Act*, R.S.S. 1978, ch. F-21, art. 3; *Fraudulent Preferences Act*, R.S.A. 1980, ch. F-18, art. 2; *Fraudulent Conveyance Act*, R.S.B.C. 1979, ch. 142, art. 1, et *Fraudulent Preference Act*, R.S.B.C. 1979, ch. 143, art. 3; *Loi sur les préférences et les transferts frauduleux*, L.R.Y. 1986, ch. 72, art. 2. (Remarque: les Territoires du Nord-Ouest n'ont aucun texte de loi sur les préférences ou transferts frauduleux). De fait, plusieurs juridictions inférieures ont avancé que les dispositions faites de mauvaise foi, dans le but de frustrer les créanciers, peuvent être annulées sous le régime de ces lois. Bien qu'il ne soit pas absolument nécessaire en l'espèce de trancher la question, étant donné que le juge Baynton a statué que le Dr Ramgotra avait agi de bonne foi, je suis conscient du besoin de donner certaines indications aux faillis, aux syndics, aux créanciers et aux juridictions inférieures.

56 Generally, where a conveyance has rendered property exempt from execution or seizure by creditors under provincial legislation, but the conveyance itself is void against those creditors pursuant to provincial fraud legislation, then the exemption is not in effect vis-à-vis those creditors. In terms of the law of bankruptcy, I would hold that a bankrupt cannot enjoy the benefit of a s. 67(1)(*b*) exemption where the property in question became exempt by reason of a fraudulent conveyance declared void pursuant to provincial law. I note that Houlden J. concluded in *Geraci* (trial), at p. 92, that a s. 67(1)(*b*) exemption has force even where the property became exempt under provincial law as a result of a fraudulent conveyance. I do not agree. In my view, a precondition to s. 67(1)(*b*) protection is that the property in question is exempt against the claims of creditors under provincial law. A fraudulent conveyance rendering property exempt is void against creditors, as illustrated by s. 3 of the Saskatchewan Act:

> **3.** . . . every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in a bank, company or corporation, or of any other property real or personal, made by a person at a time when he is in insolvent circumstances or is unable to pay his debts in full or knows that he is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice his creditors or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced. [Emphasis added.]

Since a fraudulent conveyance rendering property exempt is void against creditors by operation of provincial law, the property is not exempt from execution or seizure by creditors under provincial law, as required by s. 67(1)(*b*) *BIA*. Section 67(1)(*b*) therefore has no application, once a fraudulent conveyance is found to have occurred.

57 Can a life insurance beneficiary designation be set aside as a fraudulent conveyance of property?

De façon générale, lorsqu'un transfert a pour effet de rendre un bien exempt d'exécution ou de saisie par les créanciers sous le régime des lois provinciales pertinentes, mais que le transfert lui-même est inopposable à ces créanciers conformément aux lois provinciales relatives à la fraude, l'exemption est inopérante à l'égard de ces créanciers. En matière de droit de la faillite, je conclurais qu'un failli ne peut bénéficier de l'exemption prévue à l'al. 67(1)*b*) si le bien en question est devenu exempt par suite d'un transfert frauduleux déclaré nul conformément au droit provincial. Je note que le juge Houlden a conclu, dans *Geraci* (première instance), à la p. 92, que l'exemption prévue à l'al. 67(1)*b*) s'applique même lorsque le bien est devenu exempt sous le régime des lois provinciales par suite d'un transfert frauduleux. Je ne suis pas d'accord. À mon avis, une condition préalable à l'application de la protection offerte par l'al. 67(1)*b*) est que le bien en question soit à l'abri des réclamations des créanciers sous le régime des lois provinciales. Un transfert frauduleux ayant pour effet de rendre un bien exempt est inopposable aux créanciers, comme le fait voir l'art. 3 de la Loi de la Saskatchewan:

> [TRADUCTION] **3.** . . . les donations, transferts, cessions, remises ou paiements de quelque bien que ce soit, réel ou personnel — chatels ou effets, lettres de change, obligations, billets ou titres, ou actions, dividendes, primes ou bonis d'une banque, d'une compagnie ou d'une personne morale —, qu'effectue une personne insolvable ou incapable au moment de l'opération de payer la totalité de ses dettes — ou qui se sait sur le point d'être insolvable — en vue de frustrer, d'entraver, de retarder ou de léser ses créanciers ou certains d'entre eux sont inopposables aux créanciers concernés. [Je souligne.]

Étant donné qu'un transfert frauduleux ayant pour effet de rendre un bien exempt est inopposable aux créanciers par l'application des lois provinciales, le bien en question n'est pas, comme l'exige l'al. 67(1)*b*) *LFI*, exempt d'exécution ou de saisie par les créanciers sous le régime des lois provinciales. L'alinéa 67(1)*b*) ne s'applique donc pas si un transfert est jugé frauduleux.

Est-il possible de faire annuler, en tant que transfert frauduleux de biens, la désignation d'un

This question has generated some conflict in the lower courts. In *Geraci* (trial), for example, Houlden J. found at p. 89 that the beneficiary designation could be attacked under s. 2 of Ontario's Act, since it was a conveyance made with the fraudulent intent of defeating creditors. The Court of Appeal, *per* Jessup J.A., agreed, at p. 259:

> I agree with the learned trial Judge that the declaration made by the bankrupt, changing the beneficiary of his policy of insurance to his wife while he was insolvent, was a fraudulent conveyance within the meaning of s. 2 of The Fraudulent Conveyances Act and, if it were necessary to do so, I would hold that it was therefore fraudulent and void against his creditors and that such a void designation does not attract the protection against creditors provided by either s. 162 or s. 157 of the present Insurance Act.

Geraci was not followed on this point in *Sovereign General Insurance Co. v. Dale* (1988), 32 B.C.L.R. (2d) 226 (S.C.). There, the defendant had transferred the funds from a non-exempt RRSP into an insurance annuity which was exempt from execution or seizure under s. 147 of British Columbia's *Insurance Act*, R.S.B.C. 1979, c. 200, because his wife was the designated beneficiary of the plan. The plaintiff, who had obtained judgment against the defendant, sought to set aside the transfer of the RRSP funds into the annuity on the basis that it was a fraudulent conveyance. Gibbs J. held that the defendant had the necessary intent for fraud because he effected the fund transfer in order to hinder the plaintiff from realizing on its judgment. He then turned to the question of whether the transfer was a "disposition of property" which could be set aside under the British Columbia's *Fraudulent Conveyance Act*. After stating that Jessup J.A.'s reasons in *Geraci* were obiter on this point, and that the issue remained unresolved, Gibbs J. held at pp. 230-31:

bénéficiaire d'une assurance-vie? Cette question a donné lieu à des opinions divergentes dans les juridictions inférieures. Dans *Geraci* (première instance), par exemple, le juge Houlden a conclu, à la p. 89, que la désignation d'un bénéficiaire pouvait être attaquée aux termes de l'art. 2 de la Loi ontarienne, puisqu'il s'agit d'un transfert fait dans l'intention frauduleuse de frustrer les créanciers. Le juge Jessup, s'exprimant pour la Cour d'appel, a souscrit à cette conclusion, à la p. 259:

> [TRADUCTION] Je suis d'accord avec le juge de première instance que la déclaration qu'a faite le failli afin de désigner son épouse à titre de bénéficiaire de sa police d'assurance, pendant qu'il était insolvable, était une cession frauduleuse au sens de l'art. 2 de la Loi sur les cessions en fraude des droits des créanciers. De plus, s'il était nécessaire de le faire, je conclurais que cette désignation par le failli était en conséquence frauduleuse et inopposable à ses créanciers, et qu'une telle désignation inopposable ne jouit pas de la protection contre les créanciers offerte par l'art. 162 ou l'art. 157 de l'actuelle Loi sur les assurances.

L'arrêt *Geraci* n'a pas été suivi sur ce point dans *Sovereign General Insurance Co. c. Dale* (1988), 32 B.C.L.R. (2d) 226 (C.S.). Dans cette affaire, le défendeur avait transféré les fonds d'un REER non exempt dans une rente d'assurance qui, en vertu de l'art. 147 de l'*Insurance Act* de la Colombie-Britannique, R.S.B.C. 1979, ch. 200, était exempte d'exécution ou de saisie parce que son épouse était la bénéficiaire désignée du régime. La demanderesse, qui avait obtenu jugement contre le défendeur, a demandé l'annulation de la conversion en rente des fonds des REER en plaidant qu'il s'agissait d'un transfert frauduleux. Le juge Gibbs a conclu que le défendeur avait eu l'intention requise en matière de fraude puisqu'il avait effectué le transfert des fonds dans le but d'empêcher la demanderesse d'exécuter son jugement. Le juge s'est ensuite demandé si le transfert était une «disposition de biens» qui pouvait être annulée aux termes de la *Fraudulent Conveyance Act* de la Colombie-Britannique. Après avoir déclaré que les motifs du juge Jessup sur ce point dans l'arrêt *Geraci* constituaient une opinion incidente et que la question n'avait pas encore reçu de réponse, le juge Gibbs a statué ainsi, aux pp. 230 et 231:

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In my opinion, it is not appropriate to look at the consequences that flow from the naming of the wife as beneficiary under the insurance contract to determine whether an interest in property has been disposed of. That seems to have happened in a number of the cases cited. With respect, I think that is the wrong approach for whatever statutory protection might or might not be afforded to the "interest" conveyed cannot be determinative of what the "interest" is. In my view, the task must be to inquire whether the "interest", if that is the correct terminology, has any of the commonly understood incidents of property. When I follow that course I am led to the conclusion that it does not.

. . .

Until a vesting occurs, the expression "interest" is probably nothing more than a convenient label to describe a future expectation which may never become a reality; for instance, the insured may change the beneficiary, or the beneficiary may predecease the insured. Until vesting, if that ever occurs, the expectation of the beneficiary is not real property, or personalty; it is not a chose in action; it is not merchantable; it is not exigible. At the most it is expectancy based upon a contingency. It has been held to be within the broad definition of property in the Bankruptcy Act which includes a future contingent interest incident to property, but it does not follow that it is subsumed within the single word "property" in the Fraudulent Conveyance Act. In my opinion, it is not.

Thus, according to Gibbs J., the transfer of funds at issue was not a conveyance of "property" which could be set aside under the British Columbia Act.

59 I do not intend to resolve this issue in the case at bar. However, I would make the following observation. The technical question of whether a life insurance beneficiary designation is a "property conveyance" does not arise under art. 1631 of the *Civil Code of Québec*, which allows creditors to set aside fraudulent "juridical acts":

1631. A creditor who suffers prejudice through a juridical act made by his debtor in fraud of his rights, in particular an act by which he renders or seeks to render

[TRADUCTION] À mon avis, il ne convient pas d'examiner les conséquences qui découlent de la désignation de l'épouse à titre de bénéficiaire aux termes du contrat d'assurance pour déterminer s'il a été disposé d'un intérêt dans un bien. Il semble pourtant que ce soit ce qu'on a fait dans un certain nombre des affaires citées. Avec égards, je ne crois pas que ce soit la bonne méthode, car la nature de la protection d'origine législative dont pourrait bénéficier ou non l'«intérêt» transféré ne détermine pas la nature de cet «intérêt». À mon avis, il faut plutôt se demander si l'«intérêt», si c'est bien là le terme qui convient, a l'un ou l'autre des attributs communément reconnus de la propriété. Lorsque j'applique cette analyse, j'en arrive à la conclusion que non.

. . .

Jusqu'à ce qu'il y ait dévolution, l'expression «intérêt» n'est probablement rien d'autre qu'une étiquette commode pour décrire une attente future, qui pourrait ne jamais se concrétiser; en effet, l'assuré pourrait désigner un bénéficiaire différent, ou le bénéficiaire désigné pourrait décéder avant l'assuré. Jusqu'à ce qu'il y ait dévolution, si effectivement cela se produit, l'attente du bénéficiaire ne constitue pas un bien réel ou un bien personnel; elle n'est pas un droit incorporel; elle n'a pas de valeur marchande et elle n'est pas exigible. Tout au plus repose-t-elle sur une éventualité. On a dit de cette attente qu'elle est visée par la définition générale de «*property*» [«biens» en français] dans la Loi sur la faillite, qui comprend un intérêt futur et éventuel se rattachant à des biens, mais il ne s'ensuit pas pour autant qu'elle est subsumée dans le seul mot «*property*» figurant dans la Fraudulent Conveyance Act. À mon avis, elle ne l'est pas.

Ainsi, selon le juge Gibbs, le transfert de fonds en question n'était pas un transfert de «biens» susceptible d'être annulé en vertu de la Loi de la Colombie-Britannique.

Je n'entends pas résoudre cette question en l'espèce, mais je ferai néanmoins la remarque suivante. La question spécifique de savoir si la désignation d'un bénéficiaire d'une assurance-vie est un «transfert de biens» ne se pose pas sous le régime de l'art. 1631 du *Code civil du Québec*, qui permet aux créanciers de faire annuler des «actes juridiques» frauduleux:

1631. Le créancier, s'il en subit un préjudice, peut faire déclarer inopposable à son égard l'acte juridique que fait son débiteur en fraude de ses droits, notamment

himself insolvent, or by which, being insolvent, he grants preference to another creditor may obtain a declaration that the act may not be set up against him.

However, the other provincial statutes all refer to some sort of "conveyance" or "disposition" of "property" with the "intent to defeat" creditors' claims. All the provincial fraud provisions are clearly remedial in nature, and their purpose is to ensure that creditors may set aside a broad range of transactions involving a broad range of property interests, where such transactions were effected for the purpose of defeating the legitimate claims of creditors. Therefore, the statutes should be given the fair, large and liberal construction and interpretation that best ensures the attainment of their objects, as required by provincial statutory interpretation legislation (see, for example, *The Interpretation Act, 1993*, S.S. 1993, c. I-11.1, s. 10). I agree with the following observation by Professor Dunlop in *Creditor-Debtor Law in Canada* (2nd ed. 1995), at p. 598, that the purpose of fraudulent conveyance legislation:

> . . . is to strike down all conveyances of property made with the intention of delaying, hindering or defrauding creditors and others except for conveyances made for good consideration and *bona fide* to persons not having notice of such fraud. The legislation is couched in very general terms and should be interpreted liberally. [Emphasis added.]

Given the need for a broad and liberal interpretation, I would suggest that there is a strong case for concluding that a life insurance beneficiary designation is both a "juridical act", and a "disposition" or "conveyance" of "property".

5. *The Application of the Statute of Elizabeth*

In the Court of Appeal, Jackson J.A. suggested that *An Acte agaynst fraudulent Deedes Gyftes Alienations, &c. (Statute of Elizabeth)*, 1571 (Eng.) 13 Eliz. 1, c. 5, would be available to challenge fraudulent transactions rendering property exempt from execution or seizure. The *Statute of Elizabeth* is the model for the fraudulent conveyance legisla-

l'acte par lequel il se rend ou cherche à se rendre insolvable ou accorde, alors qu'il est insolvable, une préférence à un autre créancier.

Cependant, les autres lois provinciales font toutes état de quelque forme de «transfert» ou «aliénation» de «biens» dans «l'intention de frustrer» les réclamations des créanciers. Toutes les dispositions législatives provinciales en matière de fraude visent manifestement à créer un recours, et elles ont pour objet de permettre aux créanciers de faire annuler une vaste gamme d'opérations mettant en cause un large éventail d'intérêts de propriété, lorsque de telles opérations ont été effectuées dans le but de frustrer leurs réclamations légitimes. Les lois en question devraient donc recevoir une interprétation équitable, large et libérale qui favorise la réalisation de leur objet, comme l'exigent les diverses lois d'interprétation provinciales (voir, par exemple, *The Interpretation Act, 1993*, S.S. 1993, ch. I-11.1, art. 10). Je suis d'accord avec l'observation suivante du professeur Dunlop, dans *Creditor-Debtor Law in Canada* (2e éd. 1995), à la p. 598, qui affirme que les lois relatives aux transferts frauduleux ont pour objet:

> [TRADUCTION] . . . de permettre l'annulation de tous les transferts de biens effectués dans l'intention de retarder, d'entraver ou de frauder les créanciers et d'autres personnes, sauf les transferts faits de bonne foi et avec contrepartie valable à des personnes n'ayant aucune connaissance de cette fraude. Ces lois sont rédigées en termes très généraux et devraient être interprétées de manière libérale. [Je souligne.]

Étant donné l'interprétation large et libérale qu'il faut donner, je dirais qu'il y a de bonnes raisons de conclure que la désignation d'un bénéficiaire d'une assurance-vie est à la fois un «acte juridique» et une «aliénation» ou un «transfert» de «biens».

5. *L'application du Statute of Elizabeth*

En Cour d'appel, le juge Jackson a avancé que la loi intitulée *An Acte agaynst fraudulent Deedes Gyftes Alienations, &c. (Statute of Elizabeth)*, 1571 (Ang.) 13 Eliz. 1, ch. 5, pourrait être invoquée à l'encontre d'opérations frauduleuses ayant pour effet de rendre des biens exempts d'exécution ou de saisie. Le *Statute of Elizabeth* est le texte

tion of the common law provinces, as discussed above. Its archaic language states that:

> . . . all and every Feoffement Gyfte Graunte Alienation Bargayne and Conveyaunce of Landes Tenements Hereditams Goodes and Catalls or of any of them [[which were] contryved of Malyce Fraude Covyne Collusion or Guyle [with the] Purpose and Intent to delaye hynder or defraude Creditors] [shall be] clearely and utterly voyde frustrate and of none Effecte.

In *Nicholson v. Milne* (1989), 74 C.B.R. (N.S.) 263 (Alta. Q.B.), Virtue J. considered the applicability of the *Statute of Elizabeth* in a situation where the defendants had each rendered RRSP and mutual funds exempt under Alberta's *Insurance Act*, R.S.A. 1980, c. I-5, s. 265, by transferring the funds into life insurance policies under which family members were named as beneficiaries. The issue before Virtue J. was whether the transfers could be set aside under Alberta's *Fraudulent Preferences Act*, or alternatively under the *Statute of Elizabeth*. He observed that the principal difference between the two statutes was that the provincial legislation required the gift or conveyance to have been made when the debtor was insolvent, was unable to pay his or her debts in full, or knew that he or she was on the eve of insolvency, whereas this was not a requirement under the *Statute of Elizabeth*. He then decided to proceed under the *Statute of Elizabeth*, in order to avoid dealing with the insolvency issue. He found that the fund transfers were effected for the purpose of defeating creditors, and then decided that the transfers, and the beneficiary designations, were "conveyances" subject to the *Statute of Elizabeth*, at p. 274:

> The term "Conveyance" (like the term transfer) is itself wide enough to encompass every method of disposing of, or parting with, property or an interest therein, absolutely or conditionally. The word is of general meaning and, given a liberal interpretation, includes the transactions here which resulted in the transfer of entitlement to the benefits of the R.R.S.P. property from

qui, dans les provinces de common law, a servi de modèle pour la rédaction des lois relatives aux transferts frauduleux dont il a été question précédemment. Rédigée dans un langage archaïque, cette loi prévoit ceci:

> [TRADUCTION] . . . tous les fieffements, donations, concessions, aliénations, marchés et transferts de bien-fonds, tènements, héritages, marchandises et chatels, ou de l'un d'eux, [faits avec malice, fraude, collusion, duperie ou supercherie [dans l']intention de retarder, d'entraver ou de frauder les créanciers sont] clairement et absolument nuls et de nul effet.

Dans *Nicholson c. Milne* (1989), 74 C.B.R. (N.S.) 263 (B.R. Alb.), le juge Virtue s'est penché sur l'applicabilité du *Statute of Elizabeth* dans une situation où les différents défendeurs avaient rendu des REER et des fonds mutuels exempts sous le régime d'une loi de l'Alberta, l'*Insurance Act*, R.S.A. 1980, ch. I-5, art. 265, en transférant les sommes en cause dans des polices d'assurance-vie dont ils avaient désigné des membres de leur famille respective bénéficiaires. La question dont était saisi le juge Virtue était de savoir si ces transferts pouvaient être annulés en vertu de la *Fraudulent Preferences Act* de l'Alberta ou, subsidiairement, en vertu du *Statute of Elizabeth*. Le juge a souligné que la principale différence entre les deux lois était que la loi provinciale exigeait que les donations ou transferts aient été faits lorsque le débiteur était insolvable ou incapable de payer la totalité de ses dettes, ou encore à un moment où il se savait sur le point d'être insolvable, alors que le *Statute of Elizabeth* ne posait pas cette exigence. Il a alors décidé d'appliquer le *Statute of Elizabeth* afin d'éviter d'avoir à examiner la question de l'insolvabilité. Il a d'abord conclu que les transferts de fonds avaient été effectués dans le but de frustrer les créanciers, puis, à la p. 274, il a statué que les transferts et les désignations de bénéficiaires étaient des «transferts» visés par le *Statute of Elizabeth*:

> [TRADUCTION] Le mot «transfert» (tout comme le mot cession) est lui-même suffisamment large pour englober tous les moyens par lesquels une personne dispose ou se départit d'un bien ou d'un intérêt sur celui-ci, de façon absolue ou conditionnelle. Ce mot a un sens général et, si on l'interprète de manière libérale, il vise aussi les opérations effectuées en l'espèce et qui ont eu pour effet

the debtor to another in such a way as to remove it from execution by creditors. In my view, such a transaction comes within the meaning of "conveyance", as that term is used in the Statute of Elizabeth.

Thus, the fraudulent transfers and beneficiary designations were void, and the funds in the life insurance policies were not exempt from execution or seizure under the *Insurance Act* (see also *Technurbe Building Construction Ltd. v. McKinley* (1989), 76 C.B.R. (N.S.) 106 (Alta. Q.B.)).

Several of the provincial fraudulent conveyance statutes impose an insolvency requirement, like that contained in Alberta's Act: Nova Scotia, New Brunswick, Prince Edward Island, Saskatchewan and Yukon. Thus, assuming without deciding that the *Statute of Elizabeth* remains in force in those jurisdictions, it would allow creditors to challenge fraudulent conveyances without having to prove that, at the time of the conveyance, the debtor was insolvent, was unable to pay his or her debts in full, or knew that he or she was on the eve of insolvency.

There remains some controversy as to whether the *Statute of Elizabeth* is in force in all of the common law provinces and territories. Professor Dunlop discusses this issue in *Creditor-Debtor Law in Canada*, *supra*, and suggests at p. 597 that the Statute has likely been repealed in British Columbia, Manitoba, Newfoundland and Ontario, where pure fraudulent conveyance legislation (i.e., legislation without the insolvency requirement) has been enacted. Since the matter was not argued in the case at bar, it would be inappropriate to decide here whether the *Statute of Elizabeth* remains in force in any particular jurisdiction. Suffice it to say that if the Statute is in force in a province or territory, then it will be available to challenge fraudulent conveyances rendering property exempt from execution or seizure under provincial law. I should add that my comments above concerning the issue of whether a life insurance beneficiary designation

de transférer le droit aux prestations du REER du débiteur à une autre personne, de telle façon que ce bien a été soustrait aux mesures d'exécution des créanciers. À mon avis, une telle opération est visée par le mot «transfert» utilisé dans le Statute of Elizabeth.

En conséquence, les désignations de bénéficiaire et transferts frauduleux étaient nuls, et les fonds des polices d'assurance-vie n'étaient pas exempts d'exécution ou de saisie en vertu de l'*Insurance Act* (voir également *Technurbe Building Construction Ltd. c. McKinley* (1989), 76 C.B.R. (N.S.) 106 (B.R. Alb.)).

Plusieurs lois provinciales relatives aux transferts frauduleux imposent une exigence d'insolvabilité analogue à celle figurant dans la Loi de l'Alberta: Nouvelle-Écosse, Nouveau-Brunswick, Île-du-Prince-Édouard, Saskatchewan et Yukon. Par conséquent, à supposer — sans en décider — que le *Statute of Elizabeth* soit toujours en vigueur dans ces provinces et ce territoire, ce texte permettrait aux créanciers de contester des transferts frauduleux sans avoir à prouver que, au moment où ceux-ci ont été effectués, le débiteur était insolvable ou incapable de payer la totalité de ses dettes, ou encore qu'il se savait sur le point d'être insolvable.

Il subsiste une certaine controverse quant à savoir si le *Statute of Elizabeth* est en vigueur dans l'ensemble des provinces et territoires de common law. Le professeur Dunlop analyse cette question dans *Creditor-Debtor Law in Canada*, *op. cit.*, et avance, à la p. 597, que le Statute a vraisemblablement été abrogé en Colombie-Britannique, au Manitoba, à Terre-Neuve et en Ontario, provinces où ont été édictées des mesures législatives visant les transferts purement frauduleux (c'est-à-dire ne comportant d'exigence d'insolvabilité). Comme la question n'a pas été débattue en l'espèce, il serait inopportun de décider si le *Statute of Elizabeth* est encore en vigueur dans une province donnée. Qu'il suffise de dire que si le Statute est en vigueur dans une province ou dans un territoire il pourra alors être invoqué pour contester des transferts frauduleux ayant pour effet de rendre des biens exempts d'exécution ou de saisie sous le régime des lois

is a "property conveyance" apply equally in the case of the *Statute of Elizabeth*.

6. *Conclusion*

64 When Dr. Ramgotra transferred the funds from his two RRSPs into an RRIF under which his wife was the designated beneficiary, the funds became exempt from execution or seizure by reason of s. 67(1)(*b*) *BIA*, when read in conjunction with ss. 2(kk)(vii) and 158(2) of *The Saskatchewan Insurance Act*. Even though the beneficiary designation was a settlement within s. 91 *BIA*, and was void against the trustee in bankruptcy pursuant to the second branch of s. 91(2), the RRIF remained exempt from the claims of Dr. Ramgotra's creditors and, in particular, the appellant bank.

VI. Disposition

65 The appeal is therefore dismissed with costs to the respondents.

Appeal dismissed with costs.

Solicitors for the appellant: Gauley & Co., Saskatoon.

Solicitors for the respondent North American Life Assurance Company: MacDermid, Lamarsh, Saskatoon.

Solicitors for the respondent Balvir Singh Ramgotra: Goldstein, Jackson, Gibbings, Saskatoon.

provinciales applicables. J'ajouterais que les commentaires que j'ai formulés plus tôt sur la question de savoir si la désignation d'un bénéficiaire d'une assurance-vie constitue un «transfert de biens» s'appliquent également en ce qui concerne le *Statute of Elizabeth*.

6. *Conclusion*

Lorsque le Dr Ramgotra a transféré les fonds de ses deux REER dans un FERR dont son épouse a été désignée bénéficiaire, ces sommes sont devenues exemptes d'exécution ou de saisie par l'effet conjugué de l'al. 67(1)*b*) *LFI* ainsi que du sous-al. 2kk)(vii) et du par. 158(2) de *The Saskatchewan Insurance Act*. Même si la désignation d'un bénéficiaire était une disposition au sens de l'art. 91 *LFI*, et qu'elle était inopposable au syndic conformément au second volet du par. 91(2) *LFI*, le FERR est demeuré à l'abri des réclamations des créanciers du Dr Ramgotra et, en particulier, de celle de la banque appelante.

VI. Dispositif

Le pourvoi est par conséquent rejeté avec dépens en faveur des intimés.

Pourvoi rejeté avec dépens.

Procureurs de l'appelante: Gauley & Co., Saskatoon.

Procureurs de l'intimée la Nord-Américaine, compagnie d'assurance-vie: MacDermid, Lamarsh, Saskatoon.

Procureurs de l'intimé Balvir Singh Ramgotra: Goldstein, Jackson, Gibbings, Saskatoon.

TAB 2

COURT OF APPEAL FOR ONTARIO

CITATION: Montor Business Corporation v. Goldfinger, 2016 ONCA 406
DATE: 20160530
DOCKET: C57879

Cronk, Pepall and Lauwers JJ.A.

In the Matter of the Bankruptcy of Summit Glen Waterloo/2000 Developments Inc., of the City of Toronto, in the Province of Ontario

BETWEEN

A. Farber & Partners Inc., the Trustee of the Bankruptcy Estate of Montor Business Corporation, Annopol Holdings Limited and Summit Glen Brantford Holdings Inc.

Applicant (Appellant/ Respondent by way of cross-appeal)

and

Morris Goldfinger, Goldfinger Jazrawy Diagnostic Services Ltd., Summit Glen Bridge Street Inc., Mahvash Lechcier-Kimel, Annopol Holdings Limited and Summit Glen Brantford Inc.

Respondents (Respondents/Appellants by way of cross-appeal)

Patrick Shea and Brent Arnold, for the appellant/respondent by way of cross-appeal

Maurice J. Neirinck and Michael McQuade, for the respondents/appellants by way of cross-appeal

Heard: October 14 and 15, 2015

On appeal from the judgment of Justice David M. Brown of the Superior Court of Justice, dated October 28, 2013, with reasons reported at 2013 ONSC 6635, 8 C.B.R. (6th) 200.

Pepall J.A.:

INTRODUCTION

[1] A failed relationship between an investor, Dr. Morris Goldfinger, and a real estate developer, Jack Lechcier-Kimel ("Kimel"), and the subsequent bankruptcy of several of Kimel's companies has generated three appeals. The appeals involve claims to funds asserted by A. Farber & Partners Inc. ("Farber"), the Trustee in bankruptcy of five companies: Annopol Holdings Limited ("Annopol"), Summit Glen Brantford Holdings Inc. ("SG Brantford"), Summit Glen Waterloo/2000 Developments Inc. ("SG Waterloo"), Summit Glen Group of Companies Inc. ("SG Group") and Montor Business Corporation ("Montor"). All but Montor were companies owned and controlled by Kimel or his then-spouse, Mahvash Lechcier-Kimel ("Mahvash").

[2] In the primary appeal, which is the subject matter of these reasons, Farber, in its capacity as Trustee of Annopol, challenges the trial judge's refusal to set aside transactions arising from a settlement between Goldfinger, Kimel and some of Kimel's companies. In particular, Farber seeks to set aside certain transactions arising from the settlement: (1) payments totalling $2.5 million to Goldfinger from Annopol (the "Payments"); and (2) mortgages granted to Goldfinger by SG Brantford and Summit Glen Bridge Street Inc. ("SG Bridge") over their respective properties, and Annopol's subordination of mortgage security in favour of Goldfinger (the "Brantford/Bridge 2008 Transactions").

[3] The trial judge rejected Farber's assertions that the transactions were:

- transfers at undervalue under s. 96 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "*BIA*");
- unjust preferences under s. 4 of the *Assignments and Preferences Act*, R.S.O. 1990, c. A.33 (the "*APA*");
- fraudulent conveyances under s. 2 of the *Fraudulent Conveyances Act*, R.S.O. 1990, c. F.29 (the "*FCA*");
- oppressive under s. 248 of the Ontario *Business Corporations Act*, R.S.O. 1990, c. B.16 (the "*OBCA*"); and
- an unjust enrichment.

[4] Goldfinger cross-appeals on the basis that the trial judge erred in setting aside a $471,000 payment in his favour from SG Brantford. The trial judge found that the payment was contrary to s. 2 of the *FCA* and oppressive under s. 248 of the *OBCA*.

[5] In the remaining two appeals, both Farber and Goldfinger or his company, 1830994 Ontario Ltd., take issue with the treatment of certain claims asserted in the various bankruptcy proceedings. These appeals are addressed in separate sets of reasons released contemporaneously with these reasons, bearing court file numbers C57898 and C58356.

[6] For the reasons that follow, I would dismiss this appeal and Goldfinger's cross-appeal.

BACKGROUND FACTS

A. The Parties' Relationship

[7] Kimel was a real estate developer. He incorporated numerous companies for that purpose. He attracted investors to lend to and invest in his companies. Those companies would then lend money to other Kimel companies that would in turn acquire real estate. The investor loans were to be repaid from the proceeds generated from selling the real estate. The investors would also receive a portion of the profit generated from the sales.

[8] Goldfinger was not a real estate developer; he was a radiologist. He was also a good friend of Kimel. He decided to lend and invest money into some of Kimel's companies. From February 1999 to December 2005, Goldfinger lent approximately $6.5 million to Kimel's companies, $2,956,000 of which he claimed was advanced to Annopol. Annopol's affairs were directed by Kimel. Annopol then lent these funds to other Kimel companies for the purpose of acquiring properties in the Kitchener/Waterloo and Brantford areas.

[9] The terms of the arrangements with Goldfinger were not reduced to writing. Goldfinger described the funds advanced as "interest-free loans" and claimed that he was engaged in a "joint venture" with Kimel.

[10] In 2007, the relationship between Goldfinger and Kimel broke down. Goldfinger discovered that Kimel had misled him and that many of the properties that had been acquired were encumbered by mortgages of which he was unaware. He sought explanations and the return of his money, but Kimel stalled. Goldfinger retained counsel who, in letters dated November 12 and 13, 2007, threatened litigation. Goldfinger prepared a draft affidavit in support of a request for a court-appointed receiver over some of Kimel's companies, including Annopol. In that affidavit, he asserted that he had repeatedly requested an accounting from Kimel without success and had concluded that Kimel had not been dealing in good faith. Kimel also retained counsel.

B. The First Settlement

[11] The parties commenced settlement negotiations and negotiated the dissolution of their business relationship (the "First Settlement"). Goldfinger and Kimel reached a resolution independently and arrived at an amount to be paid to Goldfinger, but the overall structure and details of the settlement were negotiated with the assistance of counsel. The parties agreed that Goldfinger would withdraw from the various projects and would be repaid his shareholder loans of $6.5 million, plus an additional $5 million in return for his shares in the various companies. At the time, this latter sum was thought to represent his equity in the properties.

[12] As agreed, between December 2007 and January 2008, Annopol paid $2.5 million to Goldfinger. The Payments were broken down as follows. On December 5, 2007, Annopol transferred $1.5 million to Goldfinger. Annopol also issued four cheques in his favour dated December 12 and 28, 2007 in the amount of $300,000 each and December 21, 2007 and January 10, 2008 in the amount of $200,000 each, for a total of $1 million. Each cheque bore the notation "re-purchase shares". Annopol relied on transfers of funds from other Summit Glen entities to cover the amounts paid to Goldfinger.

[13] The settlement was memorialized in a Memorandum of Agreement (the "Memorandum") dated December 11, 2007 but signed on May 20, 2008 and amended on June 6, 2008. The terms of the Memorandum originated around the time that the aforesaid payments were made. Goldfinger testified that the Payments of $2.5 million were consideration in contemplation of the settlement. Kimel also stated that the Payments were made in anticipation of the settlement.

[14] The parties to the Memorandum were: Goldfinger, Kimel, Mahvash, Annopol, and enumerated Summit Glen companies including SG Brantford and SG Bridge (collectively, the "Summit Glen Companies").

[15] The Memorandum provided that:

- Notwithstanding that shares of the Summit Glen Companies had not been formally issued, Goldfinger was, and for all purposes deemed to be, the

legal and beneficial owner of 50% of the share capital of each of the Summit Glen Companies.

- The Summit Glen Companies acknowledged the $6.5 million debt to Goldfinger which, in aggregate, was allocated to each of them in separate amounts. The advances were described as shareholder loans.
- The Memorandum accurately recorded the parties' understanding of the discussions that had taken place.
- Each of the Summit Glen Companies was to deliver an interest-free promissory note for its share of the $6.5 million to Goldfinger, one-half payable on December 11, 2008 and the other half payable on December 11, 2009.
- Kimel and each of the Summit Glen Companies were to guarantee the payment of $6.5 million.
- The Summit Glen Companies were to provide $6.5 million in collateral mortgages to Goldfinger. These included mortgages on 176 Henry St., Brantford, which was owned by SG Brantford, and on 70 Bridge St. W., Kitchener, which was owned by SG Bridge.
- Kimel would purchase Goldfinger's shares for $5 million. The parties agreed that the $2.5 million already paid represented a partial payment of the purchase price. The remainder was to be paid by a $1.5 million secured promissory note and a $1 million unsecured promissory note.

- Each of the Summit Glen Companies, including SG Brantford and SG Bridge, was to guarantee payment to Goldfinger of these secured and unsecured promissory notes and was to give collateral third mortgages as security for the guarantees. SG Brantford granted a third mortgage over 176 Henry St. in Brantford and SG Bridge granted a third mortgage over 70 Bridge St. W. in Kitchener to secure the sum of $1.5 million.
- Annopol, Kimel and Mahvash postponed all of their claims against the Summit Glen Companies, including SG Brantford and SG Bridge, in favour of Goldfinger.
- Annopol also postponed its mortgages, including those over 176 Henry St. and 70 Bridge St. W., in favour of Goldfinger (the "Annopol Subordinations").
- Kimel and the Summit Glen Companies provided Goldfinger with an indemnity and they, together with Mahvash and Annopol, also provided him with a release.

[16] Lawyers acted for the parties on the settlement, but Goldfinger's lawyers testified that Kimel and Goldfinger had agreed on the $2.5 million figure prior to approaching them.

[17] The settlement "was designed in such a way as to repay to Goldfinger the amounts already lent to the SG Companies and to enable Goldfinger to extract

an amount representing his notional equity or profit in the various real estate developments": reasons, at para. 213.

[18] The Memorandum transactions closed in June 2008 and Goldfinger received the promissory notes, guarantees, postponements and mortgages due to him pursuant to the terms of the Memorandum.

C. The Brantford/Bridge 2008 Transactions

[19] Prior to the closing, the 176 Henry St. property owned by SG Brantford was subject to: a first mortgage of $2.85 million in favour of First National Financial Corporation ("First National"); a second mortgage of $450,000 in favour of Montor; and a third mortgage of $750,000 in favour of Annopol. Montor was owned by Jack Perelmuter, an accountant who had provided accounting services to Kimel's companies.

[20] As a result of the settlement, SG Brantford provided Goldfinger with two mortgages over 176 Henry St. and Annopol agreed to postpone its third mortgage in favour of Goldfinger's two mortgages. As such, Goldfinger's mortgages were in third and fourth position on the property and Annopol's mortgage was in fifth place.

[21] The 70 Bridge Street property owned by SG Bridge was subject to a mortgage in favour of Annopol. As a result of the settlement, SG Bridge provided

Goldfinger with two mortgages over 70 Bridge Street and Annopol postponed its mortgage in favour of Goldfinger's two mortgages.

D. Events Surrounding the Bankruptcies

[22] By July 2008, Goldfinger alleged that Kimel had breached the terms of the Memorandum and he proceeded to serve demand notices on some of Kimel's companies.

[23] Meanwhile, the global credit market crisis was brewing, with matters coming to a head with Lehman Brothers' Chapter 11 filing in mid-September 2008.

[24] In November 2008, the 176 Henry St. property had to be refinanced, as the first mortgage in favour of First National was due. It was renegotiated and the principal sum secured was increased. As part of the transaction, Kimel signed an agreement on behalf of Montor to subordinate its second mortgage so that the principal amount of the first mortgage could be increased. SG Brantford then paid $471,000 to Goldfinger, and his third and fourth mortgages were discharged. This payment to Goldfinger was made in the absence of any payment to Montor.

[25] On December 1, 2008, Goldfinger obtained an order appointing Zeifman & Partners Inc. as receiver of a number of Kimel's companies to which Goldfinger had made loans, including SG Waterloo, but not including Annopol. Following this, some other Kimel companies defaulted on loans.

[26] Perelmuter assigned his company, Montor, into bankruptcy on February 6, 2009. Farber was subsequently appointed Montor's Trustee in bankruptcy.

[27] Annopol and SG Brantford were each adjudged bankrupt on May 27, 2010, the initial bankruptcy event having occurred on May 26, 2009, in the case of Annopol, and on April 30, 2009 in the case of SG Brantford. Farber was appointed Trustee in bankruptcy of both companies, as well as of SG Group and SG Waterloo. SG Waterloo was adjudged bankrupt on June 28, 2010, the date of its initial bankruptcy event being April 3, 2009.

E. The Litigation

[28] As mentioned, Farber, in its capacity as Trustee in bankruptcy of Annopol, challenged the $2.5 million Payments from Annopol to Goldfinger. It argued that the Payments were: (1) transfers at undervalue contrary to s. 96 of the *BIA*; (2) unjust preferences under s. 4 of the *APA*; (3) fraudulent conveyances under s. 2 of the *FCA*; (4) oppressive under s. 248 of the *OBCA*; and (5) an unjust enrichment.

[29] The trial judge heard the proceedings in a hybrid trial conducted over the course of eight days. He heard *viva voce* evidence and also reviewed extensive documentary records, including several transcripts of out-of-court cross-examinations.

[30] The trial judge dismissed all of Farber's challenges to the Payments. Farber now appeals from that judgment, arguing that the trial judge erred in upholding the Payments on each of the grounds set out above.

[31] Also relying on the same statutory provisions, before the trial judge Farber challenged the Brantford/Bridge 2008 Transactions (the mortgages granted by SG Brantford and SG Bridge to Goldfinger and the Annopol Subordinations) and the $471,000 paid to Goldfinger. The trial judge dismissed Farber's claims with the exception of the $471,000 payment to Goldfinger, which he found to be contrary to s. 2 of the *FCA* and s. 248 of the *OBCA*. On appeal, Farber submits that the trial judge erred in failing to set aside the Brantford/Bridge 2008 Transactions under the *OBCA.*

[32] Goldfinger cross-appeals from the trial judge's decision ordering him to repay Farber the $471,000.

APPEAL RELATING TO THE PAYMENTS

A. Are the Payments Transfers at Undervalue under the *BIA*?

(i) Introduction

[33] Dealing first with the *BIA* claim, Farber challenged the Payments as transfers at undervalue contrary to s. 96 of the *BIA*. In order to succeed on this ground, Farber was required to establish that:

(a) the Payments were transfers at undervalue;

(b) the transfer occurred:

(i) within one year before the initial bankruptcy event (May 26, 2009), if Goldfinger was at arm's length with the debtor, Annopol; or

(ii) within five years before the initial bankruptcy event (May 26, 2009), if Goldfinger was not at arm's length with the debtor, Annopol; and

(c) the debtor, Annopol, was insolvent at the time of the Payments or was rendered insolvent by the Payments; and

(d) the debtor, Annopol, intended to defraud, defeat or delay a creditor.

[34] As I will discuss, undervalue means either that no consideration has been received by the debtor or that the consideration received is conspicuously less than the fair market value of the consideration given by the debtor: *BIA* s. 2. Section 96 is reproduced in Schedule "A" attached to these reasons.

(ii) Trial Judge's Decision on s. 96 of the *BIA*

[35] Before the trial judge, Farber argued that it had established all of the s. 96 requirements and therefore was entitled to an order that the Payments were transfers at undervalue.

[36] The trial judge rejected this argument. He found that the transfers were not at undervalue because consideration was given to Annopol by Goldfinger.

[37] The trial judge explained that forbearance from suit, either actual or promised, can constitute good consideration. He found that Goldfinger had lent

$6.5 million to Kimel's companies and could bring proceedings for that amount. Moreover, formal demand had been made on Kimel and in November 2007, Goldfinger had his counsel prepare an affidavit for him to swear in an action he was contemplating against Kimel, Annopol and the Summit Glen Companies, for the appointment of a receiver over a number of their properties. Instead, Goldfinger settled and did not proceed with his threatened litigation.

[38] The trial judge held that the terms of the settlement reflected a compromise of Goldfinger's claims to recover his investment of $6.5 million. Goldfinger deposed that: (1) but for the prior payment of $2.5 million, he would not have entered into the settlement and would have proceeded with the litigation against Kimel and his various companies; and (2) over the course of his dealings, $2.956 million of his money had been deposited into Annopol. Goldfinger's forbearance from suit was not consideration that was conspicuously less than the fair market value of the Payments and there were no transfers at undervalue. This was the ratio of the trial judge's decision on s. 96 of the *BIA*.

[39] Nonetheless, he proceeded to consider the other elements Farber was required to establish under s. 96 of the *BIA*.

[40] The trial judge concluded that at the time of the Payments (December 2007 and January 2008), Annopol was insolvent using a balance sheet test.

[41] The trial judge also addressed the nature of the relationship between Goldfinger and Annopol and considered whether they were at arm's length. Although the Memorandum deemed Goldfinger to be a shareholder, the trial judge found that Goldfinger was not a registered shareholder of Annopol. He found that this deal structure was simply a technical device that was probably tax-driven. Goldfinger never exercised any control over the affairs of Annopol, or any of Kimel's other companies. As a result, Goldfinger and Annopol were not related persons within the meaning of ss. 4(2) and (3) of the *BIA*.

[42] In addition, he addressed s. 4(4) of the *BIA*, which provides that "[i]t is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length." He concluded that they were acting at arm's length.

[43] Although the trial judge accepted that Goldfinger and Kimel had been close friends, he acknowledged that one had to examine the nature of their relationship at the time the Payments were made. Goldfinger had not been involved in the operation of Kimel's companies and had quite limited information about their affairs. In 2007, Goldfinger discovered that he had been misled. He sought explanations, but Kimel stalled. Although Goldfinger and Kimel arrived at the amount of $2.5 million together, the overall structure and details of the settlement were negotiated with the assistance of counsel. The trial judge determined that the facts did not disclose bonds of "dependence, control or influence", which are

generally necessary in order to find that two parties are not acting at arm's length.

[44] Given that the parties were found to be at arm's length, to succeed under s. 96 of the *BIA*, Farber had to show that the Payments were made within one year prior to the initial bankruptcy event. Annopol's initial bankruptcy event was May 26, 2009 and therefore, the one-year statutory review period commenced on May 26, 2008. The Payments, having occurred between December 5, 2007 to January 10, 2008, were outside the one-year statutory review period reflected in s. 96(1)(a) of the *BIA*. Accordingly, the trial judge concluded that the Payments were not reviewable under s. 96.

[45] Lastly, the trial judge considered whether, by making the Payments, Annopol intended to defraud, defeat or delay a creditor. He accepted Farber's submission that Annopol's intention should be determined by reference to the intention of Kimel, who directed Annopol's affairs.

[46] The trial judge recognized that an inference of intent may arise from suspicious facts or circumstances, sometimes referred to as "badges of fraud". He found that when making the Payments, Kimel and Goldfinger did not intend to defraud, defeat or delay any of Annopol's creditors. In making that finding, he relied on the following facts:

- the terms of the Memorandum, which originated around the time the Payments were made, indicated that the parties thought the Summit Glen Companies would continue as going concerns and that the properties would generate sufficient value to repay the remaining amount owing to Goldfinger by December 11, 2009;
- the parties to the Memorandum also believed that the properties owned by the Summit Glen Companies had significant future value;
- the Memorandum was not put together in a rush, but was negotiated over six months and both parties were represented by counsel;
- the parties were at arm's length;
- the two lawyers' evidence on the parties' thought processes at the time suggested a genuine belief in the sufficient value of the subject properties;
- consideration was given;
- the Payments and the Memorandum were not put in place in the face of claims by Annopol's judgment creditors; and
- this was all done prior to the collapse of the credit markets, which occurred months after the execution of the Memorandum.

(iii) Farber's s. 96 Submissions on Appeal

[47] On appeal, Farber advances three arguments with respect to the trial judge's treatment of the s. 96 *BIA* claim.

[48] First, in concluding that the Payments were not transfers at undervalue, Farber submits that the trial judge erred in deciding that Goldfinger provided valuable consideration. Compromising his potential legal claim did not amount to sufficient consideration, as s. 96 requires that the consideration be given at the same time as the transfer and the compromise only occurred at the time of the Memorandum. Furthermore, Annopol did not receive anything in exchange for the Payments; the Memorandum lists the $2.5 million as payment for a debt owing by Kimel. Farber also submits that the trial judge erred in failing to examine the sufficiency of the consideration provided – there was no documentary evidence of any forbearance or settlement with Annopol at the time of the Payments.

[49] Second, Farber submits that the trial judge erred in finding that the parties were acting at arm's length. Although he identified the correct test, he failed to apply it. Specifically, he failed to consider the parties' relationship at the time of the Payments and that the Payments were the opposite of what one would expect from arm's-length parties. The trial judge also failed to consider that Goldfinger refused to produce his e-mail exchanges with Kimel from the time of the Payments and failed to consider Goldfinger's evidence that he used his relationship with Kimel to obtain the Payments.

[50] Third, Farber argues that the trial judge erred in his analysis of Annopol's intention to defraud, defeat or delay a creditor. Again, Farber states that the trial

judge focused on the evidence relating to the Memorandum rather than the Payments themselves and also failed to identify and consider the badges of fraud that were present. In addition, Annopol had a subjective intent to defraud its creditors, HSBC and a third-party investor, Srubiski, and its actions were deliberate. It had borrowed money from those creditors on the basis that the funds would be invested in real estate; instead, Annopol gave the money to Goldfinger. The effect of the Payments was to defraud and defeat its creditors.

(iv) Analysis

(1) *Transfers at Undervalue*

[51] Section 2 of the *BIA* defines a "transfer at undervalue" as follows:

> [A] disposition of property or provision of services for which no consideration is received by the debtor or for which the consideration received by the debtor is conspicuously less than the fair market value of the consideration given by the debtor.

[52] In the absence of evidence to the contrary, Farber's opinion on both the fair market value of the property or services and the value of the actual consideration given or received by the debtor are to be accepted by the court: see s. 96(2) of the *BIA*.

[53] Weighing the adequacy of consideration is not an exercise in precision but one of judgment. Nominal or grossly inadequate consideration is insufficient and

may be an indication or badge of fraud: see *Feher v. Healey*, [2006] O.J. No. 3450 (Sup. Ct.), at para. 45, aff'd 2008 ONCA 191.

[54] Forbearance from suit and a settlement agreement may constitute adequate consideration: see *Ronald Elwyn Lister Ltd. v. Dunlop Canada Ltd.*, [1982] 1 S.C.R. 726, at p. 743; *Stott v. Merit Investment Corp.* (1988), 63 O.R. (2d) 545 (C.A.), at pp. 558-60, leave to appeal dismissed, [1988] S.C.C.A. No. 185.

[55] Here, formal demand had been made on Kimel and in November 2007 Goldfinger had his counsel prepare an affidavit for him to swear in an action he was contemplating against Kimel, several of the Summit Glen Companies and Annopol. Rather than proceeding with the litigation, Goldfinger negotiated a resolution to the parties' dispute. He abandoned his pursuit of the legal action against Kimel and his companies, including Annopol. But for the $2.5 million payment, he would have commenced and continued with his litigation.

[56] The evidence supports the finding that Goldfinger was genuinely threatening legal action. In particular, the record contains Goldfinger's draft affidavit and, as well, his lawyer prepared a memorandum referring to the proposed settlement and that as a result, "Jack [Kimel] staves off receivership". In addition, Annopol was to be a beneficiary of a release under the settlement.

The trial judge did not err in concluding that Goldfinger's forbearance constituted consideration.

[57] One must then consider whether the consideration given by Goldfinger was adequate, or, to use the language of s. 2 of the *BIA*, was "conspicuously less than the fair market value" of the consideration given by Annopol.

[58] Of the $6.5 million invested by Goldfinger, $2.956 million had been paid to Annopol. Based on the record before him, it was open to the trial judge to conclude that a payment of $2.5 million in return for a compromise of Goldfinger's remaining rights was adequate consideration. At a minimum, Goldfinger paid Annopol and Kimel $2.9 million. Given the potentially ruinous consequences of a lawsuit, the trial judge did not err in concluding that the Payments did not constitute a transfer at undervalue.

[59] Farber also asserts that s. 96 requires that consideration be given at the same time as the transfer and, in this case, the compromise only occurred at the time of the Memorandum.

[60] Section 96 does not address timing and Farber provided no authority for this proposition. However, assuming without deciding that Farber's proposition is correct, the trial judge found at para. 274 of his reasons that the terms of the settlement originated around the time the $2.5 million was paid. This finding of

fact is also relevant to the trial judge's determination that the Payments were not motivated by a desire to defraud, defeat or delay a creditor.

[61] This finding was also available on the record. Goldfinger testified that he and Kimel came up with the terms of the settlement themselves and only then approached the lawyers to structure and paper the agreement. In one of his affidavits, he stated that the parties had reached an agreement in November 2007, before the first payment was made. The evidence of Goldfinger's two lawyers lends credence to Goldfinger's version of events.

[62] In addition, one of the lawyers, Carl Schwebel, prepared a memo dated November 28, 2007 that recorded discussions with Goldfinger, Kimel and members of Schwebel's firm at a meeting that same day. Although not identical to the terms of the Memorandum, the memo recorded the terms of the settlement negotiated by Goldfinger and Kimel, including the payment of $2.5 million.

[63] In light of this evidence, I would not give effect to Farber's submission that the trial judge erred in his transfer at undervalue analysis.

(2) *Acting at Arm's Length*

[64] Given my conclusion on the transfer at undervalue issue, it is not strictly necessary to address Farber's other arguments about s. 96 of the *BIA.* I will do so because my conclusions on the balance of the s. 96 factors inform my

conclusions on Farber's other grounds of appeal attacking the validity of the Payments.

[65] On the issue of whether the parties were at arm's length, Farber does not challenge the trial judge's description of the applicable test or his finding that Goldfinger and Annopol were unrelated. Rather, it challenges his application of the test and his conclusion that Goldfinger and Annopol were acting at arm's length.

[66] Section 4(4) of the *BIA* states: "It is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length." As a result, absent a palpable and overriding error, the trial judge's finding on this issue is entitled to deference.

[67] The trial judge considered the *dicta* in *Abou-Rached (Re)*, 2002 BCSC 1022, 35 C.B.R. (4th) 165, at para. 46:

> [A] transaction at arm's length could be considered to be a transaction between persons between whom there are no bonds of dependence, control or influence, in the sense that neither of the two co-contracting parties has available any moral or psychological leverage sufficient to diminish or possibly influence the free decision-making of the other. Inversely, the transaction is not at arm's length where one of the co-contracting parties is in a situation where he may exercise a control, influence or moral pressure on the free will of the other. Where one of the co-contracting parties is, by reasons of his influence or superiority, in a position to pervert the ordinary rule of supply and demand and force the other to transact for a consideration which is substantially

> different than adequate, normal or fair market value, the transaction in question is not at arm's length.

[68] He also considered *Piikani Energy Corporation (Trustee of) v. 607385 Alberta Ltd.*, 2013 ABCA 293, 556 A.R. 200, which identified factors that provide guidance on non-arm's length analysis in the context of *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) jurisprudence. These factors, enumerated at para. 29 of *Piikani*, are: was there a common mind which directed the bargaining for both parties to a transaction; were the parties to the transaction acting in concert without separate interests; and was there *de facto* control?

[69] There was no common mind directing Goldfinger and Annopol or indeed, Kimel. They were adverse in interest and on the verge of litigation. The evidence also fails to suggest that they were acting in concert. As discussed, the trial judge did not fail to consider the parties' relationship at the time of the Payments. Nor did Goldfinger or Annopol exercise *de facto* control over the other.

[70] Goldfinger was never involved in the operation of the companies, had little information about their operation or finances, discovered Kimel had misled him and then threatened to sue. As mentioned, although Goldfinger and Kimel decided on the amount Goldfinger would be paid, the overall structure and details of the settlement were negotiated with the assistance of counsel.

[71] Farber argues that the Payments were the opposite of what one would expect from arm's length parties and that the trial judge erred in declining to draw

certain inferences from the evidence. However, the trial judge is the fact finder, not this court, and he was not required to recite every piece of evidence in his 372 paragraphs of reasons. Moreover, there was a dearth of evidence suggesting that the parties were not at arm's length and the trial judge did not err in finding to the contrary. I would reject this argument.

(3) *Intention to Defraud, Defeat or Delay a Creditor*

[72] The burden was on Farber to establish the requisite intent under s. 96 of the *BIA*. An inference of intent may arise from the existence of one or more badges of fraud. However, the presence of such indicia does not mandate a finding of intent. Whether the intent exists is a question of fact to be determined from all of the circumstances as they existed at the time of the conveyance: see *Re Fancy* (1984), 46 O.R. (2d) 153 (H. Ct. J.), at p. 159.

[73] Case law has identified the following, non-exhaustive list of "badges of fraud" (see *DBDC Spadina v. Walton*, 2014 ONSC 3052, at para. 67; *Indcondo Building Corp. v. Sloan*, 2014 ONSC 4018, 121 O.R. (3d) 160, aff'd 2015 ONCA 752, 31 C.B.R. (6th) 110, at para. 52):

- the transferor has few remaining assets after the transfer;
- the transfer was made to a non-arm's length person;
- the transferor was facing actual or potential liabilities, was insolvent, or about to enter a risky undertaking;

- the consideration for the transaction was grossly inadequate;
- the transferor remained in possession of the property for his own use after the transfer;
- the deed of transfer contained a self-serving and unusual provision;
- the transfer was secret;
- the transfer was effected with unusual haste; or
- the transaction was made in the face of an outstanding judgment against the debtor.

[74] As stated, Farber complains that the trial judge failed to consider the presence of badges of fraud, focused on the evidence relating to the Memorandum rather than the Payments themselves, and ignored Annopol's intent to defraud its creditors.

[75] The trial judge found that the terms of the settlement originated around the time that the $2.5 million was paid. Furthermore, the evidence suggested that the parties expected the Summit Glen Companies and Annopol to continue as going concerns. As is evident from paras. 260 and following of his reasons, the trial judge did consider the issue of badges of fraud, but ultimately concluded that there was no intent. Indeed, his findings undermine Farber's assertions that badges of fraud were present. He assessed the evidence and made findings of fact that supported his reasons for finding an absence of intent. Those findings were available on the record. I see no basis to interfere with them.

[76] As for Farber's submissions relating to Annopol's alleged subjective intent to defraud its creditors, HSBC and Srubiski, the evidence did not support such a finding of intent. Neither the Payments nor the settlement were effected in the face of claims by Annopol's judgment creditors. No evidence was tendered from any creditor and there was no evidence that established that Annopol paid creditor funds to Goldfinger.

[77] In conclusion, I would reject Farber's submissions on s. 96 of the *BIA*.

B. Are the Payments Unjust Preferences under the *APA*?

(i) Introduction

[78] At the trial, Farber also argued that the Payments were void as unjust preferences pursuant to s. 4 of the *APA*. To be successful, Farber needed to establish that:

(a) Annopol was insolvent at the time of the Payments;

(b) Annopol intended to defeat, hinder, delay or prejudice a creditor; and

(c) Goldfinger was not a creditor of Annopol within the meaning of s. 5(1) of the *APA*.

[79] Sections 4 and 5 of the *APA* are reproduced in Schedule "A" attached to these reasons.

(ii) Trial Judge's Decision on the *APA*

[80] The trial judge did not accept Farber's *APA* argument. He found that the first and third requirements under the *APA* were satisfied – Annopol was insolvent, and Goldfinger was not a creditor of Annopol within the meaning of s. 5(1) of the *APA*. However, the trial judge relied on his earlier analysis under s. 96 of the *BIA* to conclude that the second requirement was not met: Annopol did not have the requisite intent to defeat, hinder, delay or prejudice a creditor.

(iii) Parties' *APA* Submissions on Appeal

[81] On appeal, Farber reiterates its position on intent. In response, Goldfinger takes issue with the trial judge's finding that he was not a creditor within the meaning of s. 5(1).

(iv) Analysis

[82] I have already addressed the issue of intent under s. 96 of the *BIA* and that analysis is equally applicable to the requirement of intent under the *APA*. For these reasons, I would dismiss Farber's *APA* ground of appeal. Given that conclusion, there is no need to address Goldfinger's submission on his status.

C. Are the Payments void under the *FCA*?

(i) Introduction

[83] Before the trial judge, Farber submitted that the Payments were also contrary to s. 2 of the *FCA*. To succeed, Farber had to demonstrate that:

> (a) Annopol made the Payments with an intent to defeat, hinder, delay or defraud creditors or others; and
>
> (b) Goldfinger did not provide good consideration in exchange for the Payments; or
>
> (c) if Goldfinger did provide good consideration, he had notice or knowledge of Annopol's intent to defeat, hinder, delay or defraud creditors or others.

[84] Sections 2 and 3 of the *FCA* are reproduced in Schedule "A".

(ii) Trial Judge's Decision on the *FCA*

[85] The trial judge confined his *FCA* analysis to an examination of intent. He concluded that the evidence concerning intent under the other statutes applied equally to Farber's claim under the *FCA*. Consequently, he dismissed the *FCA* claim.

(iii) Farber's Submissions on Appeal

[86] On appeal, Farber submits that the trial judge erred in failing to consider the factual matrix surrounding the Payments; the evidence relating to Annopol's actual or imputed intent; and that Goldfinger was wilfully blind.

(iv) Analysis

[87] I have already addressed the issue of intent, which is equally fatal to this ground of appeal. There is therefore no need to address the issue of Goldfinger's knowledge. The trial judge was correct in dismissing Farber's claim under the *FCA*.

D. Oppression Claim

(i) Introduction

[88] Before the trial judge, Farber submitted that the Payments were oppressive within the meaning of s. 248 of the *OBCA*. To succeed, Farber had to establish that:

> (a) it was a "complainant" within the meaning of s. 245 of the *OBCA*; and
>
> (b) the Payments were oppressive, unfairly prejudicial or unfairly disregarded the interests of Annopol's creditors.

Section 248 of the *OBCA* is reproduced in Schedule "A".

(ii) Trial Judge's Decision on Oppression

[89] The trial judge proceeded with his analysis of the oppression claim on the basis that Farber, as Trustee in bankruptcy of Annopol, had status as a complainant under s. 245 of the *OBCA*. In that regard, he noted that in *Olympia & York Developments Ltd. (Trustee of) v. Olympia & York Realty Corp.* (2003), 68

O.R. (3d) 544, at para. 46, this court held that where it was likely the creditors of a bankrupt would have been recognized as complainants for the purpose of challenging a transaction under s. 248 of the *OBCA*, it was proper to recognize the Trustee of the bankrupt as a complainant "in effect on behalf of the creditors" of the bankrupt.

[90] The trial judge accepted that creditors of a corporation have a reasonable expectation that the corporation will not engage in conduct that runs afoul of provincial preference legislation or the preference/transfer for undervalue provisions of the *BIA*. However, the trial judge had already found that the Payments by Annopol to Goldfinger did not run afoul of the *BIA*, the *APA* or the *FCA*, and he therefore relied on the same findings to conclude that the Payments did not violate the reasonable expectations of Annopol's creditors.

[91] Farber also argued that Goldfinger was a shareholder of Annopol at the time of the Payments and the $2.5 million represented the repurchase of shares or the payment of a dividend. However, the trial judge rejected this contention. Rather, in substance, Goldfinger received the re-payment of $2.5 million of the funds he had loaned to Kimel and his companies, together with some additional security. He wrote, at para. 300 of his reasons: "The business substance of the December, 2007 and January, 2008 payments was that Goldfinger received back some of the principal he had invested; there was no profit or equity yet available for distribution." For these reasons, he rejected Farber's oppression claim.

(iii) Parties' Oppression Submissions on Appeal

[92] Goldfinger submits that while the court has discretion to recognize a Trustee in bankruptcy as a complainant under the *OBCA*, the exercise of that discretion was unjustified in this case. Furthermore, Farber put forward no evidence on the reasonable expectations of the creditors on whose behalf it purported to act. Goldfinger submits that the trial judge erred in recognizing Farber as a complainant.

[93] For its part, Farber asserts that Goldfinger is raising the issue of Farber's status as a complainant for the first time on this appeal. The decision was within the trial judge's discretion and there is no basis on which this court should interfere.

[94] On the issue of oppression, Farber reiterates that the Payments were unlawful preferences. In addition, Farber submits that Annopol's creditors expected that its funds would be used for real estate development. The Payments to Goldfinger resulted in unfair prejudice, as Annopol's creditors will likely recover nothing from its bankrupt estate. Annopol and Kimel acted with unfair disregard for Annopol's creditors' interests. As a result, Farber submits that Goldfinger should be ordered to repay the $2.5 million to Annopol's bankrupt estate.

(iv) Analysis

[95] Dealing first with the issue of Farber's status as a complainant, s. 245 of the *OBCA* defines "complainant" for the purposes of the oppression remedy as follows:

> (a) a registered holder or beneficial owner, and a former registered holder or beneficial owner, of a security of a corporation or any of its affiliates,
>
> (b) a director or an officer or a former director or officer of a corporation or of any of its affiliates,
>
> (c) any other person who, in the discretion of the court, is a proper person to make an application under this Part.

[96] Farber relied on subsection (c) in support of its position that it should be given standing as a complainant. In *Olympia & York Developments Ltd.,* at para. 45, this court held that Trustees in bankruptcy are neither automatically barred nor automatically entitled to standing, but it is a matter of discretion in each case whether to grant standing.

[97] I do not read the trial judge's reasons as having conclusively held that Farber was a proper person to be a complainant under s. 245. Rather, given his other findings, the trial judge simply proceeded on the assumption that Farber, in its capacity as Trustee in bankruptcy of Annopol, was a complainant. In light of his conclusion on the merits of the oppression claim, and my concurrence with it, I see no need to interfere with his approach. I would also observe that Goldfinger

objected to Farber's status to assert a claim for oppression for the first time on this appeal.

[98] Turning to the merits of the oppression ground of appeal, this court has recognized that the oppression remedy contained in s. 248 of the *OBCA* is a "flexible, equitable remedy that affords the court broad powers to rectify corporate malfeasance": see *Unique Broadband Systems, Inc. (Re)*, 2014 ONCA 538, 121 O.R. (3d) 81, at para. 107. The granting of an oppression remedy is a discretionary decision.

[99] In *BCE Inc. v. 1976 Debentureholders*, 2008 SCC 69, [2008] 3 S.C.R. 560, the Supreme Court addressed the oppression provision found in the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, which is similar to the provision found in the *OBCA*. At para. 68, the Court outlined the following two-step test: (1) Does the evidence support the reasonable expectations asserted by the claimant? and (2) Does the evidence establish that the reasonable expectation was violated by conduct falling within the terms "oppression", "unfair prejudice" or "unfair disregard" of a relevant interest?

[100] The Court addressed the concept of reasonable expectations under the first part of the test, at paras. 62 and 63:

> [T]he concept of reasonable expectations is objective and contextual. The actual expectation of a particular stakeholder is not conclusive. In the context of whether it would be "just and equitable" to grant a remedy, the

> question is whether the expectation is reasonable having regard to the facts of the specific case, the relationships at issue, and the entire context, including the fact that there may be conflicting claims and expectations.
>
> Particular circumstances give rise to particular expectations. Stakeholders enter into relationships, with and within corporations, on the basis of understandings and expectations, upon which they are entitled to rely, provided they are reasonable in the context. These expectations are what the remedy of oppression seeks to uphold. [Citations omitted.]

[101] The court addressed the second stage of the test, at para. 67:

> Even if reasonable, not every unmet expectation gives rise to a claim under [s. 248]. The section requires that the conduct complained of amount to "oppression", "unfair prejudice" or "unfair disregard" of relevant interests. "Oppression" carries the sense of conduct that is coercive and abusive, and suggests bad faith. "Unfair prejudice" may admit of a less culpable state of mind, that nevertheless has unfair consequences. Finally, "unfair disregard" of interests extends the remedy to ignoring an interest as being of no importance, contrary to the stakeholders' reasonable expectations. The phrases describe, in adjectival terms, ways in which corporate actors may fail to meet the reasonable expectations of stakeholders. [Citations omitted.]

[102] The trial judge's analysis under the *BIA*, the *APA* and the *FCA* effectively disposed of that part of Farber's submissions relating to unjust preferences. As for Farber's argument that there was unfair disregard for the interests of Annopol's creditors, this submission must be placed in context. While Kimel stated that he was not thinking of his creditors when he made the Payments, Kimel and his companies were facing the prospect of potentially ruinous litigation.

He believed that the Payments would permit the companies to continue as going concerns and that they would generate profit. The evidence did not suggest that this was a misguided proposition at that time. The cataclysmic, and unforeseen, economic meltdown that enveloped the global economy months after the Payments were made cannot be ignored. In this context, the trial judge did not err in exercising his discretion and dismissing Farber's claim of unfair disregard for the interests of Annopol's creditors.

[103] As for the expectations of HSBC and Srubiski as creditors, Farber claims that Annopol paid Goldfinger with funds it had received from Srubiski. The trial judge found that it was not possible to trace the vast majority of funds to any particular source or creditor. As the trial judge noted, Kimel's evidence was that money may have come from Srubiski or Mahvash. There was also no conclusive evidence that the funds paid by Annopol to Goldfinger came from Srubiski. Moreover, the line of credit from HSBC was provided to SG Group and not to Annopol. Consequently, HSBC was not a creditor of Annopol. HSBC, a sophisticated party, would have known that it was not a creditor of Annopol. There could be no reasonable expectation to the contrary.

[104] The trial judge's decision reflected an exercise in discretion and is entitled to deference. I would not accede to Farber's submissions on oppression.

E. Did the Payments Unjustly Enrich Goldfinger?

(i) Introduction

[105] Before the trial judge, Farber submitted that the Payments unjustly enriched Goldfinger. To succeed, Farber had to establish that:

(a) the Payments enriched Goldfinger;

(b) there was a corresponding deprivation suffered by Annopol; and

(c) there was no juristic reason for that enrichment.

(ii) Trial Judge's Decision on Unjust Enrichment

[106] The trial judge gave brief reasons for his dismissal of Farber's unjust enrichment claim. In essence, he relied on his reasons for dismissal of the oppression claim, stating at para. 304 of his reasons: "Farber also advanced a claim sounding in unjust enrichment on the basis that the $2.5 million payments were a re-purchase of shares or equity distribution. For similar reasons [*i.e.* similar to those for dismissing the oppression claim], I dismiss that claim."

(iii) Parties' Submissions on Appeal

[107] Farber submits that the trial judge failed to consider the test for unjust enrichment, which it says was met based on the evidence. Farber says that the first two parts of the test were easily satisfied on the basis of the Payments from Annopol to Goldfinger. With respect to lack of a juristic reason, the Payments

were contrary to the reasonable expectations of Annopol's creditors and it was contrary to public policy for Goldfinger to have received the Payments from an insolvent company.

[108] Goldfinger responds that he merely received his money back and Annopol got what it bargained for. The Payments were a repayment of an obligation and in line with the parties' expectation of a settlement of their dispute. Settlement of disputes is supported by public policy and may constitute the rationale for a payment.

(iv) Analysis

[109] As Iacobucci J. noted in *Garland v. Consumers' Gas Co.*, 2004 SCC 25, [2004] 1 S.C.R. 629, at para. 30, the test for unjust enrichment requires that a claimant establish the following three elements:

a) an enrichment of the defendant;

b) a corresponding deprivation of the plaintiff; and

c) an absence of juristic reason for the enrichment.

[110] As noted in *Garland*, at para. 31, the first two elements are determined by applying a "straightforward economic approach". Iacobucci J. explained, at para. 36: "Where money is transferred from plaintiff to defendant, there is an enrichment."

[111] The analysis in respect of the third element proceeds in two steps.

[112] At the first stage, the claimant has the burden of demonstrating that "no juristic reason from an established category exists to deny recovery." The established categories include a contract, a disposition of law, a donative intent, and other valid common law, equitable or statutory obligations: see *Garland*, at para. 44.

[113] If the claimant can show that there is no established juristic reason, then, at the second stage, the defendant bears the burden of demonstrating that there is another reason to deny recovery. When determining if there is a reason to deny recovery at this stage, courts are required to consider the reasonable expectations of the parties and public policy considerations: see *Garland*, at paras. 45-46.

[114] As this court noted in *Campbell v. Campbell* (1999), 43 O.R. (3d) 783, at pp. 794-95, and *Simonin Estate v. Simonin*, 2010 ONCA 900, 329 D.L.R. (4th) 513, at para. 24:

> [W]hat is at the heart of the third requirement is the reasonable expectation of the parties, and whether it would be just and fair to the parties considering all of the relevant circumstances, to permit the recipient of the benefit to retain it without compensation to those who provided it.

[115] Applying these principles to the issues on appeal, the first two requirements for unjust enrichment were clearly met. Goldfinger was enriched

and there was a corresponding deprivation to Annopol. The real issue turns on the third element: was there a juristic reason for the enrichment?

[116] Farber was unsuccessful in attacking the Memorandum and, in any event, it did not ask that the Memorandum be set aside. A contract is a recognized category on which to reject a claim for unjust enrichment. The settlement provided an established rationale for the Payments and hence amounted to a juristic reason. In addition, Goldfinger's advance of $2.9 million to Annopol amounted to a juristic reason.

[117] Finally, a juristic reason may be made out based on an examination of the reasonable expectations of the parties. On the facts of this case, Goldfinger advanced funds to whichever company Kimel requested. He advanced a total of about $2.9 million to Annopol itself. Kimel treated all the companies as, effectively, a common pool. Therefore, it was in line with past practice and the reasonable expectations of the parties that Goldfinger received payment in respect of funds from Annopol.

[118] This ground of appeal therefore fails.

APPEAL RELATING TO THE BRANTFORD/BRIDGE 2008 TRANSACTIONS

A. Are the Brantford/Bridge 2008 Transactions Oppressive under the *OBCA*?

(i) Introduction

[119] As mentioned, Farber had originally advanced an oppression claim with respect to the Brantford/Bridge 2008 Transactions. Ultimately, the dispute devolved into a claim to approximately $280,000 in proceeds from the sale of the Bridge Street property that is held in trust pending resolution of the action. The payment of this sum turns on whether the Brantford/Bridge 2008 Transactions were oppressive within the meaning of s. 248 of the *OBCA* and therefore ought to have been set aside by the trial judge.

(ii) Trial Judge's Decision on the Brantford/Bridge 2008 Transactions and Oppression

[120] The trial judge relied on his findings under the *BIA*, the *APA* and the *FCA* claims to conclude that Goldfinger's charges over the SG Brantford and SG Bridge properties, as well as the Annopol Subordinations, did not violate the reasonable expectations of creditors. There was no intent to defeat, hinder, delay or defraud creditors. He concluded that no s. 248 *OBCA* remedy was justified.

(iii) Farber's Submissions on Appeal

[121] Farber submits that the trial judge did not consider whether the transactions should be set aside pursuant to s. 248 of the *OBCA*. Its primary

submission is that the trial judge dismissed its claim on the basis of lack of intent; however, this is an irrelevant consideration in an oppression analysis. Goldfinger was at best an unsecured creditor, and Annopol held prior security over the Henry Street and Bridge Street properties. As a result of the Memorandum, Goldfinger became secured. But for the transactions, Annopol's creditors would be entitled to the $280,000 in sale proceeds.

[122] Farber argues that the trial judge erred in failing to make a finding of oppression and in refusing to set aside the Brantford/Bridge 2008 Transactions.

(iv) Analysis

[123] The trial judge clearly turned his mind to the oppression claim as is evident from paras. 317, 327, 328, 348, 349 and 351 of his reasons. It is a fair inference from his reasons and his conclusion on the Brantford/Bridge 2008 Transactions that he was of the view that his prior findings supported his conclusion that they did not violate the reasonable expectations of creditors.

[124] The trial judge relied on his same reasons, found at paras. 274-280, for concluding that Annopol did not intend to defeat, hinder, delay or defraud its creditors by making the Payments to Goldfinger. In addition, the trial judge's reasons were that the Payments were part of a global settlement meant to avoid potentially ruinous litigation; the settlement in question was concluded at arm's

length after fairly lengthy negotiations; and the parties' compromise was reasonable at the time they reached it.

[125] The trial judge's decision that the Payments and the Brantford/Bridge 2008 Transactions were defensible for the same reasons was justified on the record. Both sets of transactions resulted from the same settlement. Therefore, the validity of the Brantford/Bridge 2008 Transactions falls to be decided on the same basis as that applicable to the Payments. For the reasons given, I would reject Farber's submissions with respect to the Brantford/Bridge 2008 Transactions.

CROSS-APPEAL

A. Is the $471,000 Payment to Goldfinger a Fraudulent Conveyance?

(i) Introduction

[126] Farber, in its capacity as Trustee in bankruptcy of SG Brantford, asked the trial judge to order Goldfinger to return the sum of $471,000 to SG Brantford. Goldfinger objected.

(ii) Trial Judge's Decision

[127] To recap, about five months after the Memorandum, the mortgage from the first mortgagee, First National, on 176 Henry St., a property owned by SG Brantford, came due. As part of the refinancing, the First National mortgage was

to be increased. To complete the refinancing with First National, SG Brantford had to arrange for the postponement of the second mortgage in favour of Montor.

[128] The trial judge was not prepared to find that Kimel forged Montor's signature on the postponement. He instead found that the Montor postponement was signed by Kimel purporting to act as the secretary-treasurer of Montor.

[129] However, he did find that the postponement arose as a result of Kimel's and SG Brantford's deliberate misrepresentation of the true state of affairs to Montor. Moreover, Perelmuter, the sole shareholder of Montor, was unaware that part of the refinancing proceeds would be paid to a junior secured creditor, namely Goldfinger. The trial judge concluded that Kimel and SG Brantford made the misrepresentation in order to defeat, hinder, delay or defraud Montor.

[130] He held that the evidence on intent as of November 26, 2008 was materially different from the evidence at the time of the Memorandum. By November 2008, Goldfinger knew that Kimel and his companies, including SG Brantford, had defaulted on their obligations. He and Kimel also knew that there were insufficient funds to pay Goldfinger's charges over the SG Brantford and SG Bridge properties if Montor were to be paid from the refinancing.

[131] On the trial judge's findings, when Kimel and SG Brantford misrepresented the true state of affairs to Montor, they did so intending to defeat, hinder, delay or

defraud Montor. Goldfinger had notice or knowledge of that intent within the meaning of s. 3 of the *FCA*.

[132] The trial judge concluded that Goldfinger knew that the payment of $471,000 to him would prefer his interests over those of Montor. He based his conclusion on the *FCA*, but held that he would have reached a similar result under s. 248 of the *OBCA*. Therefore, the payment by SG Brantford to Goldfinger of $471,000 in preference to the payment of that amount to Montor violated s. 2 of the *FCA* and was not saved by s. 3 of the *FCA*.

[133] Accordingly, Goldfinger was ordered to repay the sum of $471,000 to Farber, as Trustee in bankruptcy of SG Brantford.

(iii) Goldfinger's Submissions on Appeal

[134] Goldfinger argues that he was not involved with, and did not know, the terms of the postponement. He asserts that the trial judge erred in finding that he had the intent to defeat Montor's interest. He had nothing to do with the postponement of the Montor mortgage. Goldfinger was unconditionally entitled to payment of the $471,000.

[135] He asks that if his cross-appeal is denied, he should, in the alternative, be given judgment for the restoration of his position, including judgment for $183,000 representing the net proceeds from the sale of the Henry Street

property on August 31, 2010 being held by the Trustee pending the outcome of the appeals.

(iv) Analysis

[136] I would reject Goldfinger's cross-appeal. As Goldfinger notes in his factum, at para. 53, where the issue on appeal involves the trial judge's interpretation of the evidence as a whole, his findings should not be overturned absent palpable and overriding error: *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235, at paras. 23-24.

[137] The trial judge's conclusion on this issue rested on factual findings. In particular, he found that Goldfinger had notice or knowledge of Kimel's and SG Brantford's intent to defeat, hinder, delay or defraud Montor and that he knew the $471,000 payment would prefer his interests over those of Montor. Goldfinger has not identified any palpable and overriding error that would serve to displace these findings.

[138] For these reasons, I would dismiss the cross-appeal.

[139] Further, I see no basis on which to grant the alternative relief Goldfinger requests. Based on the evidence, even with the repayment of the $471,000, there will be a significant shortfall in recovery on account of Montor's mortgage. Moreover, no such request was made of the trial judge.

Disposition

[140] For these reasons, I would dismiss both the appeal and the cross-appeal. As agreed by the parties, I would order Farber to pay Goldfinger $40,000 in costs of the appeal and Goldfinger to pay Farber $20,000 in costs of the cross-appeal, both sums inclusive of disbursements and applicable taxes.

Released:

“MAY 30 2016” “S.E. Pepall J.A.”

“EAC” “I agree E.A. Cronk J.A.”

“I agree P. Lauwers J.A.”

SCHEDULE "A"

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

96 (1) On application by the trustee, a court may declare that a transfer at undervalue is void as against, or, in Quebec, may not be set up against, the trustee — or order that a party to the transfer or any other person who is privy to the transfer, or all of those persons, pay to the estate the difference between the value of the consideration received by the debtor and the value of the consideration given by the debtor — if

(a) the party was dealing at arm's length with the debtor and

(i) the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and that ends on the date of the bankruptcy,

(ii) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, and

(iii) the debtor intended to defraud, defeat or delay a creditor; or

(b) the party was not dealing at arm's length with the debtor and

(i) the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and ends on the date of the bankruptcy, or

(ii) the transfer occurred during the period that begins on the day that is five years before the date of the initial bankruptcy event and ends on the day before the day on which the period referred to in subparagraph (i) begins and

(A) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, or

(B) the debtor intended to defraud, defeat or delay a creditor.

(2) In making the application referred to in this section, the trustee shall state what, in the trustee's opinion, was the fair market value of the property or services and what, in the trustee's opinion, was the value of the actual consideration given or received by the debtor, and the values on which the court makes any finding under this section are, in the absence of evidence to the contrary, the values stated by the trustee.

(3) In this section, a person who is privy means a person who is not dealing at arm's length with a party to a transfer and, by reason of the transfer, directly or

indirectly, receives a benefit or causes a benefit to be received by another person.

***Assignments and Preferences Act*, R.S.O. 1990, c. A.33**

4. (1) Subject to section 5, every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects, or of bills, bonds, notes or securities, or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made by a person when insolvent or unable to pay the person's debts in full or when the person knows that he, she or it is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice creditors, or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced.

(2) Subject to section 5, every such gift, conveyance, assignment or transfer, delivery over or payment made by a person being at the time in insolvent circumstances, or unable to pay his, her or its debts in full, or knowing himself, herself or itself to be on the eve of insolvency, to or for a creditor with the intent to give such creditor an unjust preference over other creditors or over any one or more of them is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

(3) Subject to section 5, if such a transaction with or for a creditor has the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them, it shall, in and with respect to any action or proceeding that, within sixty days thereafter, is brought, had or taken to impeach or set aside such transaction, be presumed, in the absence of evidence to the contrary, to have been made with the intent mentioned in subsection (2), and to be an unjust preference within the meaning of this Act whether it be made voluntarily or under pressure.

(4) Subject to section 5, if such a transaction with or for a creditor has the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them, it shall, if the debtor within sixty days after the transaction makes an assignment for the benefit of the creditors, be presumed, in the absence of evidence to the contrary, to have been made with the intent mentioned in subsection (2), and to be an unjust preference within the meaning of this Act whether it be made voluntarily or under pressure.

(5) The word "creditor" when used in the singular in subsections (2), (3) and (4) includes any surety and the endorser of any promissory note or bill of exchange who would upon paying the debt, promissory note or bill of exchange, in respect

of which the suretyship was entered into or the endorsement was given, become a creditor of the person giving the preference within the meaning of those subsections.

5. (1) Nothing in section 4 applies to an assignment made to the sheriff for the area in which the debtor resides or carries on business or, with the consent of a majority of the creditors having claims of $100 and upwards computed according to section 24, to another assignee resident in Ontario, for the purpose of paying rateably and proportionately and without preference or priority all the creditors of the debtor their just debts, nor to any sale or payment made in good faith in the ordinary course of trade or calling to an innocent purchaser or person, nor to any payment of money to a creditor, nor to any conveyance, assignment, transfer or delivery over of any goods or property of any kind, that is made in good faith in consideration of a present actual payment in money, or by way of security for a present actual advance of money, or that is made in consideration of a present actual sale or delivery of goods or other property where the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor.

(2) In case of a valid sale of goods or other property and payment or transfer of the consideration or part thereof by the purchaser to a creditor of the vendor under circumstances that would render void such a payment or transfer by the debtor personally and directly, the payment or transfer, even though valid as respects the purchaser, is void as respects the creditor to whom it is made.

(3) Every assignment for the general benefit of creditors that is not void under section 4, but is not made to the sheriff nor to any other person with the prescribed consent of creditors, is void as against a subsequent assignment that is in conformity with this Act, and is subject in other respects to the provisions thereof until and unless a subsequent assignment is executed in accordance therewith.

(4) Where a payment has been made that is void under this Act and any valuable security was given up in consideration of the payment, the creditor is entitled to have the security restored or its value made good to him before, or as a condition of, the return of the payment.

(5) Nothing in this Act,

> **(a)** affects the *Wages Act* or prevents a debtor providing for payment of wages due by him or her in accordance with that Act;

(b) affects any payment of money to a creditor where the creditor, by reason or on account of the payment, has lost or been deprived of, or has in good faith given up, any valid security held for the payment of the debt so paid unless the security is restored or its value made good to the creditor;
(c) applies to the substitution in good faith of one security for another security for the same debt so far as the debtor's estate is not thereby lessened in value to the other creditors; or
(d) invalidates a security given to a creditor for a pre-existing debt where, by reason or on account of the giving of the security, an advance in money is made to the debtor by the creditor in the belief that the advance will enable the debtor to continue the debtor's trade or business and to pay the debts in full.

***Fraudulent Conveyances Act*, R.S.O. 1990, c. F.29**

2. Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns.

3. Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section.

***Business Corporations Act*, R.S.O. 1990, c. B.16**

248. (1) A complainant and, in the case of an offering corporation, the Commission may apply to the court for an order under this section.

(2) Where, upon an application under subsection (1), the court is satisfied that in respect of a corporation or any of its affiliates,
(a) any act or omission of the corporation or any of its affiliates effects or threatens to effect a result;
(b) the business or affairs of the corporation or any of its affiliates are, have been or are threatened to be carried on or conducted in a manner; or
(c) the powers of the directors of the corporation or any of its affiliates are, have been or are threatened to be exercised in a manner,

that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer of the corporation, the court may make an order to rectify the matters complained of.

(3) In connection with an application under this section, the court may make any interim or final order it thinks fit including, without limiting the generality of the foregoing,

(a) an order restraining the conduct complained of;
(b) an order appointing a receiver or receiver-manager;
(c) an order to regulate a corporation's affairs by amending the articles or by-laws or creating or amending a unanimous shareholder agreement;
(d) an order directing an issue or exchange of securities;
(e) an order appointing directors in place of or in addition to all or any of the directors then in office;
(f) an order directing a corporation, subject to subsection (6), or any other person, to purchase securities of a security holder;
(g) an order directing a corporation, subject to subsection (6), or any other person, to pay to a security holder any part of the money paid by the security holder for securities;
(h) an order varying or setting aside a transaction or contract to which a corporation is a party and compensating the corporation or any other party to the transaction or contract;
(i) an order requiring a corporation, within a time specified by the court, to produce to the court or an interested person financial statements in the form required by section 154 or an accounting in such other form as the court may determine;
(j) an order compensating an aggrieved person;
(k) an order directing rectification of the registers or other records of a corporation under section 250;
(l) an order winding up the corporation under section 207;
(m) an order directing an investigation under Part XIII be made; and
(n) an order requiring the trial of any issue.

(4) Where an order made under this section directs amendment of the articles or by-laws of a corporation,

(a) the directors shall forthwith comply with subsection 186 (4); and
(b) no other amendment to the articles or by-laws shall be made without the consent of the court, until the court otherwise orders.

(5) A shareholder is not entitled to dissent under section 185 if an amendment to the articles is effected under this section.

(6) A corporation shall not make a payment to a shareholder under clause (3) (f) or (g) if there are reasonable grounds for believing that,

(a) the corporation is or, after the payment, would be unable to pay its liabilities as they become due; or

(b) the realizable value of the corporation's assets would thereby be less than the aggregate of its liabilities.

TAB 3

Ontario Court (General Division)

Citation: Central Guaranty Trust Co. v. Bruncor Leasing Inc.
Court File: B99/92
Date: 1992-10-16

Ground J.

Counsel:
Harvey G. Chaiton, for applicant.
Raymond M. Slattery, for respondent.

[1] GROUND J.:—Both counsel made at both hearings of this motion specific submissions with respect to the JSW Model BH80 Excavator (the "Excavator"). Counsel for Bruncor submits that, if I should find the security interest of Central is effective with respect to the equipment generally, this would not affect the priority of Bruncor's security interest in the Excavator. Bruncor's security interest in the Excavator was created by a chattel mortgage entered into in 1988 and perfected by the registration of a financing statement under the *Personal Property Security Act*, R.S.O. 1980, c. 375, in 1988. The financing of the purchase price of the Excavator was renegotiated in April, 1991, and a new chattel mortgage entered into covering all the equipment, and a financing statement relative to that chattel mortgage was registered on April 19, 1991, being subsequent to the date of registration of the financing statement in favour of Central covering all the equipment.

[2] It would accordingly appear that, if Bruncor's security interest in the Excavator has been continuously perfected since 1988, s. 21 of the *Personal Property Security Act*, R.S.O. 1990, c. P.10 (P.P.S.A.) would provide that it takes priority over the security interest of Central in the Excavator which was not perfected until March 2, 1990. Section 21 of P.P.S.A. provides as follows:

> 21 (1) If a security interest is originally perfected in any way permitted under this Act and is again perfected in some way under this Act without an intermediate period when it was unperfected, the security interest shall be deemed to be perfected continuously for the purposes of this Act.
>
> (2) An assignee of a security interest succeeds in so far as its perfection is concerned to the position of the assignor at the time of the assignment.

[3] Counsel for Central maintains that, as a result of the refinancing in April, 1991, the contract with respect to the Excavator was paid out by the application on April 17, 1991, of approximately $35,500 of the $55,000 notionally advanced on the refinancing to the payment of the balance owing under the original conditional sale contract covering the Excavator. It appears to be his submission that, by its terms, the conditional sale agreement ceased to have any force and effect at that time, that the security interest secured only the balance of the purchase payable under the conditional sale agreement and that that security interest ended as of April 17, 1991, and a new security was not perfected until April 19, 1991, when the new financing statement was registered and, as there was a two-day period during which Bruncor's

security interest in the Excavator was not perfected, s. 21 of the P.P.S.A. is not applicable.

[4] Counsel for Central further maintains that s. 21 of the P.P.S.A. is not applicable because it applies only where a single security interest created under one and the same instrument is perfected in two different ways, for example perfection by possession followed by perfection by registration.

[5] Counsel for Central further submits that, s. 21 of the P.P.S.A. not being applicable, Bruncor, to maintain priority, must rely on s. 45 (3) and (4) of the P.P.S.A. which provide as follows:

> 45 (3) Where the collateral is not consumer goods, the financing statement referred to in subsection (1) may be registered before or after the security agreement is signed by the debtor.
>
> (4) Except where the collateral is consumer goods, one financing statement may perfect one or more security interests created or provided for in one or more security agreements between the parties.

[6] Counsel for Central submits that, as the original chattel mortgage on the Excavator was given by Nelson Excavating and not by Andy's, the two chattel mortgages are not "between the same parties" as required by s. 45 (4) of the P.P.S.A. and, accordingly, Bruncor cannot rely on s. 45 (3). Counsel for Central also points out that the registration in 1988 of the financing statement for the original chattel mortgage was before the P.P.S.A. was amended to include s. 45 (4).

[7] Counsel for Central has also submitted that, if I should find that s. 21 of the P.P.S.A. is applicable, the trial of an issue should be directed to determine whether the refinancing between Andy's and Bruncor in April, 1991, constituted a preference and ought to be set aside. On this latter point it does not seem to me that there are any facts in dispute with respect to the refinancing in April, 1991, or as to the application of the $55,000 notionally advanced on such refinancing and, accordingly, it would appear that the only issue involved is a question of law and may be determined on this application without directing the trial of an issue: rule 20.04 (4), Rules of Civil Procedure.

[8] Counsel for Bruncor maintains that s. 21 of the P.P.S.A. is applicable in that there was no intervening period when Andy's was not indebted to Bruncor and that accordingly there was a continuing obligation on Andy's secured by the security interests on the Excavator and no intervening period when such security interests were not perfected. He points out that the P.P.S.A. itself contemplates that a security interest can be perfected even where no debt exists in that ss. 45 (3) and 23 of the P.P.S.A. provide that, if a financing statement is registered prior to the execution of a security agreement, the perfection of the security interest dates back to the registration of the financing statement.

[9] With respect to the first submission made by counsel for Central, *i.e.*, that s. 21 of the P.P.S.A. is applicable only in the case of a single security interest under one and the same instrument perfected in two different ways, counsel cited no authority for this proposition but

relied upon the definitions of "security agreement" and "security interest" in s. 1 of the P.P.S.A. where both terms are defined in the singular as follows:

> "security agreement" means an agreement that creates or provides for a security interest and includes a document evidencing a security interest;
>
> "security interest" means an interest in personal property that secures payment or performance of an obligation, and includes, whether or not the interest secures payment or performance of an obligation, the interest of a transferee of an account or chattel paper;

I am not persuaded that defining these terms in the singular leads one to interpret s. 21 of the P.P.S.A. as not being applicable when a security interest in the same subject-matter continues to be perfected although created under two different successive security agreements. Clauses (*j*) and (*k*) of s. 28 of the *Interpretation Act*, R.S.O. 1990, c. I.11, provide in effect that, unless the context otherwise requires, the use of the singular in a statute includes the plural: see *Greater Niagara Transit Commission v. Matson* (1977), 78 D.L.R. (3d) 265, 16 O.R. (2d) 351 (H.C.J.); *Re Murray and Clark* (1974), 50 D.L.R. (3d) 71, 5 O.R. (2d) 261 (H.C.J.). In the case of the definitions in the P.P.S.A. referred to by counsel, I see no basis for concluding that the context otherwise requires. In addition, it is, I believe, common practice in the business community for a financial institution to regularly renew its security agreements with customers and to register financing statements evidencing such renewals and in my view s. 21 of the P.P.S.A. is clearly applicable in these circumstances and in the case before the bar.

[10] With respect to the second submission of counsel for Central, *i.e.*, that the original security interest in the Excavator ceased to exist as of April 17, 1991, when all obligations of Andy's under the original conditional sale agreement had been fulfilled, this submission seems to be based on the proposition that one cannot have a perfected security interest absent a debt owing from the grantor to the grantee of the security interest.

[11] Counsel for Central relies for this proposition upon the decision of the Saskatchewan Court of Queen's Bench in *Saskatoon Credit Union Ltd. v. Bank of Nova Scotia* (1985), 5 P.P.S.A.C. 123, [1985] 6 W.W.R. 556, 42 Sask. R. 187, and to a lesser extent upon the decisions of the Saskatchewan Court of Queen's Bench and the Saskatchewan Court of Appeal in *Birch Hills Credit Union Ltd. v. Canadian Imperial Bank of Commerce* (1987), 7 P.P.S.A.C. 250, [1987] 6 W.W.R. 265, 62 Sask. R. 288; affirmed 52 D.L.R. (4th) 113, 8 P.P.S.A.C. 199, [1988] 5 W.W.R. 592, respectively. I agree with counsel for Bruncor that these decisions can be distinguished on the facts. In the *Saskatoon Credit Union* case the registration of the security interest of the original security agreement had expired and in *Birch Hills* the credit union had granted and registered a discharge of the original security interest. None of these decisions appears to directly address the point of whether it is possible for a valid and perfected security interest to exist absent any debt owing between the grantor and the grantee of the security interest and I have been cited no authority on this point. I note, however, that s. 13 of the P.P.S.A. clearly states that a security agreement may secure future advances. McLaren, *Secured Transactions in Personal Property in Canada*, 2nd ed. (Toronto: Carswells, 1989), expands upon the section as follows at p. 2-23:

> Section 13 states that a security agreement may secure future advances. Section 1 (1) indicates that the future advance may be one to which the secured party is either committed or may make at its discretion.

and at pp. 2-24 and 2-25:

> Consistent with the theory of secured transactions, s. 1 (1) defines security interest as an interest in collateral and thus attaches to the collateral and not to the value given for that collateral. Section 11 makes the giving of value one of the three events necessary to achieve attachment and the value required is not monetary, but consideration sufficient to support a simple contract (s. 1 (1)).
>
> • • • • •
>
> Policy arguments based on the Act's priority rules provide further support for the position that a future advance does not create a separate security interest. The general priority rule in s. 30 (1) is based on the principle of the first to perfect having priority. Therefore, if A has an attached security interest contemplating future advances and B then creates a second security interest in the same collateral before A makes a subsequent advance under this agreement, A will still have priority if A perfected first. The resolution of the dispute does not depend upon attachment but rather on the time of perfection.

[12] It seems to me, therefore, that although a security interest could not be enforced, for example by seizure and sale, if there is no debt owing between the grantor and the grantee, this does not mean that the security interest does not exist and will become an enforceable security interest when moneys are advanced from grantee to grantor. As pointed out by counsel for Bruncor, the P.P.S.A. itself seems to contemplate this situation and grants priority to the holder of a security interest perfected by registration prior to the existence of any debt owing from the grantor to the grantee of the security interest.

[13] I therefore must reject the submissions of counsel for Central with respect to the application of s. 21 of the P.P.S.A. and hold that it is applicable in the case before the bar and that Bruncor's security interest in the Excavator takes priority over the security interest of Central. Having concluded that s. 21 of P.P.S.A. is applicable to the current situation, I need not deal with the submissions of counsel for Central with respect to s. 45 (3) and (4) of the P.P.S.A.

[14] With respect to the question of whether the April, 1991 refinancing between Andy's and Bruncor constituted a preference which ought to be set aside, s. 95 of the *Bankruptcy Act*, R.S.C. 1985, c. B-3 requires that in order to set aside a conveyance or transfer of property as being made with a view to giving a creditor a preference, it must have been made within three months prior to the date of bankruptcy of the person who made the conveyance or transfer. (Under s. 96 the relevant period is 12 months if the parties are related, which does not appear to be the case here.) In our situation, the refinancing was effected in April, 1991, and the financing statement was registered on April 19, 1991. The assignment in bankruptcy was not filed until August 31, 1991, and accordingly s. 95 of the *Bankruptcy Act* is not applicable.

[15] I have also considered the provisions of the *Assignments and Preferences Act*, R.S.O. 1990, c. A-33 (the "A.P.A."). Section 4 (2) of the A.P.A. provides in part as follows:

> 4 (2) ... every such gift, conveyance, assignment or transfer, delivery over or payment made by a person being at the time in insolvent circumstances, or unable to pay his, her or its debts in full, or knowing himself, herself or itself to be on the eve of insolvency, to or for a creditor with the intent to give such creditor an unjust preference over other creditors or over any one or more of them is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

This section has been interpreted by the courts to require that the evidence establish a joint intention of the debtor and the creditor to give and receive a preference. There are presumptions that there was the necessary intent in s. 4 (3) and (4) of the A.P.A. Such presumptions, however, apply only if the transaction has the effect of giving a creditor a preference over any one or more of the other creditors and an action is brought against the debtor or the debtor makes an assignment within 60 days of the transaction. That is not the situation in the present case.

[16] In addressing the issue of requisite intent pursuant to the A.P.A., the Ontario High Court held in *Bank of Montreal v. Shean*, [1931] 4 D.L.R. 305 at pp. 308-9, 12 C.B.R. 479, [1931] O.R. 489, as follows:

> The transaction in question can only be attacked successfully when there is an intention on behalf of both the debtor and the creditor to create a preference. There must be an intention on the part of the debtor to give, and an intention on the part of the creditor to obtain, an unjust preference.

[17] Further support for this proposition is found in the decision of *Brocklesby v. Freedman-Ellis Ltd.*, [1932] 1 D.L.R. 187, 13 C.B.R. 77, [1932] O.R. 56 (H.C.J.), where it was held at pp. 191-2 as follows:

> On the language of this subsection, and without the assistance of judicial interpretation, it is clear that three conditions must concur to enable the plaintiff, in such an action as this, to succeed: — (1) The debtor must have been in insolvent circumstances, or unable to pay his debts in full, or must have known himself to be on the eve of insolvency; (2) the intention of the debtor must have been to give to the favoured creditor an unjust preference; and (3) the effect of the transaction must have been to give a favoured creditor such a preference. But in the course of the years the judicial glosses have added to the plaintiff's burden, and in the present state of the authorities he must also prove: — (4) that the creditor knew that the debtor's financial situation was that described in the section; (5) that there was an intention on the part of the favoured creditor to gain a preference; and (6) that the preference was not only an unjust, but a fraudulent preference.

[18] Furthermore, s. 5 (1) of the A.P.A. provides in part that s. 4 does not apply "to any conveyance, assignment, transfer or delivery over of any goods or property of any kind that is made ... by way of security for a present actual advance of money". Although there is a paucity

of judicial decisions interpreting s. 5 (1), it would appear clear that in our situation the new security interest in the Excavator created pursuant to the refinancing in April, 1991, was given by way of security for a present actual advance of money and s. 4 would not operate to deem such security interest to be void as against the other creditors.

[19] Accordingly, I find that the security interest of Bruncor in the Excavator ranks in priority to the security interest of Central in that piece of the equipment and that Bruncor is entitled to the proceeds of sale of that piece of equipment.

[20] Counsel are invited to make written submissions to me as to costs of both hearings of this application.

[21] Order accordingly.

TAB 4

CITATION: Krates v. Crate, 2018 ONSC 2399
COURT FILE NO.: CV-15-10830-00CL
DATE: 20180425

ONTARIO

SUPERIOR COURT OF JUSTICE

COMMERCIAL LIST

BETWEEN:	)	
	)	
KRATES KESWICK INC.	)	*Mark Dunn*, for the Applicant
	)	
Applicant	)	
	)	
– and –	)	
	)	*Lisa S. Corne*, for the Dickinson Wright LLP
STEVEN CRATE, ROBIN ANN CRATE a.k.a. ROBIN PRICE, GREGORY CRATE, LYNN J. MARKO and RYAN G. CRATE	)	No one appearing for the Canada Revenue Agency although served.
	)	
Respondents	)	
	)	
	)	
	)	**HEARD:** April 12, 2018

L. A. PATTILO J.:

Introduction

[1] The Applicant, Krates Keswick Inc. ("KKI") brings this motion for vesting orders vesting it legal ownership of four properties in Keswick, Ontario in order to align legal title to beneficial ownership. KKI submits the four properties should be vested free and clear of any encumbrances.

[2] Dickinson Wright LLP ("DW") is a law firm that acted for Crate Marine Sales Limited ("Crate Marine") in connection with its receivership and bankruptcy which occurred on December 8, 2014. DW holds a mortgage on two of the four properties which it obtained from the Respondents, Steven Crate ("Steven") and Lynn Marko ("Lynn"), to secure its legal fees. DW does not object to the vesting order. It submits, however, that it should be subject to its mortgage.

[3] Her Majesty the Queen in Right of Canada as represented by the Minister of National Revenue (the "CRA") has filed liens against the two properties owned by Steven on account of monies owing by him. CRA has indicated that it does not oppose the relief sought by KKI.

[4] For the reasons that follow, I have concluded that the vesting orders should be granted vesting ownership in the four properties to KKI, free and clear of the CRA liens but subject to DW's mortgage.

Background

[5] Crate Marine and various related companies operated from, among other locations, a large lakeside property that it owned in Keswick. Crate Marine was a family business and the officers, directors and shareholders of Crate Marine were Steven, Lynn and Gregory Crate ("Gregory") (collectively the "Crates") who are siblings. The Respondent Robin Ann Crate a.k.a. Robin Price was Steven's wife.

[6] Between 2000 and 2007, Crate Marine embarked on a development plan to assemble a number of properties adjacent to its Keswick Marina. Four properties were purchased by Crate Marine: 176, 200 and 292 Wynhurst Road, Georgina, Ontario and 274 The Queensway South, Keswick, Ontario (the "Properties"). Registered title to the Properties was placed in the name of Steven and Robin with respect to 176 Wynhurst Road, Steven with respect to 274 The Queensway South and Lynn with respect to both 200 and 292 Wynhurst Road.

[7] On September 24, 2013, CRA registered liens against 176 Wynhurst Road and 274 The Queensway South as a result of outstanding tax debts owed by Steven. CRA also registered a lien against Steven's house.

[8] On November 6, 2014, following a demand by Crawmet Corp. ("Crawmet"), its major creditor, for payment and notice of intention to enforce its security under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"), Crate Marine retained DW to act for it and signed a Corporate Retainer Agreement. David Preger, the partner at DW who acted on the file deposed that notwithstanding that the Retainer Agreement identified the client as Crate Marine; the retainer was intended to extend to DW's advice and legal services rendered to the Crates and the other debtor companies, with the objective of protecting the Crates equity in them.

[9] On November 14, 2014, Crate Marine and several related companies filed Notices of Intention to Make a Proposal pursuant to s. 50.4(1) of the *BIA*.

[10] On November 21, 2014, Crawmet commenced an application to terminate the Proposal Proceedings and appoint a receiver over the assets of Crate Marine and its related companies. Justice Penny adjourned the application but issued an order (the "Penny Order") appointing A. Farber & Partners Inc. as Interim Receiver (the "Interim Receiver"). The Penny Order provided, among other things, that while the Debtors could not make any payments to any party related to the Debtors or Steven without the written consent of Crawmet or court order, the Debtors were "entitled to withdraw reasonable legal fees and ordinary living expenses."

[11] On December 8, 2014, Crawmet's motion was granted and the Proposal Proceedings were terminated and the Receiver was appointed. At the same time, Crate Marine was put into bankruptcy.

[12] On November 21, 2014, DW had outstanding unbilled work in progress in excess of the retainer provided to it. As a condition of continuing to represent Crate Marine and the Crates, DW required that the Crates provide security to protect payment of DW's fees.

[13] On December 8, 2014, following receipt of independent legal advice, Steven and Lynn executed a guarantee of Crate Marine's debt to DW (the "Guarantee") and granted a mortgage to DW over the 292 Wynhurst Road and the 274 The Queensway South properties, which were registered in their name (the "DW Mortgage"). The Mortgage was registered on December 8, 2014.

[14] The DW Mortgage secures payment of all indebtedness and liabilities of any kind of Crate Marine, Steven and Lynn to DW, whether as principal or surety, up to an aggregate principal amount of $270,000. It provides, in part, under the heading "Indebtedness Secured By This Mortgage" as follows:

> You have at our request agreed to give this mortgage as a continuing collateral security for payment and satisfaction to us of all indebtedness, obligations and liabilities of any kind, now or hereafter existing, direct or indirect, absolute or contingent, joint or several, of the Borrower and/or you to us, whether as principal or surety, together with all expenses (including legal fees on a solicitor and client basis) incurred by us, our receiver or agent in the preparation, perfection and enforcement of security or other agreements held by us in respect of such indebtedness, obligations or liabilities, and interest thereon, including, without limitation, any indebtedness of the Borrower and/or Guarantors under the Payment Arrangements (collectively, the "Indebtedness"), but it being agreed that this mortgage at any one time will not secure that portion of the aggregate principal component of the Indebtedness outstanding at such time which exceeds the sum of TWO HUNDRED AND SEVENTY THOUSAND DOLLARS ($270,000.00).

[15] In January 2015, the Receiver determined that the Properties were (or should be) beneficially owned by Crate Marine. It commenced this application (the "Application") and

obtained leave to register a Certificate of Pending Litigation which it registered on title to the Properties on January 14, 2015.

[16] In April 2015, most of Crate Marine's assets, including its interest in the Properties, were sold to KKI, a joint venture between Crawmet and Crate Marine's next largest creditor (the "Asset Sale"). As part of the Asset Sale, the Application was assigned to KKI.

[17] In Reasons for Decision released October 17, 2017 (2017 ONSC 6195), Myers J. held that the Properties were held on a resulting trust for Crate Marine and beneficial ownership of them passed to KKI as part of the Asset Sale.

Position of the Parties

[18] KKI submits that the Properties should be vested free and clear of both the CRA liens and the DW Mortgage. In respect of the CRA liens, KKI submits that they do not have priority over its beneficial interest in the Properties.

[19] KKI further submits that the DW Mortgage is void as an improper assignment or preference pursuant to s. 4 of the *Assignments and Preferences Act*, R.S.O. 1990, c. A.33 (the "*Act*"). In the alternative, if the DW Mortgage is valid, it secures only a small portion of what is owed to DW in respect of services to Crates Marine because most of the debt was incurred after the appointment of the Interim Receiver on November 21, 2014 and the Receiver on December 8, 2014.

[20] By letter dated March 8, 2015, CRA advised that it did not intend to appear on the motion.

[21] DW submits that it is a *bona fide* mortgagee for value without notice of Crate Marine's beneficial interest. It denies that the DW Mortgage was a wrongful assignment or preference under the *Act* and submits that KKI has failed to establish that the DW Mortgage was made in contravention of the *Act*. Finally it submits, having regard to work performed, the orders of the court and the terms of the DW Mortgage, the DW Mortgage secures the total debt owing for services rendered on behalf of Crate Marine up to December 8, 2014, the date of the Receiver's appointment, and thereafter on behalf of the Crates.

Analysis

[22] Section 100 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43, as amended, provides in part that the court may by order vest in any person an interest in real property "that the court has authority to be disposed of, encumbered or conveyed."

[23] A party must have a valid and independent entitlement to possession or ownership in order for a court to issue a vesting order that extinguishes a third party's real property interest:

Third Eye Capital Corporation v. Resources Dianor Inc./Dianor Resources Inc., 2018 ONCA 253, at para. 111.

1. The CRA Liens

[24] In *Trang v. Nguyen*, 2012 ONCA 885, the Court of Appeal held that CRA liens do not create a "charge" on land within the meaning of s. 93 of the *Land Titles Act*, R.S.O. 1990, c. L.5 and accordingly do not have priority over valid prior unregistered equitable interests. Accordingly, as Crate Marine's (subsequently KKI's) unregistered equitable interest existed prior to the CRA liens, KKI's interest in the Properties has priority.

[25] As a result, I am satisfied that as CRA has no valid interest in the Properties, KKI is entitled to a vesting order granting it title to the Properties, free and clear of CRA's liens.

2. The DW Mortgage

[26] As noted above, KKI submits that the DW Mortgage is void as an improper assignment or preference pursuant to s. 4 of the *Act* and in the alternative, if the Mortgage is valid; it secures only a small portion of what is owed to DW in respect of services to Crates Marine.

i. Improper Assignment or Preference

[27] Section 4(2) of the *Act* provides:

> (2) Subject to section 5, every such gift, conveyance, assignment or transfer, delivery over payment made by a person being at the time in insolvent circumstances, or unable to pay his, her or its debts in full, or knowing himself, herself or itself to be on the eve of insolvency, to or for a creditor with intent to give such creditor an unjust preference over other creditors or over any one or more of them is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

[28] In order to establish that the DW Mortgage is void as an unjust preference under section 4(2) of the *Act*, the onus is on KKI to prove, on a balance of probabilities: 1. that a transfer or conveyance was made; 2. to a pre-existing creditor; 3. at a time when Steven and Lynn were insolvent (or knew they were on the eve of insolvency); 4. that in granting the DW Mortgage, Steven and Lynn intended to prefer DW over other creditors; and 5. DW intended to receive a preference in priority over other creditors.

[29] DW submits that KKI has no standing to bring a claim under the *Act* as there is no evidence that KKI was a creditor of the Crates at the time of the DW Mortgage. At the time of the DW Mortgage, Steven and Lynn had each signed personal guarantees on a $1 million promissory note held by a creditor of Crate Marine. Subsequently, those guarantees and the note have been assigned to KKI. Accordingly, I am satisfied that KKI has standing to assert the DW Mortgage is an unjust preference under the *Act*.

[30] The parties agree that the DW Mortgage was a transfer or conveyance within the meaning of the *Act*. KKI takes the position that DW acted only for Crates Marine and not the Crates. For subsequent reasons herein, I have rejected that position. Accordingly, as of December 8, 2014, I am satisfied that DW had outstanding debts and was a creditor of the Crates.

[31] Based on the evidence, or lack thereof, however, I am not satisfied that KKI has established that Steven and Lynn were insolvent as at December 8, 2014 or were on the eve of insolvency, that neither Steven and Lynn entered into the DW Mortgage with the intent to prefer DW over their other creditors or that DW entered into the DW Mortgage intending to receive a preference in priority to other creditors.

[32] There is no question that as at the date of the DW Mortgage, Steven and Lynn had outstanding personal liabilities. However, that does not necessarily lead to the conclusion that they were either unable to meet their obligations as they became due or that the totality of their assets was insufficient to meet their debt. Without a list of assets to compare the debts to, it is difficult to draw an inference that Steven and Lynn were insolvent. Further, neither Steven nor Lynn commenced personal bankruptcy proceedings until December 2017, more than three years after the DW Mortgage.

[33] Nor do I consider that KKI has proved that by granting the DW Mortgage, Steven and Lynn intended to prefer DW over their other creditors. KKI submits that the effect of the DW Mortgage was to prefer DW. Absent one of the presumptions set out in ss. 4(3) and (4) of the *Act* applying (and neither do in this case), the fact that a transfer has the effect of preferring one creditor in favour of another is insufficient to satisfy the intention requirements under the *Act*.

[34] KKI also submits that the circumstantial evidence around the transfer is consistent with several "badges of fraud" that raise the specter of fraudulent or unjust intent. They submit that the Crates had "actual or potential" personal liabilities at the time of the transfer; that they granted the DW Mortgage for insufficient consideration and they granted the DW Mortgage with unusual haste.

[35] The "badges of fraud" approach can establish intent under the *Act*: *Boudreau v. Marler* (2004), 185 O.A.C. 261 (C.A.), at para. 70. In my view, however, the facts relied on by KKI do not raise a specter of fraud serious enough to infer fraudulent intent. The fact that Steven and Lynn had personal liabilities at the time of the transfer is not by itself a badge of fraud. As noted, there is no evidence of their assets or whether they were unable to pay their debts as they came due. Further, there is no evidence to suggest that the DW Mortgage was granted for insufficient consideration. Finally, the evidence does not suggest there was any unusual haste in granting the DW Mortgage. The requirement for security for past and ongoing legal costs was raised with Steven and Lynn when the Interim Receiver was appointed on November 21, 2014. They subsequently sought and obtained independent legal advice, following which the DW Mortgage was granted and registered. In my view, the timing of the transfer was governed by the needs of the ongoing insolvency proceedings, not a fraudulent intent.

[36] I am satisfied from the evidence that the predominant intention of both Steven and Lynn in granting the DW Mortgage was to secure continuing legal representation in order to avoid the receivership/bankruptcy of Crate Marine and at the same time protect their interests in the insolvency proceedings.

[37] While the above findings with respect to Steven and Lynn not being insolvent or having the requisite intention to prefer DW over other creditors are sufficient to defeat KKI's submission that the DW Mortgage is void under s. 4(2) of the *Act*, I am also not satisfied that KKI has established that at the time of the transfer, DW had an intention to receive a preference in priority to other creditors of Steven and Lynn.

[38] While the requirement that the recipient of the transfer had an intention to receive a preference is not apparent from the language of s. 4(2) of the *Act*, such a requirement has been in place in Ontario since at least 1885. See: *Frauds on Creditors: Fraudulent Conveyances and Preferences* (Thompson Reuters Canada Limited, WestlawNext Canada online edition, February 2018 update), Part IV, Ch. 18(e)(ii), "The Intent of the Recipient Creditor to Receive a Preference"). See too: *Central Guarantee Trust Co. v. Bruncor Leasing Inc.*, 1992 CarswellOnt 1732, (Ont. Gen. Div.) at paras. 15 to 17.

[39] KKI concedes that at the time the DW Mortgage was granted, DW had no knowledge of Crate Marine's beneficial interest. Notwithstanding the personal liabilities of Steven and Lynn, given their ownership of the Properties, it cannot be inferred, in my view, that DW knew at the time that Steven and Lynn could not meet their obligations as they fell due and accordingly that the DW Mortgage constituted a preference.

[40] For the above reasons, therefore, I am not satisfied that KKI has met its onus of establishing the requirements of section 4(2) of the *Act* such that the DW Mortgage should be declared void. I find that the DW Mortgage is a valid mortgage and because it was registered prior to the finding of KKI's beneficial ownership of the Properties, KKI's title takes subject to it.

ii. The DW Mortgage Secures only a Small Portion of Crate Marine's Debt

[41] DW's work on behalf of Crate Marine and the Crates took place between early November 2014 and, essentially May 2015. At the outset, DW received a total retainer of $100,000 from Crate Marine. The retainer was held in trust and subsequently applied against invoices rendered for services. The last portion of the retainer was applied to partially cover an invoice dated November 30, 2014. Based on all of the invoices rendered, there remains owing to DW approximately $200,000 (excluding interest).

[42] KKI concedes that DW is entitled to be reimbursed for fees and disbursements owing on account of work done for Crate Marine prior to November 21, 2014, the date of the Penny Order appointing the Interim Receiver. KKI estimates that amount to be approximately $26,000. (I note that counsel advised me that there is a disagreement between KKI and DW as to the amount

owing in respect of each period. It was left that counsel would resolve the amounts, if necessary. Given my decision, I do not consider it necessary. I will refer to the amounts submitted by KKI.)

[43] Accordingly, the DW Mortgage secures the fees and disbursements incurred prior to November 21, 2014.

[44] KKI submits that DW is not entitled to any fees for work done on behalf of Crate Marine after November 21, 2014, which is the date on which the Interim Receiver was appointed. KKI submits that as a result of the appointment of the Interim Receiver, DW could no longer act for Crate Marine. It submits that between November 21, 2014 and December 8, 2014, DW's fees and disbursements amounted to approximately $124,000.

[45] The role of the Interim Receiver under the Penny Order was essentially one of overseeing the operation of Crate Marine and its related companies to preserve the *status quo* pending the return of the motion. The Interim Receiver's powers were limited. Although the Interim Receiver was granted control over Crate Marine's "assets, undertakings and properties", it was subject to the powers provided in the Penny Order. Specifically, it did not authorize the Interim Receiver to retain counsel. Further, paragraph 7 of the Penny Order specifically authorized Crate Marine and its related companies to withdraw reasonable legal fees.

[46] I disagree with KKI's submission that following the appointment of the Interim Receiver, DW could no longer act for Crate Marine. The Penny Order contains no such restriction. In fact, it recognizes that Crate Marine will incur "reasonable" legal fees. Crawmet's motion to terminate the proposals and appoint a receiver was still extant. It cannot be that prior to a receiver being appointed, a debtor under fire is not entitled to retain and pay counsel to defend itself. Crate Marine was entitled to retain DW to resist Crawmet's motion and DW is entitled to be paid its reasonable fees for doing so.

[47] KKI submits that the Penny Order authorized the Crates to "withdraw" reasonable legal fees, not cause Crate Marine to incur a significant debt to DW and then provide the DW Mortgage as security. It submits that in fact no legal fees were withdrawn from Crate Marine over the period. I do not interpret the Penny Order as being that restrictive. In my view, the authorization extended to incurring reasonable legal fees to permit Crate Marine to continue its opposition to Crawmet's application.

[48] KKI further submits that there is no evidence that the fees and disbursements incurred on behalf of Crate Marine between November 21, 2014 and December 8, 2014 were reasonable. However, it is KKI that submits that the fees incurred during the period were not authorized. I have concluded that reasonable legal fees were authorized. As a result, I consider the onus is on KKI to establish that the fees incurred were not reasonable. They have not done so.

[49] Accordingly, DW is entitled to be reimbursed for its fees and disbursements incurred between November 21, 2014 and December 8, 2014 and the Mortgage stands as security for them.

[50] KKI further submits that following the Receiver's appointment on December 8, 2014, Crate Marine could no longer instruct counsel and accordingly DW could no longer continue to act for Crate Marine. Only the Receiver was authorized to retain counsel on behalf of Crate Marine and the Receiver did not retain DW. KKI submits that the fees incurred by DW subsequent to December 8, 2014 were approximately $50,000 to $60,000.

[51] DW acknowledges and agrees that upon the appointment of the Receiver on December 8, 2014, its retainer by Crate Marine was terminated. It also agrees that it was not retained by the Receiver to act for Crate Marine. It submits, however, that after December 8, 2014, it continued to act for the Crates and specifically Steven and Lynn concerning their interests as officers, directors and shareholders of Crate Marine. DW further submits that the terms of the Mortgage, as set out above, specifically provide that, in addition to any indebtedness of Crate Marine, the Mortgage secures any indebtedness of Steven and Lynn to DW. Accordingly, it submits that the Mortgage also secures the fees and disbursements incurred after December 8, 2014 on behalf of Steven and Lynn.

[52] KKI takes issue with Mr. Preger's evidence that DW acted for both Crate Marine and the Crates. It submits that all of the documentary evidence establishes that DW's only client was Crate Marine. Specifically it points to the Retainer Agreement which identified the "Client" as Crate Marine; all of the invoices were addressed to Crate Marine only; and that the Crates are identified as guarantors, not clients, in the various documents relating to the DW Mortgage.

[53] Notwithstanding that the above documents refer to just Crate Marine, I accept Mr. Preger's evidence that DW acted for Crate Marine, its related companies and the Crates from the outset. While the initial retainer was only with respect to Crate Marine, the Crates interests as officers, directors and shareholders were also very much in play. Further, once the Receiver was appointed, it follows that the retainer would continue for the Crates to protect their remaining interests. The fact that there is no written retainer from the Crates is not determinative particularly given the sequence of events and the fact that events were happening quickly.

[54] Accordingly, for the above reasons, I find that the DW Mortgage also secures DW's fees and disbursements incurred after December 8, 2014.

Conclusion

[55] Based on the above, vesting orders are granted providing KKI with legal ownership of the Properties, free and clear of all interests except for the DW Mortgage.

[56] As DW was successful on this motion, it is entitled to its costs on a partial indemnity basis. Both parties have submitted Cost Outlines and the partial indemnity costs claimed are within $700.00. Given the issues, I consider the costs claimed to be fair and reasonable. Costs to DW fixed at $24,000.00 in total, payable by KKI.

[57] DW's Cost Outline indicates that its actual costs of the motion are $36,768.05. It submits, that, in accordance with the provisions of the DW Mortgage which stands as security, not only

for any indebtedness but also for "all expenses (including legal fees on a solicitor client basis) incurred by [DW]", that the difference between its partial indemnity costs payable by KKI and its actual costs of the motion should be added to the debt owing and secured under the DW Mortgage. I agree.

[58] Accordingly, the amount of $12,768.05 ($36,768.05 – $24,000.00) shall be added to the amount owing to DW by the Crate parties and secured under the DW Mortgage.

[59] Finally, the unredacted Crate invoices, provided by counsel for DW to me during the hearing, contain privileged information arising from the solicitor/client relationship. As a result, the invoices should be sealed and I so order.

L. A. Pattillo J.

Released: April 25, 2018

CITATION: Krates v. Crate, 2018 ONSC 2399
COURT FILE NO.: CV-15-10830-00CL
DATE: 20180425

ONTARIO

SUPERIOR COURT OF JUSTICE

COMMERCIAL LIST

BETWEEN:

KRATES KESWICK INC.

Applicant

– and –

STEVEN CRATE, ROBIN AN CRATE a.k.a. ROBIN PRICE, GREGORY CRATE, LYNN J. MARKO and RYAN G. CRATE

Respondents

REASONS FOR JUDGMENT

PATTILLO J.

Released: April 25, 2018

TAB 5

Plaskett & Associates Ltd.,
trustee of the estate of 633746 Ontario Inc. v.
Salvati, Masciangelo and Robert Matthew Cosmetics Inc.

Indexed as: 633746 Ontario Inc. (Trustee of) v. Salvati
(S.C. Bkcy.)

73 O.R. (2d) 774
[1990] O.J. No. 995
Action No. 31-203672-T

ONTARIO
Supreme Court of Ontario in Bankruptcy
Saunders J.
June 13, 1990.

Bankruptcy -- Fraudulent transactions -- Bankrupt declaring and paying dividend which had effect of causing liabilities of bankrupt to exceed its assets -- Indebtedness created by dividend secured under general security agreement -- Dividend contrary to s. 38 of Business Corporations Act -- Transaction leading to registration of security agreement contrary to s. 2 of Fraudulent Conveyances Act -- Security agreement void as against unsecured creditors -- Business Corporations Act, 1982, S.O. 1982, c. 4 -- Fraudulent Conveyances Act, R.S.O. 1980, c. 176.

The bankrupt company was operated until July 1987 by R.M. and V.G. Members of the G. family owned one-half of the shares and the other half was owned by R.M.C.I., the shares of which were owned by E.M., the wife of R.M. In the summer of 1987, the G. family shares were transferred to F.S. From July 27, the business was operated by R.M. and F.S. F.S. projected that the retained earnings for the following year might be high, so in August 1987, a dividend of $150,000 was declared, payable on that date but not paid until the following December. The effect

of the declaration of the dividend was to cause the liabilities of the bankrupt to exceed its assets.

In August 1987, R.S. (the brother of F.S.) and E.M. each advanced $100,000 in cash to the bankrupt. The advances were described as loans. The bankrupt issued two cheques dated December 9, 1987 for $100,000 each to E.M. and R.S. E.M. and R.S. each issued cheques for $100,000 dated December 10, 1987 which were deposited in the bank account of the bankrupt and which were said to be loans. The bankrupt entered into a general security agreement dated December 10, 1987 with R.S. and E.M. as secured parties whereby it granted a security interest to them in the assets of the bankrupt. A financing statement was registered on December 17, 1987. At the time, the bankrupt was indebted to suppliers for substantial amounts.

The dividend was paid on December 21, 1987 by issuing six promissory notes to various people but endorsed by those people in such a way that the indebtedness created by the dividend was payable to E.M. and R.S. in the amount of $75,000 each. That indebtedness was secured under the general security agreement entered into earlier in the month. E.M. and R.S. each owed $75,000 to R.M.C.I. and F.S. respectively.

In April 1988 the bankrupt informed its banker that it was insolvent. The bank appointed a receiver on May 6, a creditor issued a petition in bankruptcy on May 19, and on June 22 the bankrupt consented to a receiving order being made. The effect of the transaction described above was to provide a secured position to R.S. and E.M. on any liquidation of the assets of the bankrupt.

The trustee in bankruptcy attacked the declaration and payment of the dividend on the ground that they were made at a time when the bankrupt was insolvent or had the effect of rendering it insolvent. The trustee also submitted that the transactions were part of a settlement under s. 91 of the Bankruptcy Act. The trustee attacked the general security agreement as a preference under s. 95 of the Bankruptcy Act and submitted that the security agreement was void by reason of the Fraudulent Conveyances Act, as well as by reason of the

Assignments and Preferences Act.

Held, the declaration and payment of the dividend were prohibited under s. 38 of the Business Corporations Act and the payment was made at a time when the bankrupt was insolvent within the meaning of the Bankruptcy Act. The security agreement was void as against unsecured creditors by reason of s. 2 of the Fraudulent Conveyances Act.

Section 38(3) of the Business Corporations Act provides that the directors shall not declare and the corporation shall not pay a dividend if there are reasonable grounds for believing that the realizable value of the corporation's assets would thereby be less than the aggregate of its liabilities and its stated capital of all classes. The declaration of the dividend in this case was contrary to s. 38 of the Business Corporations Act. At the time of the purported payment of the dividend, the bankrupt was an insolvent person within the meaning of the Bankruptcy Act. The payment of the dividend was prohibited by s. 38 of the Business Corporations Act. In view of the finding that the dividend was improper, it was not necessary to decide whether the dividend transactions constituted a settlement within the meaning of s. 91 of the Bankruptcy Act.

Section 95 of the Bankruptcy Act did not apply to the transaction leading up to the registration of the security agreement as the impugned transaction occurred more than three months prior to the bankruptcy and neither R.S. nor E.M. was related to the bankrupt.

The exchange of cheques and the execution and delivery of the security agreement were made by the bankrupt with the intention to defeat, hinder, delay or defraud the creditors of the bankrupt. By the terms of s. 2 of the Fraudulent Conveyances Act, the security agreement was void as against the unsecured creditors. The saving provisions of s. 3 of the Fraudulent Conveyances Act could not be relied on in the circumstances. The defendants failed to show that the transactions were bona fide.

The evidence did not establish an agreement to charge

interest on the advances made by E.M. and R.S. E.M. and R.S. could make no claim for interest on the $200,000 indebtedness against the bankrupt estate.

Cases referred to

Benallack v. Bank of British North America (1905), 36 S.C.R. 120; Caulfield, Burns & Gibson Ltd. v. Kitchen (1956), 5 D.L.R. (2d) 669, 36 C.B.R. 59, [1956] O.W.N. 697 (H.C.J.); Koop v. Smith (1915), 51 S.C.R. 554, 25 D.L.R. 355, 8 W.W.R. 1203; Lloyd's Bank Ltd. v. Marcan, [1973] 2 All E.R. 359 (Ch. D.) [affd [1973] 3 All E.R. 754, [1973] 1 W.L.R. 1387, 117 Sol. Jo. 761 (C.A.)]; Mulcahy v. Archibald (1898), 28 S.C.R. 523; Re Panfab Corp.; Duro Lam Ltd. v. Last, [1971] 2 O.R. 202, 15 C.B.R. (N.S.) 20, 17 D.L.R. (3d) 382 (H.C.J.)

Statutes referred to

Assignments and Preferences Act, R.S.O. 1980, c. 33, ss. 4, 4(1), (2)
Bankruptcy Act, R.S.C. 1985, c. B-3, ss. 2 "insolvent person", 4, 4(3)(c), 91 [am. R.S.C. 1985, c. 31 (1st Supp.), s. 70], 95, 95(1), 101, 101(1), (2), (5)
Business Corporations Act, 1982, S.O. 1982, c. 4, s. 38 [am. 1986, c. 57, s. 4]
Fraudulent Conveyances Act, R.S.O. 1980, c. 176, ss. 2, 3, 4
Statute of Elizabeth, 13 Eliz. 1 (Eng., 1571), c. 5

ATTACK by trustee in bankruptcy on certain transactions as being contrary to the Bankruptcy Act, Fraudulent Conveyances Act and Assignments and Preferences Act.

Harry M. Fogul, for plaintiff.

James T. Beamish, for defendants.

SAUNDERS J.:-- This was a trial of issues directed by Mr. Justice Catzman, on September 8, 1988. The trustee attacked

certain transactions entered into by the bankrupt. The issues involved a dividend declaration, a security agreement and several related transactions.

The background facts are as follows:

1. The bankrupt was in the business of buying and selling footwear at the wholesale level. It dealt mainly in slow moving, off season or discontinued product lines.

2. Until July, 1987, the business was operated by Robert Masciangelo and Vincent Gil. Members of the Gil family owned one-half of the shares and the other half was owned by Robert Matthew Cosmetics Inc. (R.M.C.I.). The shares of R.M.C.I. were owned by Eva Masciangelo, the wife of Robert.

3. Some time in the summer of 1987, the Gil family shares were transferred to Eva Masciangelo. On July 27, 1987, she transferred those shares to Frank Salvati. It was not disputed that those transfers were part of a series of transactions whereby the Gil interest was bought out by Salvati. Frank Salvati said that he paid $50,000 for a one-half interest in the enterprise. There was some difficulty and delay in completing the arrangements with Gil. The nature and extent of the problems are not clear from the evidence and are not material to the issues. It is agreed that from July 27, 1987, the business was operated by Robert Masciangelo and Frank Salvati.

4. A solicitor was engaged for the bankrupt in the transactions. He also gave advice to some of the defendants. As a result of a dispute, the former solicitor for the bankrupt did not deliver the corporate records until late November or early December. The new solicitor then prepared resolutions which he backdated and had executed.

5. The audited financial statements of the bankrupt as at July 31, 1987 (subject to a qualification on opening inventory) showed an excess of assets over liabilities of approximately $75,000, notwithstanding a loss for the year under review of approximately $12,000. The report of the auditor is dated

October 2, 1987 but it was not released until November.

6. As a result of investigations prior to acquiring an interest in the bankrupt, Frank Salvati projected that the retained earnings for the following year might be as high as $235,000. On this basis, he says he planned to have distributed $75,000 to each of the shareholders and to leave the balance of the to be earned surplus in the company for working capital.

7. On instructions received about October 5, 1987, from Robert Masciangelo as president of the bankrupt, the solicitor prepared and had executed a directors' resolution dated August 3, 1987 declaring a dividend of $150,000 payable on that date. No payment was made until the following December.

Based on the July 31 audited balance sheet, and on the absence of any evidence to the contrary, the effect of the declaration of the dividend was to cause the liabilities of the bankrupt to exceed its assets.

8. Robert Salvati is a dental surgeon and the brother of Frank Salvati. On August 13, 1987, Robert Salvati and Eva Masciangelo (sometimes collectively called the 'lenders') each advanced $100,000 in cash to the bankrupt. The sum of $5,000 was used to pay legal fees and the balance of $95,000 was deposited in the bank account of the bankrupt. The advances were said to have been loans by the two individuals to the bankrupt. There was no contemporaneous written agreement with respect to the loans and in particular, the bankrupt did not issue promissory notes or enter into a security agreement.

9. As at December 1, 1987, the bankrupt was indebted to three suppliers in the following amounts: (i) Terra Footwear Ltd. -- $32,000; (ii) Genfoot Inc. -- $116,341.70; (iii) Tarrus Footwear Inc. -- $293,553.

With respect to the indebtedness to Terra, the records indicate that the last delivery of product was prior to April 30, 1987 when there was outstanding $112,098. The indebtedness was reduced to $32,000 prior to December 1, 1987. The sum of $8,000 was paid in each of the months of September and October.

Although the account was substantially reduced, the credit manager of Terra testified that the bankrupt did not comply with payment arrangements that had been stipulated by Terra and agreed to by the bankrupt.

The last significant invoice from Genfoot was dated October 30, 1987 and referred to goods of the approximate price of $34,000. A payment of $50,000 was made in October and $40,000 was paid in November. Frank Salvati said that Genfoot was not pressing for payment in 1987. The credit manager for Genfoot said that there had been no discussions with respect to payments until January 1988. The product that was sold was referred to as a ''close out" which would not have been offered to the regular customers of Genfoot. The credit manager said that it would not be unusual in such a sale to negotiate special payment terms for those products.

The last purchase from Tarrus was in July 1987 and there was no payment until December 29, when $50,000 was paid.

In addition, another substantial creditor, S. Gasperari Carlo, filed a proof of claim for product delivered in October 1987 in the amount of approximately $50,000. No payment was made to that creditor. Cheques dated in April, May and June, 1988 were not honoured.

10. The bankrupt issued two cheques dated December 9, 1987 for $100,000 each to Eva Masciangelo and Robert Salvati. The cheques were cleared by the bank of the bankrupt on December 14, 1987.

11. Eva Masciangelo and Robert Salvati each issued cheques for $100,000 dated December 10, 1987 which were deposited in the bank account of the bankrupt. The advances were said to be loans. No promissory note or evidence of indebtedness was issued by the bankrupt. However, the bankrupt entered into a general security agreement dated December 10, 1987 with Robert Salvati and Eva Masciangelo as secured parties whereby it granted a security interest to such parties in the assets of the bankrupt. A financing statement evidencing such security interests was registered on December 17, 1987.

12. About December 21, 1987, the bankrupt paid the dividend declared the previous August by issuing promissory notes. There were six promissory notes in evidence, all dated December 21, 1987 in the principal amount of $75,000 and bearing interest at 15 per cent payable semi-annually. The notes were (1) from the bankrupt to R.M.C.I. which was endorsed by that corporation to Eva Masciangelo; (2) from the bankrupt to Frank Salvati which was endorsed to Robert Salvati; (3) from Eva Masciangelo to R.M.C.I.; (4) from Robert Salvati to Frank Salvati; (5) from the bankrupt to Eva Masciangelo; (6) from the bankrupt to Robert Salvati.

In the statement of claim, it is said that Eva Masciangelo and Robert Salvati, on or about December 21, 1987, advanced the sum of $75,000 each to the bankrupt. That statement was admitted by the defendants but there is no evidence that the bankrupt received that amount. At trial, the parties agreed that notes (1) and (2) were issued in payment of the dividend. Notes (3) and (4) were given back in consideration of the endorsements on notes (1) and (2) and notes (5) and (6) were replacement notes evidencing the indebtedness created by the endorsements.

The result of the exchange of the promissory notes was:

(1) that the dividend was paid, creating an indebtedness of $150,000;

(2) by reason of the endorsements and the issuance of notes (5) and (6), the indebtedness created by the dividend was payable to Eva Masciangelo and Robert Salvati in the sum of $75,000 each;

(3) that indebtedness was secured under the general security agreement entered into earlier in the month;

(4) Eva Masciangelo and Robert Salvati each owed $75,000 to R.M.C.I. and Frank Salvati respectively.

There was no reference or reflection of the dividend or the

resulting indebtedness on the financial statements as at December 31, 1987, which were prepared, reviewed and commented on by the independent auditor of the bankrupt. The letter from the auditor was dated February 19, 1988. Frank Salvati said the failure to record the dividend on the books of the bankrupt or to inform the auditors about it was an oversight.

13. In late April 1988, after seeking advice from a licensed trustee, the bankrupt informed its banker that it was insolvent. The bank was not previously aware of the situation although it had been pressing for the April results which had not been provided. The bank appointed a receiver on May 6. A creditor issued a petition in bankruptcy on May 19. On June 22, the bankrupt consented to a receiving order being made.

Frank Salvati and Robert Masciangelo testified that in December 1987, they intended to continue carrying on the business and did not anticipate its failure a few months later. They attributed the failure to general economic conditions, lower sales, competition and other factors. It is worth noting that the inventory of the bankrupt rose from $540,000 at December 31, 1987 to $1,200,000 at the time of the appointment of the receiver. Accounts payable also rose from $363,000 to $1,200,000 in the same period.

The trustee attacked the declaration and payment of the dividend on the ground that they were made at a time when the bankrupt was insolvent or had the effect of rendering it insolvent. The trustee also submitted that the transactions were part of a settlement under s. 91 [am. R.S.C. 1985, c. 31 (1st Supp.), s. 70] of the Bankruptcy Act, R.S.C. 1985, c. B-3. The trustee also attacked the general security agreement as a preference under s. 95 of the Bankruptcy Act. The trustee also submitted that the security agreement was void by reason of the Fraudulent Conveyances Act, R.S.O. 1980, c. 176, as well as by reason of the Assignments and Preferences Act, R.S.O. 1980, c. 33.

The defendants submitted that the dividend was properly declared and payable and that it fell under the security agreement. They also submitted that the security agreement was

valid and enforceable with respect to both the advances made to the bankrupt and with respect to the dividend indebtedness.

Before examining the impugned transactions in detail, some preliminary comments can be made. The effect of the transactions was to provide a secured position to Robert Salvati and Eva Masciangelo on any liquidation of the assets of the bankrupt. They would be behind the bank but ahead of the unsecured creditors.

Frank Salvati is a chartered accountant. His brother Robert and Eva Masciangelo are not sophisticated in corporate affairs. The solicitor candidly admitted that he did not understand or participate in the December 21 dividend payment transactions. He also had little understanding of the December 9 and 10 transactions although he prepared the security agreement and attended to the registration of the financing statement.

Robert Masciangelo, the president of the bankrupt, professed no knowledge of security matters. He would not even admit that the bank had a prior secured position. His evidence was not credible but he, like the lenders, did not understand the technical implications of the transactions although he probably understood their purpose. Frank Salvati knew what he wanted to do. He intended to provide security for the monies advanced and for the payment of the dividends. He planned and directed the transactions and the others went along with him. In general, he was not a credible witness and, as in many similar situations, what was done is more significant in determining intent than the subsequent expression of intent at trial.

THE DIVIDEND

The corporate records show that a dividend in the aggregate amount of $150,000 was declared by the bankrupt on August 3, 1987. The financial condition of the bankrupt at that time was set out in the audited financial statements as at July 31, 1987. They showed an excess of assets over liabilities and capital of approximately $75,000. On December 20, 1987, the dividend was paid by promissory notes to the shareholders. The unaudited financial statements as at the following December 31,

showed an excess of assets over liabilities and capital of approximately $141,000.

Section 38 [am. 1986, c. 57, s. 4] of the Business Corporations Act, 1982, S.O. 1982, c. 4, which governs the affairs of the bankrupt, provides for the declaration and payment of dividends. Subsection (3) of that section says in part:

> (3) The directors shall not declare and the corporation shall not pay a dividend if there are reasonable grounds for believing that,
>
> . . . . .
>
> (b) the realizable value of the corporation's assets would thereby be less than the aggregate of,
>
> (i) its liabilities, and
>
> (ii) its stated capital of all classes.

Section 101 of the Bankruptcy Act provides in part,

> 101(1) Where a corporation that is bankrupt has within twelve months preceding its bankruptcy paid a dividend ... the court may, on the application of the trustee, inquire into whether the dividend was paid ... at a time when the corporation was insolvent or whether the payment of the dividend ... rendered the corporation insolvent.
>
> . . . . .
>
> (5) For the purposes of an inquiry ... the onus of proving that the corporation was not insolvent when a dividend was paid ... or that the payment of a dividend ... did not render the corporation insolvent lies on the directors and the shareholders of the corporation.

"Insolvent person" is defined in s. 2 of the Bankruptcy Act as follows:

"insolvent person" means a person who is not bankrupt and who resides or carries on business in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and

(a) who is for any reason unable to meet his obligations as they generally become due,

(b) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or

(c) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due ...

The financial condition of the bankrupt at the time of the declaration of the dividend was as set out in the financial statements as at the previous July 31. The statements were subject to a qualification on the amount of the opening inventory. There was no evidence that an adjustment was necessary, that the liabilities were overstated or that the stated value of the assets were less than their realizable value. On the basis of the financial statements and the absence of evidence to the contrary, I conclude that the declaration of the dividend on August 3 was contrary to s. 38 of the Business Corporations Act.

More important was the payment of the dividend on the following December 20. The unaudited financial statements showed an excess of assets over liabilities and capital of approximately $141,000. The declaration and payment of the dividend were not reflected in those financial statements. If they had been, the liabilities would have exceeded the assets by about $9,000. There was no evidence that the liabilities were overstated. There was evidence to the effect that the value of the assets shown on the statement substantially exceeded the amount that would have been realized at a fairly conducted sale under legal process. That evidence was given by

Mr. Marvin Zweig, a chartered accountant and a licensed trustee, who was an employee of the receiver when the assets were disposed of. Mr. Zweig was of the opinion that the assets as set out on the balance sheet as at December 31, 1987 were substantially overstated in value. On this issue, I would prefer his evidence over that of Frank Salvati and Robert Masciangelo. He based his opinion on the amounts realized on the disposition of the inventory, the collectibility of the accounts receivable and an analysis of the financial records relating to deposits, prepaid expenses and fixed assets. He conceded that the time of the sale of the inventory and the fact that the sale was out of the ordinary course of business would have had an adverse effect on the amount realized. Taking a conservative view of his evidence, I have no difficulty in finding that as at December 31, 1987, the aggregate of the property of the bankrupt, if disposed of at a fairly conducted sale under legal process, would not have been sufficient to enable payment of all obligations due and accruing. This would have been so without regard to the dividend payment. I find that the amount of the realizable value of the assets would have been reduced by at least $200,000 from the amount shown on the balance sheet. It follows that, at the time of the purported payment of the dividend, the bankrupt was an insolvent person within the meaning of the Bankruptcy Act. Furthermore, the payment of the dividend was prohibited by s. 38 of the Business Corporations Act.

The payment of the dividend was based on the projections made by Frank Salvati in the summer of 1987 that the operations for the next year would be profitable to an extent that would permit the payment of such a dividend and leave the bankrupt with sufficient working capital. The results in the first five months were positive but not in line with the projection. Frank Salvati had estimated earnings for the year at $235,000. The net income for the five-month period before an unusual item and income taxes was $25,000. Robert Masciangelo said that the intention was to evidence the dividend obligation by promissory notes and pay off those notes when cash became available. In most corporations, the declaration and payment of a dividend does not take place until there is a cash surplus available for distribution. In any event, the intention is not significant.

If the financial condition of a corporation does not permit the declaration and payment of a dividend, certain consequences follow under the Business Corporations Act and the Bankruptcy Act. Directors are liable to the corporation for payments made contrary to s. 38 of the Business Corporations Act. Shareholders may also be required to repay money or property received by them with respect to an improper dividend. Section 101(2) of the Bankruptcy Act provides that where it is found that a payment of a dividend was made when the corporation was insolvent, the court may give judgment in favour of the trustee against the directors and those recipient shareholders who are related to one or more directors.

No cash was paid. Instead, the dividend was paid by promissory notes. By a series of note transactions, the dividend indebtedness was transferred to Robert Salvati and Eva Masciangelo and thus became secured under the general security agreement. Neither Robert Salvati nor Eva Masciangelo are directors or shareholders of the bankrupt so they could not be liable for judgment under s. 101(2). However, Frank Salvati and R.M.C.I. could be so liable. The trustee did not ask for judgment. If the dividend were found to be improper, both parties were content with a declaration that the dividend was prohibited under s. 38 and that payment was made when the bankrupt was insolvent. On that basis, the bankrupt estate could be administered as if the dividend had never been declared or paid.

It was submitted that the bankrupt was insolvent on December 20, 1987 because it had ceased paying its current obligations in the ordinary course of business as they generally became due. The business of the bankrupt was not that of a typical clothing wholesaler. The bankrupt dealt in end-of-season surplus and other slow-moving goods. It took the goods off the hands of manufacturers and tried to find a market for them. It was sometimes necessary to warehouse goods for a lengthy period until a buyer could be found. I accept the evidence given on behalf of the defendants that payment terms were flexible and subject to negotiated revision.

There were substantial overdue debts to the creditors

previously referred to. There was some evidence that agreed payment arrangements had not been met. Notwithstanding, I am not prepared, in all the circumstances, to find that the bankrupt had, on December 20, 1987, ceased paying its current obligations in the ordinary course of business as they generally became due. This finding does not affect the result as I have already found the bankrupt to have been insolvent by reason of the excess of liabilities over the value of the assets.

The trustee submitted that the dividend transactions constituted a settlement within the meaning of s. 91 of the Bankruptcy Act. The trustee said that the effect of the transaction was to enable the bankrupt on a liquidation to pass out $150,000 representing equity to relatives of the directors and shareholders because of the security agreement. In view of the finding that the dividend was improper, it is not necessary to reach a conclusion on that submission.

THE GENERAL SECURITY AGREEMENT

The trustee attacked the general security agreement under three statutes: s. 95 of the Bankruptcy Act, s. 2 of the Fraudulent Conveyances Act, and s. 4 of the Assignments and Preferences Act.

An essential element under each statute is the intention of the bankrupt.

1. Section 95(1) of the Bankruptcy Act deals with transactions made with a view of giving a creditor a preference over other creditors.

2. Section 2 of the Fraudulent Conveyances Act deals with transactions made with intent to defeat, hinder, delay or defraud creditors or others.

3. Section 4(1) of the Assignments and Preferences Act deals with transactions made with intent to defeat, hinder, delay or prejudice creditors. Section 4(2) adds the intent to give an unjust preference over other creditors.

On or about August 20, 1987, each of Robert Salvati and Eva Masciangelo advanced $100,000 to the bankrupt. There is no dispute that the advances were intended to be loans. No promissory notes were issued and there was no written evidence of the indebtedness. All the defendants testified that it was the intention that the loans would be secured. The solicitor said he discussed a debenture with Frank Salvati and Robert Masciangelo. It was to be in terms similar to those in a shareholders' agreement he had prepared involving Masciangelo and other parties. Frank Salvati said that he never saw that agreement. The solicitor did not recall discussing security with either Robert Salvati or Eva Masciangelo.

The solicitor said that he had prepared a draft security agreement in April in connection with an earlier proposed transaction. He was unable to produce a copy of it. His evidence indicated a lack of familiarity with security transactions. He may have been confusing the security agreement with the shareholders' agreement he had prepared. The only security agreement in evidence was the agreement dated December 10, 1987 which was executed by the bankrupt.

The evidence of the solicitor as to the reason the security agreement was not executed until December is far from clear. He said that he needed the corporate records to check the names of the officers and directors and that he was waiting for advice from Robert Masciangelo that the "deal" had been consummated. His explanation is hard to understand. The funds constituting the advance had gone through his trust account and he knew they had been received by the bankrupt. Robert Masciangelo and Frank Salvati were operating the business although Vincent Gil may still have been on the premises. All matters involving Gil had not been completely settled. If security was to be taken, that was the time to have done it. If the solicitor had received instructions, he had in his possession, or could have obtained, the necessary information to prepare the document. He agreed that the preparation would have been his responsibility and not that of the previous solicitor.

When he did receive the corporate records, he prepared some

resolutions. He said he backdated them and had them executed. For example, the resolution declaring the dividend was backdated to August 3, 1987. He did not backdate the security agreement to August 20 or the resolution authorizing it. Instead, he prepared and had executed an agreement and resolution each dated December 10, 1987. He said he did not prepare security for the earlier advance on the advice of counsel.

The solicitor said that advice received from counsel was to the effect that if the advances were to be secured, new consideration was required. He said that he instructed his clients of that requirement. He did not make the arrangements. He apparently did no more than prepare the security agreement and resolution, have them executed and attend to the registration of the financing statement.

On December 9, 1987, the bankrupt issued cheques for $100,000 each to Robert Salvati and Eva Masciangelo. On the next day, they each deposited cheques in like amount in the bank account of the bankrupt. The December 9 cheques were cleared on December 14. Robert Masciangelo said that the transactions were discussed with the bank. It was arranged that the bankrupt might issue cheques in the aggregate amount of $200,000 on December 9, provided the equivalent funds were immediately re-deposited.

It was submitted that the dominant intent of the transactions on December 9 and 10 was to carry out an agreement made the previous August to secure the advances made August 20. I find, on the evidence, there was no such agreement. At the most, there might have been discussions about the desirability of taking security. The funds were advanced without an agreement or anything in writing about it. Even when the corporate records were available and backdated resolutions were prepared, there was nothing said about an agreement to give security in August. The advice said to have been received from counsel that new consideration was required and the mechanics of the exchange of cheques are consistent with there being no enforceable agreement to give security in existence. I find on the balance of probabilities that the solicitor did not receive

instructions to prepare the security agreement until some time in December 1987.

On December 9, the loans made in the previous August were paid off. Identical amounts were advanced the next day by the same lenders. As the December 9 cheques did not clear until five days later, there was no adverse affect on the bank balance of the bankrupt. There was no change in the relationship of the parties. The bankrupt remained indebted to each of Robert Salvati and Eva Masciangelo in the amount of $100,000.

The obvious effect of the transaction was to convert unsecured loans into secured loans. In the absence of any evidence to the contrary, it may be inferred that the bankrupt intended that effect. The result was to put the lenders ahead of the unsecured creditors.

The defendants submitted that what was done was not a last ditch attempt to shore up the indebtedness but rather that the security was granted in the honest belief that the business would carry on. I recognize that not all security taken for past indebtedness is improper. However, I cannot accept the defendants' view of the evidence. The operating results for the five-month period were considerably below expectations. Four months later the bankrupt found it necessary to confess its insolvency. While Frank Salvati and Robert Masciangelo might have had some hope for success, the situation was precarious at best. The increase in the purchase of inventory with the consequent increase in the unsecured payables was consistent with an effort by them to protect the personal liability on the guarantees to the bank as well as the advances and dividend payments which had been secured.

The transactions on December 9 and 10 had no other purpose or effect than to provide security for the advances and to set the stage for placing the purported dividend under the security agreement. They were artificial transactions devised by Frank Salvati. They were part of a scheme whereby, in the event of bankruptcy or receivership, the bank indebtedness would be discharged and the funds supplied by the defendants would be

recouped. The discharge of the bank indebtedness would have had the effect of removing the liability of the defendants who had guaranteed the indebtedness.

It is significant that the impugned transaction was made to a close relative of one shareholder and to the controlling shareholder of the other. While the transactions did not result in a retention of a benefit by the bankrupt, they were of considerable benefit to the defendants. As at December 31, 1987, there was secured bank indebtedness of $450,000 and secured indebtedness to the lenders of $350,000 for a total of $800,000. As previously found, the realizable assets of the bankrupt at that date was no more than $872,000. It can be seen that the effect of the security transaction was to leave very little for the unsecured creditors who then had claims of approximately $380,000.

In my opinion, the trustee has established the requisite intent of the bankrupt under the three statutes.

SECTION 95 OF THE BANKRUPTCY ACT

The impugned transactions occurred in December 1987. The effective date of the bankruptcy was May 19, 1988. The transactions are, therefore, outside the three-month period stipulated in s. 95(1).

The three-month period is extended to 12 months if the lenders are related to the bankrupt within the meaning of s. 4 of the Bankruptcy Act. In my opinion, neither Robert Salvati nor Eva Masciangelo were so related. Neither controlled the bankrupt or belonged to a related group that controlled it. The shareholders were R.M.C.I. and Frank Salvati who each owned one-half of the outstanding shares. There was no evidence drawn to my attention that either controlled the bankrupt. Nor was there any such evidence that the two shareholders formed a related group.

The trustee submitted that each of the shareholders had the right to acquire the shares of the other and therefore should, for the purpose of control, be considered an owner of all the

shares (s. 4(3)(c) of the Bankruptcy Act). The submission was based on a draft shareholders agreement which had been prepared when another person was negotiating to purchase the Gil shares. The agreement contained a provision requiring any party who desired to "withdraw" from the corporation to first offer his shares to the others. If the offer was not accepted, the shares could be sold to an outside party on specified terms and conditions. A shareholder would only have the right to acquire if an offer were to be made. As previously stated, Frank Salvati said he never saw the draft agreement. There is no evidence that a buy-sell agreement was ever discussed. The evidence does not support a finding that either shareholder had a right to acquire the shares of the other.

The trustee also submitted that on December 10, 1987, Eva Masciangelo owned one-half of the shares of the bankrupt directly and the other half indirectly as the sole shareholder of R.M.C.I. That submission was based on the evidence that the corporate records, including the resolution approving the transfer of shares to Frank Salvati, were not executed until some time after December 10. Assuming that to be the case, it is clear from the evidence that Frank Salvati became a beneficial owner of the shares in the previous summer and that on December 10, Eva Masciangelo did not control the bankrupt.

As neither Robert Salvati nor Eva Masciangelo were related to the bankrupt, it follows that s. 95 does not apply to the situation before the court because the impugned transactions occurred more than three months prior to the bankruptcy.

THE FRAUDULENT CONVEYANCES ACT

As stated previously, I am of the opinion that the exchange of cheques and the execution and delivery of the security agreement were made by the bankrupt with the intention to defeat, hinder, delay or defraud the creditors of the bankrupt. By the terms of s. 2 of the Fraudulent Conveyances Act, the security agreement is void as against the unsecured creditors, subject to ss. 3 and 4 which provide:

> 3. Section 2 does not apply to an estate or interest in

real property or personal property conveyed upon good consideration and bona fide to a person not having at the time of the conveyance to him notice or knowledge of the intent set forth in that section.

4. Section 2 applies to every conveyance executed with the intent set forth in that section notwithstanding that it was executed upon a valuable consideration and with the intention, as between the parties to it, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred, unless it is protected under section 3 by reason of bona fides and want of notice or knowledge on the part of the purchaser.

There are three requirements for the applicability of s. 2. They are (1) good consideration; (2) bona fide conveyance; and (3) absence of notice or knowledge of the s. 2 intent.

(1) Good consideration

The aggregate amount of $200,000 was advanced by the lenders in August 1987. The purpose of the impugned transactions was to provide security for those earlier advances. That circumstance does not take the transactions out of s. 2. Past consideration can be good consideration (Mulcahy v. Archibald (1898), 28 S.C.R. 523, at p. 529; Re Panfab Corp.; Duro Lam Ltd. v. Last, [1971] 2 O.R. 202, 15 C.B.R. (N.S.) 20, 17 D.L.R. (3d) 382 (H.C.J.), at p. 208 O.R., p. 26 C.B.R. (N.S.).

(2) Bona fide conveyance

The words bona fide constitute a separate and distinct requirement to be met before s. 3 can be applicable. Reading the section along with s. 2, it appears that a transaction made to defeat, hinder, delay or defraud creditors and others may still be bona fide. If that were not so, s. 3 would never be applicable. In my opinion, the words refer to the good faith of the transferees which, in this case, were the lenders. They may also refer as well to the good faith of the bankrupt. Furthermore, it is my opinion that a transaction may not be bona fide even if the transferee has no notice or knowledge of

the s. 2 intent.

In Lloyds Bank Ltd. v. Marcan, [1973] 2 All E.R. 359 (Ch. D.) [affd [1973] 3 All E.R. 754, [1973] 1 W.L.R. 1387, 117 Sol. Jo. 761 (C.A.)], Vice Chancellor Pennycuik was considering the modern English version of the Statute of Elizabeth, 13 Eliz. 1 (Eng., 1571), c. 5. He said at pp. 368-69 All E.R.:

> So it seems to me that a transferee seeking to take advantage of this subsection must establish both the requirements of the subsection, ie there must be a conveyance for valuable or for good consideration in either case in good faith, and the person must not have notice of the intent to defraud.
>
> I find great difficulty in seeing what is meant by the first requirement. Whose good faith is intended? Does the requirement add anything, and, if so, what, to what is already contained in sub-s (1) (sec. 2) and in the second requirement of sub-s (3) (sec. 3)? Counsel for Mr. and Mrs. Marcan contended that the words "in good faith", which reproduce the words "bona fide" from s 6 of the Statute of Elizabeth, indicate that the transaction must be a genuine one as between the parties. I was referred to a statement of Kay L.J. in Mogridge v. Clapp, [1892] 3 Ch. 382 at 401, under another section of the Act then in force, in which he says: "Good faith in that connection must mean or involve a belief that all is being regularly and properly done".

Once the intent under s. 2 has been established, the onus is on the defendants to show that s. 3 is applicable. This is particularly so where there are close family relationships. In Koop v. Smith (1915), 51 S.C.R. 554, 25 D.L.R. 355, 8 W.W.R. 1203, Mr. Justice Duff said at p. 558 S.C.R., p. 358 D.L.R.:

> ... but I think it is a maxim of prudence based upon experience that in such cases a tribunal of fact may properly act upon that when suspicion touching the reality or the bona fides of a transaction between near relatives arises from the circumstances in which the transaction took place then the fact of relationship itself is sufficient to put the burden of explanation upon the parties interested and that, in such

a case, the testimony of the parties must be scrutinized with care and suspicion; and it is very seldom that such evidence can safely be acted upon as in itself sufficient.

The monies were advanced in August. No security was given for the advance and there was no agreement to give it, although the matters might have been discussed. In December, the lenders received cheques in payment and the next day, they issued cheques to the bankrupt in identical amounts. These transactions were not drawn to the attention of either of the lenders when they testified. In cross-examination, Robert Salvati said that something was done in December but that is all that he could recall about it. Eva Masciangelo was not asked about the exchange of cheques.

The transactions were artificial and had no substance. In my opinion, they were not genuine transactions. Even if the lenders were unaware of their exact implications, they must have been aware of their artificiality. In the absence of any explanation, they must be taken to have known that the only purpose for the otherwise purposeless exercise was to give them some advantage over the other creditors. There are two possibilities. First, that they were told the purpose. If that is so, Robert Salvati has either forgotten or was not admitting it. The second possibility is that they made no inquiry but simply did as they were asked. In my opinion, participating without inquiry in purposeless transactions by issuing and receiving cheques for substantial amounts of money is not participating in a bona fide transaction. The security agreement was part of those transactions.

I would therefore conclude that the defendants have failed to show that the transactions were bona fide.

(3) Notice or knowledge of intent

The intent of the bankrupt operating through the directing mind of Frank Salvati has been established. The evidence does not support a finding that either of the lenders had notice or knowledge of that intent. However, for reasons already stated, the defendants have failed to show absence of such notice or

knowledge.

As the transactions under which it was created were not bona fide, the security agreement is void against the creditors defeated, hindered, delayed or defrauded thereby.

THE ASSIGNMENTS AND PREFERENCES ACT

In light of the finding under the Fraudulent Conveyances Act, it is not necessary to consider in detail the Assignments and Preferences Act. As in the case of the former statute, I have already determined that the bankrupt had the requisite intent required for s. 4(1) and 4(2). Although there is no such requirement in the statute, it appears that a concurrent fraudulent intent on the part of the lenders must be shown. (See Benallack v. Bank of British North America (1905), 36 S.C.R. 120, at p. 128; Caulfield, Burns & Gibson Ltd. v. Kitchen (1956), 5 D.L.R. (2d) 669, 36 C.B.R. 59, [1956] O.W.N. 697, 698 (H.C.J.).) As previously stated, the evidence does not support a finding of concurrent intent.

INTEREST

The lenders claimed interest at the rate of 15 per cent per annum on the advances made by them on August 20, 1987. The trustee does not dispute that they are each owed $100,000 but does dispute the claim for interest. The issue was not raised in the pleadings. However, the parties agree that it should be dealt with at this time.

No promissory notes were issued at the time of the August advance. The lenders each said that it was their understanding that the advance would bear interest at 15 per cent per annum. The draft shareholders agreement previously referred to called for interest on shareholders loans at the prime rate plus one per cent. Frank Salvati said he never saw that document. The solicitor does not remember showing the document to him or recommending its use. He had very little contact with the lenders and did not recall discussing interest with them. There were also no promissory notes issued in December when the lenders delivered cheques and the security agreement was

delivered. The notes issued in payment of the purported dividend on December 21 did bear interest at 15 per cent per annum.

The financial statements as at December 31, 1987 were prepared by the independent auditors who conducted a review and delivered written comments on February 19, 1988. The balance sheet shows under liabilities: "Shareholders Advances (Note 4) $200,000". Note 4 says:

> The shareholders' advances are non-interest bearing, unsecured, with no fixed terms of repayment.

There were no shareholders' advances shown on the statement as at July 31, 1987. It is common ground that the reference to shareholders' advances in the balance sheet is to the monies advanced by Robert Salvati and Eva Masciangelo. Frank Salvati said that the failure to advise the auditors of the correct terms was "somewhat of an oversight". I find that it was more than that. I find that Frank Salvati or someone with authority to speak to the auditors told them that the advances were non-interest-bearing, unsecured with no fixed terms of repayment.

When the statements were received, Frank Salvati made some changes. He added an interest liability of $12,500 which is equivalent to 15 per cent on $200,000 for a period of five months. It is noted that he did not provide for interest on the dividend transaction although he did add $150,000 to the liabilities to reflect that obligation. The changes that he made would have to have been done by him after February 19, 1988.

The ledger of the bankrupt also records a debit item of $12,500 as at December 31, 1987. A note was entered against the item to the effect that it was to record payment of interest expense of a loan to the company for five months at 15 per cent per annum. On the evidence, I find that entry must have been made after February 19, 1988 or it would have been included in the financial statements or commented upon by the auditors.

There was no demand by the lenders for either interest or the repayment of the loans until May 21, 1988. Frank Salvati said that interest may have been discussed and questions asked.

In my opinion, there was no agreement to charge interest on the advances. Apart from the testimony of the lenders and Frank Salvati, the evidence is inconsistent with such an agreement. I cannot accept the evidence of the defendants on this point.

The late effort to provide for interest was ineffective. No demand for repayment was made and there is no evidence of other consideration given for the accrual of interest on the books of the bankrupt. The entries were made no earlier than February 1988, which was about two months prior to the admitted insolvency. A demand was made on May 19 and acknowledged on the following May 23. The latter date was subsequent to the effective date of the bankruptcy. The lenders can make no claim for interest on the $200,000 indebtedness against the bankrupt estate.

CONCLUSION

The purported declaration and payment of the dividend were prohibited under s. 38 of the Business Corporations Act and the payment was made at a time when the bankrupt was an insolvent person within the meaning of the Bankruptcy Act. By reason of s. 2 of the Fraudulent Conveyances Act, the security agreement is void as against creditors and others defeated, hindered, delayed or defrauded thereby.

Robert Salvati and Eva Masciangelo are not entitled to claim interest against the estate on the monies advanced by them.

No order is made with respect to costs at this time. If the parties wish to make submissions on costs, they may do so either by exchanging and filing memoranda or by arranging an attendance.

Order accordingly.

INVT CRPT

TAB 6

COURT FILE NO.: 96-CU-114234
DATE: 20021210

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:	)	
	)	
ELISA CONTE, Executrix and Trustee for CESIDIO CONTE and ELISA CONTE	)	Joseph J. Colangelo *for the Plaintiffs*
	)	
Plaintiffs	)	
- and -	)	
	)	
JOE ALESSANDRO also known as GIUSEPPE ALESSANDRO, a bankrupt, GREGORINA ALESSANDRO, ALBA ALESSANDRO and A. Farber & Partners Inc., Trustee in bankruptcy of the estate of the said GIUSEPPE (aka) JOE ALESSANDRO	)	William G. Dingwall, Q.C. for the Defendants
	)	**HEARD:** September 17, 18, 20 and 23, 2002
Defendants	)	

ROULEAU J.:

I. INTRODUCTION

[1] This action was brought by Cesidio and Elisa Conte ("Cesidio" and "Elisa" respectively) to set aside two non arm's length transactions and to declare them fraudulent and void. The first non arm's length transaction was a conveyance of 1629 James Street, Tiny, Ontario ("the property") from the defendant Giuseppe Alessandro ("Joe") to his wife, the defendant Gregorina Alessandro ("Gregorina"). The second non arm's length transaction was a $225,000 mortgage placed on the property by Gregorina in favour of her daughter, the defendant Alba Alessandro ("Alba"). The plaintiffs also sought other ancillary relief, and the defendants counterclaimed seeking declarations that the property is in fact beneficially owned by Gregorina and that Alba's mortgage is valid.

[2] The issue in this action is whether the two transfers of property were fraudulent conveyances: the transfer of property from an insolvent husband to his wife and the subsequent mortgage of the property by the wife to their daughter. I have concluded that both transactions are fraudulent conveyances.

II. THE FACTS

[3] The plaintiff Cesidio died before trial, and the action was continued by his estate. As his death was anticipated, the parties videotaped his testimony which was admitted at trial.

[4] The defendant Joe declared bankruptcy in February 2002 and, by order of Wilson J., the plaintiffs were allowed to continue the present action. The trustee in bankruptcy decided not to continue to defend the action and consented to judgment against the bankrupt. For purposes of the trial, therefore, only the defendants Gregorina and Alba defended.

A) THE DEBT

[5] Cesidio and Joe were former partners with two others in a lumber business. In the late 1980s, Joe bought out Cesidio for $400,000 made up of $50,000 cash and a $350,000 promissory note due February 1, 1993. When the note became due in February 1993, the plaintiffs demanded payment but the debt was not paid. Cesidio brought an action for recovery of the $350,000 which resulted in the judgment of Cameron J. dated April 3, 1996. This judgment awarded Cesidio and Elisa Conte $413,768.33 and solicitor and client costs. The judgment bears interest at 10% annually.

[6] Despite repeated attempts at collection including a judgment debtor examination, nothing has been paid on this debt. As at the 17th day of September 2002, I was advised that the value of the judgment, with interest, was $642,831.74.

B) THE PROPERTY

[7] In 1972, a numbered company purchased the property that was, at the time, a vacant cottage lot near Georgian Bay. Shortly thereafter the defendant Joe took title of the property in his name “to uses.” Although there is conflicting evidence on the point, it appears that the property was purchased as part of an arrangement among several partners to acquire a series of properties, divide these into building lots and resell them at a profit. Because the partners were purchasing several adjoining lots, they purchased these in a sort of “checker board” arrangement putting properties in their names, in the names of their spouses or in joint ownership.

[8] According to the testimony of one of the partners, Giuseppe Marchese, the property was one of five properties acquired by him and three other partners, the defendant Joe, Raffaele Morano and Domenic Scroll. Four of the properties (the “Block D properties”) were adjoining, and these were registered in each of the names of the defendants, Gregorina and Joe, and in the names of Raffaele “to uses” and Mariaella Morano. The property which was not adjoining to the others was, as set out above, registered in the name of the defendant Joe “to uses.” The sale of the Block D properties generated sufficient monies to cover the full purchase price of the five properties. Therefore the remaining property held by Joe for the four partners was the “profit” of the four partners.

[9] According to Giuseppe Marchese, sometime later Joe bought out the interest in the property owned by the three other partners paying $3,000 to each of them. No transfer was necessary since the property was already in Joe's name.

[10] In August 1994 the property was transferred from Joe "to uses" to Gregorina for nominal consideration. The land transfer tax affidavit stated that the consideration was $2.00 and that Gregorina "has been the sole beneficial owner during the entire period the lands had been registered in the name of Joe."

C) THE MORTGAGE

[11] In October 1996, Alba registered a mortgage in the amount of $225,000 against the property. Alba testified that the consideration for the mortgage was a series of payments made by her to Gregorina during the period December 1993 to April 3, 1995. This series of advances had been made under an agreement entered into among the three defendants in December 1993 (the "loan agreement"). According to Alba the advances were made because her mother needed the money.

[12] There was a series of thirteen cheques totalling $258,500 entered into evidence. The defendants claimed the cheques were advances made pursuant to the loan agreement. Although the cheques were all drawn on Alba's account, Joe signed every cheque but one. The three payees of the cheques were Alessandro Holding Ltd., Joe Alessandro, and Joe and Gregorina Alessandro jointly. Little is known of the source and use of these funds as the bank statements were not entered into evidence. Alba testified that by the time she reached her early twenties, she had made hundreds of thousands of dollars trading in penny stocks. Again, no documentation was provided in support of this. It also appeared from Joe's testimony that he was a member of the Board or may have played some role in one or more of the companies, the stock of which Alba traded and profited from.

[13] Pursuant to the terms of the loan agreement, the advances of $258,500 would have become due in April 1997. It appears that there was no repayment of these sums.

[14] The mortgage was registered in October 1996, and full payment was due one year later. During the first year of the mortgage, Gregorina paid interest. However, on October 1, 1997, when the balance became due, payments stopped, and the mortgage went into default.

D) CHRONOLOGY

[15] The plaintiffs suggest that much can be inferred from the timing of various events. They have put forward a chronology setting out the dates of various key events. I agree that the timing is important and therefore will set out some of the key dates and events in this judgment. They are as follows:

September 26, 1972	Purchase of the subject property by Joe "to uses"
February 1, 1988	Joe purchases the lumber business from Cesidio and Elisa for $400,000; $50,000 payable in cash and the balance of $350,000 by promissory note
February 11, 1993	Demand for payment by the plaintiffs of the $350,000 note
December 3, 1993	Loan agreement among Alba, Joe and Gregorina pursuant to which Alba agrees to advance sums to Joe and Gregorina in the future. The agreement includes a recital that Joe holds the property in trust for Gregorina
December 6, 1993	First advance made under the loan agreement. It is a $5,000 cheque to Alessandro Holdings Ltd.
June 7, 1994	Statement of Claim issued by Cesidio and Elisa to obtain repayment of the $350,000 debt
August 30, 1994	Transfer of the property from Joe to Gregorina for $2
April 3, 1996	Judgment of Justice Cameron in the debt action granting judgment in the amount of $413,768.33, plus post-judgment interest at 10%. Included in the reasons for Justice Cameron is the statement that alleged oral agreements put forward by Joe did not occur and that Justice Cameron did not believe Joe.
July 3, 1996	Examination in aid of execution of Joe
October 4, 1996	Execution of charge on the property by Gregorina and Joe in favour of their daughter Alba
November 14, 1996	Statement of claim in the present action is issued.

III. ISSUES

[16] The issues in this case are as follows:

(a) was the transfer from Joe to Gregorio a fraudulent conveyance?

(b) was the mortgage from Gregorina to Alba a fraudulent conveyance?

(c) Did the plaintiffs and defendants settle the claim before the trial?

IV. THE LAW

A) STATUTORY FRAMEWORK

[17] The plaintiffs rely principally on two statutes, the *Fraudulent Conveyances Act* R.S.O. 1990, c.F-29 and the *Assignments and Preferences Act*, R.S.O. 1990, c.A-33.

[18] The relevant portions of the *Fraudulent Conveyances Act* are as follows:

> **2.** Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns. R.S.O. 1990, c. F.29, s. 2.
>
> **3.** Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section. R.S.O. 1990, c. F.29, s. 3.

[19] The relevant portions of the *Assignments and Preferences Act* are as follows:

> Nullity of gifts, transfers, etc., made with intent to defeat or prejudice creditors
>
> **4.-(1)** Subject to section 5, every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects, or of bills, bonds, notes or securities, or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made by a person when insolvent or unable to pay the person's debts in full or when the person knows that he, she or it is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice creditors, or any one or more of

them, is void as against the creditor or creditors injured, delayed or prejudiced. R.S.O. 1990, c. A.33, s. 4 (1).

(2) Subject to section 5, every such gift, conveyance, assignment or transfer, delivery over or payment made by a person being at the time in insolvent circumstances, or unable to pay his, her or its debts in full, or knowing himself, herself or itself to be on the eve of insolvency, to or for a creditor with the intent to give such creditor an unjust preference over other creditors or over any one or more of them is void as against the creditor or creditors injured, delayed, prejudiced or postponed.

(3) Subject to section 5, if such a transaction with or for a creditor has the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them, it shall, in and with respect to any action or proceeding that, within sixty days thereafter, is brought, had or taken to impeach or set aside such transaction, be presumed, in the absence of evidence to the contrary, to have been made with the intent mentioned in subsection (2), and to be an unjust preference within the meaning of this Act whether it be made voluntarily or under pressure.

Assignments for benefit of creditors and good faith sales, etc., protected

5.(1) Nothing in section 4 applies to an assignment made to the sheriff for the area in which the debtor resides or carries on business or, with the consent of a majority of the creditors having claims of $100 and upwards computed according to section 24, to another assignee resident in Ontario, for the purpose of paying rateably and proportionately and without preference or priority all the creditors of the debtor their just debts, nor to any sale or payment made in good faith in the ordinary course of trade or calling to an innocent purchaser or person, nor to any payment of money to a creditor, nor to any conveyance, assignment, transfer or delivery over of any goods or property of any kind, that is made in good faith in consideration of a present actual payment in money, or by way of security for a present actual advance of money, or that is made in consideration of a present actual sale or delivery of goods or other property where the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration therefor. R.S.O. 1990, c. A.33, s. 5 (1).

B) PRESUMPTION OF FRAUD

[20] In this type of case it is unusual to find direct proof of intent to defeat, hinder or delay creditors. It is more common to find evidence of suspicious facts or circumstances from which the court infers a fraudulent intent.

[21] These suspicious facts or circumstances are sometimes referred to as the "badges of fraud." These badges of fraud are evidentiary indicators of fraudulent intent and their presence can form the *prima facie* case needed to raise a presumption of fraud. These badges of fraud can be traced back to *Twyne*'s case (1602), 3 Co. Rep. 80 and are elaborated upon in *Prodigy Graphics Group Inc. v. Fitz-Andrews*, [2000] 0.J. No. 1203 (S.C.J.).

[22] The presence of one or more of the badges of fraud raises the presumption of fraud. Once there is a presumption, the burden of explaining the circumstantial evidence of fraudulent intent falls on the parties to the conveyance. The persuasive burden of proof stays with the plaintiff; it is only the evidentiary burden that shifts to the defendants.

[23] In cases of non arm's length transactions, independent corroborative evidence is strongly recommended but not required if the defendants' evidence is found to be credible. In *Koop v. Smith* (1915), 51 S.C.R. 554, Duff J. discussed the need for corroborative evidence in a case involving a transaction between two near relatives for no consideration. Duff J., at p.559 stated as follows:

> I think the true rule is that suspicious circumstances coupled with relationship make a case of *res ipsa loquitur* which the tribunal of fact may and will generally treat as a sufficient *prima facie* case, but that it is not strictly in law bound to do so; and that the question of the necessity of corroboration is strictly a question of fact. Having examined the evidence carefully I am satisfied that the learned trial judge was entitled to take the course he did take and not only that the evidence, as I read it in the record, casts the burden of explanation upon the respondent, but that the testimony given by her brother ought not in the circumstances to be accepted as establishing either the actual existence of the debt or of the *bona fides* of the transaction.

[24] Another useful case is *Petrone v. Jones* (1995), 33 C.B.R. (3d) 17 (O.C.G.D.). That case supports the proposition that where, as in the present case, the transferor is transferring the only asset he has remaining with which to pay his debts, there is a presumption of an intent to defeat creditors. Wright J., at p.20, stated the proposition as follows:

> In the absence of any direct proof of intention, if a person owing a debt makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid then, since it is the necessary consequence of the settlement that some creditors must remain unpaid, it is the duty of the judge to direct a jury that they must infer the intent of the settlor to have been to defeat or delay his creditors. (*Sun Life Assurance Co. v. Elliott* (1900), 31 S.C.R. 91.)
>
> Even if we consider the direct evidence that the defendant had no intention of defeating, hindering, *et cetera* the claims of the plaintiff, can this evidence remain standing in the face of the undoubted evidence that for the past year the defendant has in fact acted in every way to defeat, hinder or delay the plaintiff's claim?
>
> Even if the defendant had no intention, at the time of the conveyance, of defeating, hindering or delaying the plaintiff's claim, surely his actions since that date, the defence of the claim on the promissory note, the defence of this action, prevent him from raising that lack of specific intent as a defence.
>
> Further: even if the plaintiff did not intend to defeat, hinder or delay this creditor but effected the transfer with a view to defeating, hindering or delaying potential future creditors his defence would still fail.

V. ANALYSIS

[25] The plaintiffs' position is that the many suspicious circumstances and badges of fraud surrounding the transfer of the property by Joe to Gregorina and the mortgage by Gregorina to Alba raise the presumption of fraud which has not been rebutted. This leads to the inevitable conclusion that the mortgage and the transfer of the property should both be set aside pursuant to the *Fraudulent Conveyances Act.*

A) ASSIGNMENTS AND PREFERENCES ACT

[26] The plaintiffs have also relied on the *Assignments and Preferences Act* as a basis to set aside the mortgage. For the Act to apply, the transferor (or mortgagor) must be insolvent. It may well be that Joe was insolvent at the time that the mortgage was placed on the property, but the mortgage was granted by Gregorina. No evidence was led suggesting that Gregorina was insolvent. Even though Joe, as spouse, consented to the transaction, I do not believe that this would bring the *Assignment and Preferences Act* into play.

B) REQUIREMENTS TO PROVE FRAUDULENT CONVEYANCE

[27] The plaintiffs need to show that both the transfer to Gregorina and the subsequent mortgage to Alba were both part of a scheme to defeat, hinder, delay or defraud the plaintiffs contrary to the *Fraudulent Conveyances Act.*

[28] If I find that the conveyances were made with intent to defeat, hinder, delay or defraud creditors it would still not be void if the defendants could establish that the transactions were made for good consideration, were *bona fide* and the transferee or mortgagee was a person not having, at the time of the transaction, notice or knowledge of the intent to defraud. The onus to show this, however, is on the defendants. (*Bank of Montreal v. Jory*, [1981] B.C.J. No. 1014 (BCSC)).

C) TAKING TITLE "TO USES"

[29] The taking of title "to uses" was the subject of much argument. The defendants maintain this has the same effect as taking title "in trust." The plaintiffs maintain that it is simply a form of title that was used at that time to avoid the obligations flowing from dower. While both positions may be sustainable, the real determinant is the intention of the parties. Therefore, I see no need to deal with the *Statute of Uses* R.S.O. 1897, c.331 and its application to the present case.

D) THE DEFENDANTS' CASE

[30] The defendants admit that the transfer from Joe to Gregorina was not made for consideration. They take the position that the transfer was simply putting the property into Gregorina's name on the basis that, since the mid-70s, it had been held by Joe on behalf of Gregorina. They point to the fact that title had been taken by Joe "to uses" as evidence of this. If accepted, this is a complete answer to the plaintiffs' claim.

[31] If the court sets aside the transfer to Gregorina as a fraudulent conveyance, the defendants take the position that the mortgage on the property is valid and enforceable. It would remain as a charge on the property and take priority over the plaintiffs' claims.

[32] Finally, the defendants take the position that the action has been settled and that, as a result, the claim should be dismissed.

E) THE EVIDENCE

[33] The events surrounding this action date back, in some cases thirty years. As a result, some allowance must be made for faulty memories and for the difficulty in proving certain facts. Similarly, the real estate transactions carried out in the 1970s, including the acquisition of the property by Joe "to uses," involved many different lots contributing to confusion in the testimony and recollection of the parties.

[34] Even accounting for this, the evidence put forward by the defendants is far from satisfactory. I noted a number of significant inconsistencies. Some of the more significant inconsistencies surrounding key events were as follows:

1. Gregorina testified that the property had always been in her name. However, there was also evidence that:

   - according to land registry records the property was put into the name of Joe "to uses" in 1972 and not transferred to Gregorina till August 1994
   - Joe's discovery evidence was that the 1994 transfer of the property was made at Gregorina's request
   - Gregorina's discovery evidence was that the property was transferred to her because Joe had problems at the bank and did not want to lose the cottage.
   -

2. Alba testified that she gave her mother a mortgage because her mother needed the money. However, there was also evidence to the effect that:

   - the mortgage was placed on the property after all of the funds said to support the mortgage were advanced;
   - the advances purportedly supporting the mortgage were not made to Gregorina, they were made principally to Alessandro Holdings Ltd., a company apparently controlled by Joe, and to a lesser degree to Joe and Gregorina jointly.
   - Joe's discovery evidence was that some of the money was to pay his debts at the Royal Bank for which Gregorina was co-signer.
   - all but one of the cheques drawn on Alba's account were signed and likely initiated by Joe.
   - although Alba's testimony on this point is somewhat evasive, it is likely that Gregorina was giving Alba significant gifts, including cash gifts, in the same period that the alleged advances were made and remained outstanding;
   - Alba testified that it was her mother that gave the necessary instructions to the lawyer regarding the mortgage, but Gregorina's discovery evidence was that all of the paper work regarding the property was prepared or arranged by Alba;

3. Joe testified that he was never a partner in the venture that acquired the property and the Block D properties. He also testified that there were four partners: Gregorina, Giuseppe Marchese, Domenic Sgro and Raffaele Morano. Other evidence on the point, however, was as follows:

   - evidence of Gregorina that there were three partners: her, Morano and Marchese.
   - the evidence of Giuseppe Marchese was that there were four partners and that one of those four was Joe and not Gregorina;

- Joe gave previous evidence that there were five partners and that he had never held any property in trust. At trial he changed his testimony and said that these prior sworn statements were made in error.

[35] When I review the whole of the evidence and consider the reliability of the various witnesses I find Joe's testimony that he took the property in trust for four partners, including his wife, and that it was Gregorina who, as one of the four beneficiaries, paid out the other three partners thereby becoming the sole beneficial owner of the property to be self-serving and improbable. The evidence is more consistent with Joe being the partner who acquired the complete interest in the property sometime in the mid 70s, and I so find.

[36] The 1994 transfer to Gregorina was a non arm's length transaction for no consideration at a time when Joe was insolvent. It was an attempt to put the property out of the reach of his creditors.

[37] Support for this conclusion includes the following:

1. The clear and cogent evidence of Giuseppe Marchese. He testified that there were four partners, one of whom was Joe, and that after the Block D properties were sold, Joe bought out his partners by paying each of them $3,000. As a result, Joe became the sole owner of the property.

2. When one reviews all of the transactions shown in the various property registers for the area, it is clear that Joe and his partners bought and sold many properties. It does not seem reasonable that Joe would put this particular property into his name when he had no interest in it. Some properties were put in his name, in Gregorina's name and in their joint names and there seems little logic in his name appearing on title of this particular property if he had no interest in it.

3. The way Joe acted and parts of his testimony suggest that he was directly and intimately involved in these transactions and are more consistent with Joe being a partner than not.

4. Gregorina's discovery evidence read in at trial was that Joe transferred the property into her name because he had problems with the bank and did not want to lose the cottage.

5. The evidence of Cesidio and Sylvio Conte, Cesidio's son, was that Joe had advised them both that the property was " his cottage," that is, Joe's cottage.

[38] I turn now to Gregorina's evidence on the question of ownership. As set out previously, her testimony at trial was that the property had always been hers and in her name. She was visibly emotional about it, and it may well be that at the time of trial this was her honest belief. This belief, even if sincere, does not make it so. There were many transactions and payments

made in the early 70s. From her testimony, it was clear that Gregorina did not know which specific property would have been put into her name nor which property was put into the name of her husband.

[39] She testified repeatedly that the cottage lot she bought was on Ronald Avenue and, after being told that the property was located on James Street, said she must have forgotten that the lots she purchased were scattered on different streets. In fact she and Joe did buy a lot on Ronald Avenue as part of the many transactions in the area, and it is on this lot that they built their first cottage. The Ronald Avenue lot is not, however, the lot that is the subject of the present litigation. The Ronald Avenue cottage was later sold and a second cottage was built on the property located on James Street which, as stated earlier, was also acquired as part of these transactions but is in the name of Joe “to uses”.

[40] In my view, the property on which the current cottage is situated, the property that is the subject of this litigation, was not a property that Gregorina bought in the 1970s. Her testimony concerning her alleged purchase of the property is confused, inconsistent and changing. The evidence is more consistent with Joe having acquired that property.

[41] I now turn to the transactions themselves - the transfer and subsequent mortgaging of the property.

F) BADGES OF FRAUD

[42] From the chronology and facts we can identify a series of “badges of fraud” for both the transfer and mortgaging of the property.

1. Transfer from Joe to Gregorina

[43] Based on my earlier finding that Joe did not hold the property in trust and had in fact become the owner of the property in the 70s, the 1994 transaction should be viewed as a simple transfer rather than a transfer to the beneficiary under a trust arrangement. I will therefore turn to a review of some of the badges of fraud and how they relate to the transfer to Gregorina. They are as follows:

a) The transferor has few remaining assets after the transfer:
- the property transferred was the only asset owned by Joe and was done at a time when Joe was insolvent.

b) Transfer to a non arm’s length person :
- the transfer was non arm’s length from Joe to his wife.

c) There are actual or potential liabilities facing the transferor or he is about to enter upon a risky undertaking:

- the transfer was made very shortly after the plaintiffs issued the statement of claim to recover the $350,000 debt owed by Joe.

d) Grossly inadequate consideration:

- the consideration for the transfer from Joe to Gregorina was nominal.

e) The transferor remains in possession or occupation of the property for his own use after the transfer:

- Joe continued to use and benefit from the property after the transfer to Gregorina.

f) The deed contains a self-serving and unusual provision:

- the land transfer tax affidavit contained a self-serving statement being that the transferee had been the sole beneficial owner during the entire period the lands were registered in the name of Joe.

g) The transfer was effected with unusual haste:
- after holding for over 20 years the transfer is effected shortly after the plaintiffs issued the statement of claim.

[44] The presence of one or more of these badges of fraud raises a presumption of fraud. As set out earlier, while the persuasive burden of proof remains with the plaintiffs, the burden of explaining the circumstantial evidence of fraudulent intent now shifts to the defendants.

[45] In addition to these badges of fraud there is the evidence of Gregorina which was read in from the discovery transcript. Her evidence was that the transfer was done to take the property out of reach of the bank, one of Joe's creditors. Considering this evidence, not only was there little or no evidence to explain the circumstantial evidence of fraudulent intent and rebut the presumption of fraud, there was direct evidence supporting the fraudulent intent.

2. Mortgage Between Gregorina and Alba

[46] When we look for badges of fraud in a mortgage transaction that is alleged to be the second part of a two part scheme to defeat or delay creditors we need to adapt the principles somewhat to take into account the unique circumstances. Some of the badges of fraud and how they relate to the mortgage of the property are as follows:

a) Transfer to a non arm's length person:
- the transaction was non-arm's length, being between Gregorina and her daughter Alba.

b) The effect of the transaction is to delay and defeat creditors:

- there was a risk that the transfer would be set aside and the property seized by creditors, therefore, the mortgage served to protect against that.

c) Payment to a person not a party to the disposition:

- the consideration for the mortgage and the making of the mortgage were not contemporary. The consideration did not go to Gregorina but rather went principally to a company apparently controlled by Joe, and to Joe and Gregorina jointly.

d) The transfer was effected with unusual haste:

- the timing of the loan agreement which underlies the mortgage was shortly after the plaintiffs demanded payment from Joe; and:

- Gregorina and/or Alba registered the mortgage on the property shortly after the date of the judgment debtor examination of Joe.

e) The absence of a sound business or tax reason for the transaction:

- Alba and Gregorina were mother and daughter. Alba had received numerous gifts of money and goods from her mother. There was no business or tax reason for the mortgage and no reason why the mortgage should be placed on the cottage lot rather than Gregorina's home in Toronto.

f) The deed contains a self-serving and unusual provision:

- The loan agreement which deals with the purported loan from Alba to Gregorina and Joe contains a recital describing Joe as the holder in trust of the property, and Gregorina is the beneficial owner.

[47] The existence of one or more of these various badges of fraud serves to shift the burden of explaining the circumstantial evidence of fraudulent intent to the defendants.

[48] The defendants allege that the mortgage flowed from the loan agreement and that the mortgage was placed on the property as consideration for the advances made pursuant to the loan agreement.

[49] When one reviews the mortgage transaction in the context of all of the other facts and events surrounding the property it is, in my view, improbable that the mortgage was a regular financial arrangement between Alba and Gregorina. The mortgage and the loan agreement were part of the scheme to keep the property out of the reach of Joe's creditors.

[50] The advances under the loan agreement were to or for the benefit of Joe, and Gregorina did not have much involvement in it. The loan agreement was likely triggered by the plaintiffs' demand for payment from Joe or other creditors' demands. The mortgage was intended to protect the cottage from being seized by creditors and sold to provide money to repay Joe's debts.

[51] While Joe, Gregorina and Alba each tried to characterize these transactions as regular and proper, I found the evidence of each of them to be self-serving and unreliable. On the balance of probabilities, I am satisfied that the dominant purpose of both of the transactions was to prevent creditors from having access to the property for payment of Joe's debts. Gregorina and Alba were both well aware of Joe's financial situation. While Gregorina did not appear to me to be sophisticated enough to structure the various transactions, I find that she willingly cooperated with Alba and Joe who undertook to put the property out of the reach of Joe's creditors.

G) WAS THERE CONSIDERATION FOR THE MORTGAGE?

[52] If the defendants can establish that either of the transactions was made for good consideration and was a *bona fide* transaction to a person not having notice or knowledge of the intent to defraud, then the grantee may keep the property free of the taint of fraud.

[53] With respect to the transfer of the property from Joe to Gregorina, there was no valuable consideration, and I need go no further.

[54] With respect to the mortgage, the defendants tried to show that the mortgage was given for good and valuable consideration. The burden was on the defendants to establish consideration. The evidence presented by the defendants is not sufficient to discharge the burden of proof in this case. The production of various cheques, most of which were payable to one of the companies controlled by Joe was unconvincing as it was clear on the whole of the evidence that Joe was controlling the flow of funds. In the absence of the various bank accounts showing the source of the monies and the ultimate disposition of the funds, I am not satisfied that the advances were *bona fide* payments made by Alba to Gregorina in support of the mortgage. In addition, as stated earlier, I find that Alba was well aware of the reason for these various transactions, and it was no coincidence that she sought to place a mortgage on the property rather than on other assets in the name of Gregorina.

[55] I find, on a balance of probabilities, that the transfer to Gregorina and the mortgage were done with an intent to defeat, hinder, delay or defraud the creditors. The transfer and the mortgage were not made for consideration nor was the mortgage made in good faith to a person who, at the time of the placing of the mortgage, had no notice or knowledge of the intent to defeat, hinder, delay or defraud the creditor.

H) ALLEGED SETTLEMENT

[56] A full and final release, a consent and an agreement to settle the claim, all executed October 7, 1999, were entered into evidence.

[57] The defendants allege that the action was settled and that, as a result, the claim ought to be dismissed.

[58] In his videotaped evidence, Cesidio confirmed that he did in fact execute the documents but that this had been done on the understanding that the executed documents would be exchanged through intermediaries against payment in full of the debt. He testified that no payment was ever made. As a result, he never authorised the release of the settlement documents, and no settlement was effected.

[59] Joe testified that the settlement negotiations were conducted through an intermediary and that he had paid the settlement funds.

[60] It is not clear from Joe's evidence what amount was to be paid in settlement of the claim. Other than Joe's testimony, the only evidence of payment of any settlement funds was a certified cheque for $72,000 dated July 13, 1999, payable to J. Sansone, a friend of the families. There was no evidence provided regarding who cashed the cheque in October 1999 nor how the funds were used.

[61] The burden is on the defendants to establish that a settlement has been concluded. Given the evidence of Cesidio denying any payment, the proof that the settlement funds were actually paid is essential. Mr. Sansone was never called to testify concerning what the $72,000 payment to him was for nor has any other document been tendered showing that this, or any other sum, was ever paid to the plaintiffs.

[62] The defendants have not satisfied me on a balance of probabilities that a settlement was entered into which resolved all of the issues in this action. They offered no satisfactory explanation for the failure to call the payee of the cheque, J. Sansone. By reason of that failure I draw an inference adverse to the defendants that the testimony of that witness would not have assisted the defendants' case.

[63] In any event, the amount paid to Mr. Sansone was less than the amount allegedly agreed upon, and other than Joe's testimony, there is no evidence that these sums were paid. The defendants have not satisfied me that any consideration was paid for the alleged settlement. I therefore conclude that this defence must fail.

VI. CONCLUSION

[64] In the result, I grant judgment setting aside the transfer of the property described municipally as 1629 James Street, Tiny, Ontario, from Giuseppe Alessandro to Gregorina Alessandro, Instrument 01263935 dated August 31, 1994. I also grant judgment setting aside the charge granted on that same property by Gregorina Alessandro to Alba Alessandro, instrument 01325897 dated October 11, 1996.

[65] In view of my conclusions in respect of the plaintiffs' claims, I dismiss the defendants' counterclaim.

[66] If the parties are unable to agree on the issue of costs, the plaintiffs are to provide me with written submissions within 15 days of the release of these reasons, and the defendants are to respond in writing to these within 10 days thereafter.

RELEASED: _____

ROULEAU J.

COURT FILE NO.: 96-CU-114234
DATE: 20021210

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:

ELISA CONTE, Executrix and Trustee for CESIDIO CONTE and ELISA CONTE

Plaintiffs

- and -

JOE ALESSANDRO also known as GIUSEPPE ALESSANDRO, ALBA ALESSANDRO and A. Farber & Partners Inc., Trustee in bankruptcy of the estate of the said GIUSEPPE (aka) JOE ALESSANDRO

Defendants

REASONS FOR JUDGMENT

ROULEAU J.

RELEASED: December 10, 2002

TAB 7

2000 CarswellOnt 1178
Ontario Superior Court of Justice

Prodigy Graphics Group Inc. v. Fitz-Andrews

2000 CarswellOnt 1178, [2000] O.J. No. 1203, [2000] O.T.C. 237, 96 A.C.W.S. (3d) 177

Prodigy Graphics Group Inc. and Andy Patel, Plaintiffs and Kenneth Gregory Derry Fitz-Andrews, Gina Suzanna Fitz-Andrews and Ampito Investments Inc., Defendants

Kenneth Gregory Derry Fitz-Andrews, Gina Suzanna Fitz-Andrews and Ampito Investments Inc., Plaintiffs by Counterclaim and Prodigy Graphics Group Inc., Andy Patel, Prodigy Printing Services (1993) Inc. and Sulekha Patel, Defendants by Counterclaim

Cameron J.

Heard: January 24, 2000
Heard: January 25, 2000
Heard: January 26, 2000
Heard: January 27, 2000
Heard: January 28, 2000
Heard: January 31, 2000
Heard: February 1, 2000
Heard: February 2, 2000
Heard: February 3, 2000
Heard: February 4, 2000
Heard: February 7, 2000
Heard: February 8, 2000
Heard: February 9, 2000
Heard: February 10, 2000
Heard: February 11, 2000
Heard: February 14, 2000
Heard: March 16, 2000
Heard: March 17, 2000
Heard: March 20, 2000
Judgment: April 10, 2000
Docket: 94-CQ-58835

Counsel: *Messod Boussidan* and *James Diamond*, for Plaintiffs.
Kenneth Fitz-Andrews, for himself.

Subject: Contracts; Corporate and Commercial; Torts; Civil Practice and Procedure

Headnote

Torts --- Conversion — Elements of right of action — Wrongful act — Unauthorized disposition

Accountant provided consulting services to clients' corporation and clients over number of years — In 1992, clients wrote three cheques to company owned by accountant — Accountant applied cheques to account for consulting services allegedly provided — Account was addressed to clients personally, and was dated six days prior to accountant's purchase of company — Account was allegedly for "off-hours" work performed by accountant

in addition to his firm's work related to same transaction — Clients claimed purpose of cheques was to pay corporation's tax liability and that accountant produced receipts from Revenue Canada which they photocopied — Revenue Canada denied receiving amounts noted in receipts — Handwriting expert testified to high probability that handwriting on receipts was that of accountant — Client sued accountant for conversion and misappropriation of funds — Action allowed — Accountant produced only diary showing time spent, not detailed dockets, computer records or evidence from files to explain details of services provided — Account was inflated if not wholly without foundation and was never delivered to client prior to cheques being drawn — Cheques were not to pay account for services but to pay employee withholding tax liabilities — Accountant had no right to appropriate money and was liable to repay clients — Accountant also appropriated to himself cheques payable to clients' corporation, which he had not authority to appropriate — Accountant was liable to repay amount to clients' corporation — Accountant's wife, who owned shares in company, had no knowledge of accountant's appropriation of funds — It would be unjust to pierce corporate veil to make wife personally liable or make her accessory to breach of trust — No evidence existed that proceeds of clients' cheques could be traced to payment of any part of purchase price of house bought by accountant and his wife.

Fraud and misrepresentation --- Fraudulent conveyances — Fraudulent intent — General principles

Accountant was in dispute with clients over application of series of cheques to payment of account for services rendered — Accountant was also involved in litigation with former partners and landlord — Accountant and wife bought house in both names, subject to mortgage, and subsequently transferred title to wife's name exclusively — Application was brought by clients to have transaction set aside as fraudulent conveyance — Application granted — Intention of accountant was to be determined as of date of transfer being executed — Conveyance was made with intent to delay creditors — As number of badges of fraud were present, including fact accountant continued to live in house and had few other assets, presumption of intent was raised — Wife's lack of knowledge of accountant's intent was irrelevant.

Injunctions --- Procedure on application — Undertaking regarding damages — Inquiry or reference to enforce damages

Clients suing accountant for conversion and misappropriation of funds obtained interlocutory injunction freezing accountant's assets and certificate of pending litigation against his residence — Affidavits provided by clients failed to disclose clients' involvement in, and suggested accountant was responsible for, scheme to withhold taxes, which was initiated prior to accountant's retainer — Shortly before trial, accountant brought motions to set aside injunction and certificate of pending litigation — Both motions were dismissed on basis of imminent trial and failure to move forthwith — At trial, claim was brought by accountant for damages related to difficulties experienced borrowing money and maintaining bank accounts, as well as damage to reputation with banks and clients — Action dismissed — Clients' failed to make full and frank disclosure — Non-disclosure was material and might have effected outcome of motion, but accountant failed to provide evidence of his damages.

ACTION by clients against accountant for misappropriation and conversion of funds; COUNTER-CLAIM by accountant for damages related to interlocutory injunction freezing accountant's assets and certificate of pending litigation.

***Cameron J.*:**

1 The plaintiffs claim damages of $180,783.04 for fraud and conversion. The counterclaim for damages is based on inadequate disclosure in obtaining injunctive relief and the balance owing on accounts for professional services. Both cases turn on credibility and assessing alleged forgeries.

I. The Parties

1. The Patels and Prodigy

2 Andy Patel is the president, a director and 50% shareholder of Prodigy Graphics Group Inc., a 1995 amalgamation which includes Prodigy Industrial Printers Inc., later called Prodigy Printing Services (1993) Inc. (collectively "Prodigy"). Since 1975 Prodigy has operated a printing business in Mississauga. The business grew and expanded and by December 1992 had 23 employees. Sulekha Patel, Mr. Patel's wife, was and is a director and 50% shareholder of Prodigy. She worked about half of her time in Prodigy's office. Prodigy's accountant from 1986 to 1992 was a firm of chartered accountants in Brampton named Savage and Moles.

2. The Fitz-Andrews and Ampito

3 Kenneth Fitz-Andrews is a chartered accountant who had been with an international accounting firm in Trinidad and Tobago from the mid 1970s until he came to Canada in August 1989, followed shortly by his wife Gina Fitz-Andrews and their four children. They rented a home at 1224 Highgate Place in Mississauga. In October 1989, Mr. Fitz-Andrews was hired by Savage and Moles. Mr. Fitz-Andrews became one of two partners in the firm on May 1, 1990 and borrowed about $180,000 from Royal Bank to finance the purchase of his capital interest in the firm. His draw cheques were often paid in advance. The partnership agreement required the partners to devote their full time and attention to partnership affairs.

4 Gina Fitz-Andrews is the president, a director and sole shareholder of Ampito Investments Limited ("Ampito"). She is also the registered owner of the family home purchased on March 26, 1993, which she and Mr. Fitz-Andrews had leased since September 1989.

5 Gina Fitz-Andrews purchased the shares of Ampito, an Ontario corporation, on November 16, 1992 to operate a business of selling school uniforms similar to that operated by his sister in the United Kingdom. Gina Fitz-Andrews, Mr. Fitz-Andrews and his sister are the directors of Ampito.

II. Outline of the Relationship 1990-1994

6 Mr. Fitz-Andrews started providing consulting services on behalf of Savage and Moles to Prodigy and the Patels in early 1990. These services included work relating to the sale of Mr. Patel's minority interest in another company, the purchase of a Komeri press, the purchase of a larger building on Creekbank Road to house Prodigy's growing operations and consolidation of Prodigy's borrowings with The Royal Bank of Canada ("Royal Bank").

7 In February 1991, Mr. Fitz-Andrews became involved in Prodigy's negotiations of a contract for the purchase from Mitsubishi Litho Press Canada ("MLP") of three large new presses for $3 million and the financing of the purchase by Royal Bank. Mr. Fitz-Andrews testified that this involved him in much evening and weekend work in the preparation of business plans, financial projections and proposals on behalf of Prodigy. Savage and Moles rendered accounts for this work in September and December 1991 and October 1992.

8 Mr. Patel testified that he came to regard Mr. Fitz-Andrews as a "partner I didn't have".

9 In March 1992, Mr. Fitz-Andrews gave, and later withdrew, notice to terminate his partnership in Savage and Moles.

10 In April, September, October and November 1992, Prodigy paid to or for Mr. Fitz-Andrews' personal account at Royal Bank amounts of $10,000, $7,000, $7,000 and $1,500 respectively.

11 In September 1992, Mr. Fitz-Andrews started to withdraw from Savage and Moles and set up his own practice in temporary quarters. He formally registered with the Institute of Chartered Accountants of Ontario as a sole practitioner effective November 10, 1992.

12 In October 1992, Revenue Canada issued assessments against Prodigy for unremitted taxes withheld from employees in 1988 and 1989 plus penalty and interest. Mr. Fitz-Andrews delivered Prodigy's payment to Revenue Canada on

October 28, 1992. On November 13, 1992 Revenue Canada issued an assessment against Prodigy in respect of 1990 unremitted employee withholdings for $26,809.

13 On November 17, 1992, Mr. Patel and his wife wrote cheques from their personal accounts totalling $130,000 to Ampito, the shares of which Gina Fitz-Andrews had purchased the day before for $500 for the purpose of establishing a school uniform business.

14 The purpose of this payment is at the centre of this action.

15 In 1992, Mr. Fitz-Andrews and Carrol Meisner his partner in Savage and Moles were sued by a former landlord of the partnership. In December 1992, Mr. Fitz-Andrews commenced an action against Mr. Meisner arising out of the break-up of their partnership.

16 In March 1993, Mr. Fitz-Andrews moved his accounting practice from its initial temporary location to a nearby permanent office.

17 At about the same time Mr. and Mrs. Fitz-Andrews agreed to purchase the house they had been renting for the previous three years for $300,000 cash. The transaction closed on March 26 with a deed to Gina and Mr. Fitz-Andrews. On the same day Mr. Fitz-Andrews transferred his interest to his wife

18 In May 1993, Mr. Fitz-Andrews rendered an account to Prodigy of $29,000 for professional services to which Mr. Patel objected without supporting documentation.

19 In July 1993, Revenue Canada issued a Statement of Account showing unpaid amounts in respect of assessments for unremitted withholdings in 1990 and 1991 and an assessment for $2,700 in respect of 1992. In November 1993 and January 1994 further amounts were assessed respecting 1991.

20 In completing the audit of Prodigy and a related company Prodigy Graphics Inc., Mr. Fitz-Andrews submitted to Mr. Patel in November 1993 audit engagement letters for each of the companies. Two "original" copies were submitted in evidence. The letter from Mr. Fitz-Andrews' file signed by Mr. Patel authorized Mr. Fitz-Andrews to apply rebates received from Revenue Canada to his outstanding accounts. There was no such authorization in Prodigy's copy.

21 In early 1994, Mr. Fitz-Andrews wrote to Mr. Patel respecting his concern with his outstanding accounts, including the May 1993 account which remained unpaid.

22 On March 3, 1994, Mr. Fitz-Andrews wrote to Mr. Patel and Royal Bank withdrawing Prodigy's audited financial statements for the fiscal year ended July 31, 1993 because of Prodigy's failure to include a contingent liability for employee withholdings owing to Revenue Canada in respect of the calendar year 1992.

23 On the same day Mr. Fitz-Andrews wrote to Mr. Patel complaining of the non-payment of his outstanding accounts, explaining the work done and recording his upset at the request for supporting dockets "in view of previous transactions not requiring this". He concluded with a refusal to provide further services until his outstanding accounts were settled.

24 In May 1994, Mr. Fitz-Andrews remitted a statement of account to the Prodigy companies respecting accounts dating back to the disputed May 1993 account and showing payments received. The balance owing was $46,233, less amounts held in trust of $25,283.04, leaving a "net balance due" of $20,946.06. The accounts in trust included the proceeds of two cheques from Revenue Canada payable to Prodigy totalling $24,181.58 received by Mr. Fitz-Andrews in February 1994 and cashed by him.

25 In June of 1994 Mr. Patel, with his new accountant Joel Levitt, voluntarily disclosed to Revenue Canada Prodigy's failure to remit employee withholdings in the calendar year 1992. Prodigy was assessed for principal amounts owing in respect of 1992, $19,146 on July 27, 1994 and $38,679 on November 17, 1994. Additional amounts were assessed for 20% penalty and interest.

26 This action was commenced on November 29, 1994. On December 12, 1994 the plaintiffs filed affidavits in support of an *ex parte* motion resulting in a certificate of pending litigation against the home registered in Gina Fitz-Andrews' name and a *mareva* injunction freezing Mr. Fitz-Andrews' assets. The defendants filed responding material on December 21, 1994. On return of the motion the injunction was amended to release $10,000 to Mr. Fitz-Andrews, otherwise it was to continue pending deposit of security of $25,000 in cash and a letter of credit for $50,000. The motion was adjourned to allow for cross-examinations. The cross-examinations were not held until almost six years later in the autumn of 1999. On return of the motion the court continued the injunction and certificate of pending litigation until this trial.

27 There were numerous interlocutory proceedings arising out of the discovery process.

III. The Claims and Counterclaims

28 Mr. Patel has sued the defendants for damages of $130,000. Prodigy has sued the defendants for $25,500 and the defendant Mr. Fitz-Andrews for a further $24,181 based on fraud and conversion. The plaintiffs have sued Gina Fitz-Andrews to void a fraudulent conveyance to her and to make her personally liable as a director of Ampito for a fraud by Ampito.

29 Mr. Fitz-Andrews counterclaims against Andy and Sulekha Patel and Prodigy for outstanding fees of $46,233.10.

30 He also claims damages resulting from obtaining *ex parte* a certificate of pending litigation and an interim *mareva* injunction, and continuation thereof pending cross-examinations. Mr. Fitz-Andrews claims the affidavits used to obtain the certificate of pending litigation and *mareva* injunction were materially misleading and lacked material disclosure respecting Mr. Patel's participation in the tax evasion scheme which he blamed on Mr. Fitz-Andrews.

31 Mr. Fitz-Andrews' claims for damages based on allegations of libel by statements contained in the statement of claim and in the affidavits used to obtain the certificate of pending litigation and interim *mareva* injunction must be dismissed. Statements in pleadings and affidavits in court proceedings are absolutely privileged: *Dooley v. C.N. Weber Ltd.* (1994), 19 O.R. (3d) 779 (Ont. Gen. Div.). In addition, the libel charged has not been pleaded with sufficient particularity.

32 The claims against Sulekha Patel based on an alleged duty to disclose known shortcomings in the affidavits supporting the motions for interlocutory relief must be dismissed because she was not a party at the time of swearing the affidavits. She can only be liable if her conduct was such as to make her liable in her capacity as a director of Prodigy.

IV. The Issues

33 The five issues in this case turn on credibility.

1. The $130,000 Paid to Ampito

34 Mr. Patel alleges that Mr. Fitz-Andrews defrauded him of $130,000 by misappropriating the proceeds of Mr. Patel's personal cheques paid to Ampito, to pay off an account of Ampito of $130,500 for consulting services allegedly rendered by Mr. Fitz-Andrews in 1991 and 1992. Mr. Patel alleges the purpose of the cheques was to pay Prodigy's tax liabilities to Revenue Canada.

35 Mr. Patel alleges the Ampito account is fabricated. He denies receiving the account and further denies that such work was done. Mr. Patel alleges that Mr. Fitz-Andrews (a) presented to him false receipts of Revenue Canada to hide the misappropriation, (b) allowed him to make a copy of the receipts, and (c) received back from him the original receipts.

36 Mr. Fitz-Andrews asserts that his account is *bona fide* and based on time spent on evenings and weekends on Prodigy's affairs noted in his calendar diaries. Mr. Fitz-Andrews says he delivered the Ampito account to Mr. Patel. Mr. Fitz-Andrews asserts the payment of the account is in accordance with a private oral agreement between the parties respecting his services performed for Prodigy. Mr. Patel denies any such agreement.

37 Mr. Fitz-Andrews denies he obtained the Revenue Canada receipts or showed them to the Patels. He asserts that the receipts were fabricated by Mr. Patel. A handwriting expert has opined that there is a "high probability" that the handwriting on the receipts is that of Mr. Fitz-Andrews.

2. Cheques for $25,500

38 In 1992 Prodigy wrote four cheques totalling $25,500 payable to Royal Bank, which were given to Mr. Fitz-Andrews, as follows: April 10 - $10,000; September 1 - $7,000; October 1 - $7,000 and November 1 - $1,500. These were deposited to Mr. Fitz-Andrews' account.

39 Mr. Patel says these were payments for setting up a payroll computer programme and for deferral of payment of taxes withheld from employees for the purpose of making Prodigy's profits look greater so Royal Bank would fulfill its agreement to lend part of the purchase price for new printing presses payable to MLP Canada eleven months after their delivery in January, 1992. Mr. Fitz-Andrews denies participating in any such arrangement and claims the payments were for legitimate consulting services. Mr. Patel says Mr. Fitz-Andrews promised to send him an account for these payments but did not do so.

3. Mr. Fitz-Andrews' Accounts $46,233

40 Mr. Fitz-Andrews rendered accounts to the Prodigy group of companies for work done in late 1992, 1993 and early 1994 which Mr. Patel disputes. Mr. Fitz-Andrews appropriated to himself in February 1994 two Revenue Canada refund cheques payable to Prodigy totalling $24,181 alleging that he was authorized to do so by reason of an authorization on page 2 of Prodigy's engagement letter dated November 22, 1993 signed by Mr. Patel which retained Mr. Fitz-Andrews to audit the financial statements for the year ended July 31, 1993.

41 Mr. Patel alleges that Mr. Fitz-Andrews substituted the page 2 containing an authorization for the page which he says he signed which contained no such authorization. Mr. Fitz-Andrews alleges that Mr. Patel fraudulently substituted the page 2 in the letter that Mr. Patel produced for the page containing the authorization which Mr. Fitz-Andrews produced.

4. Fraudulent Conveyance

42 Was the conveyance of the family home by Mr. Fitz-Andrews to his wife made with the intent to defeat or hinder his creditors as contemplated in s.2 of the *Fraudulent Conveyances Act*?

5. Claim on Undertaking to Pay damages

43 Mr. Fitz-Andrews alleges that the Patels and Prodigy gave materially misleading evidence in the affidavits used to obtain and continue the certificate of pending litigation and the interlocutory *mareva* injunction freezing the Fitz-Andrews' house and other assets following commencement of this action in November 1994. Mr. Fitz-Andrews alleges it wrongfully accused him of fraudulent conduct and failed to disclose Mr. Patel's involvement in tax evasion.

V. Burden of Proof

44 In civil cases, where there is an allegation of criminal or morally blameworthy conduct, the civil burden of proof, namely the balance or preponderance of probabilities, applies. In determining whether it is satisfied, the court may consider the cogency of the evidence and scrutinize the evidence with greater care, bearing in mind the consequences of its decision: J. Sopinka, S.N. Lederman and A.W. Bryant, *The Law of Evidence in Canada*, 2 rd ed. (Toronto: Butterworths, 1998) at p. 156-158 citing *Continental Insurance Co. v. Dalton Cartage Ltd.*, [1982] 1 S.C.R. 164, 131 D.L.R. (3d) 559 (S.C.C.), per Laskin, C.J.C., *Boykowych v. Boykowych*, [1955] S.C.R. 151, [1955] 2 D.L.R. 81 (S.C.C.); and *Smith v. Smith*, [1952] 2 S.C.R. 312, [1952] 3 D.L.R. 449 (S.C.C.) per Cartwright J. In this case Mr. Fitz-Andrews' professional licence is clearly at risk.

VI. Assessing Credibility

45 A most difficult task for a finder of fact is to determine the truth. The process is more difficult if both sides may have a motive to offer less than the whole truth or if the events occurred so long ago as to permit human nature and time to work on the recollection of a witness. I call this unconsciously selective hindsight through rose coloured glasses.

46 I have examined and assessed the evidence of each witness and the exhibits presented at trial using, where appropriate, the following traditional criteria:

1) Lack of testimonial qualification

2) Demeanor of Witness: apparent honesty, forthrightness, openness, spontaneity, firm memory, accuracy, evasiveness

3) Bias/Interest in the Outcome (if a party, motive)

4) Relationship/Hostility to a party

5) Inherent probability in the circumstances i.e. in the context of the other evidence does it have an "air of reality"

6) Internal consistency i.e. with other parts of this witness' evidence at trial and on prior occasions.

7) External consistency i.e. with other credible witnesses and documents

8) Factors applicable to written evidence:

(a) Presence or absence of details supporting conclusory assertions

(b) Artful drafting which shields equivocation

(c) Use of language in an affidavit which is inappropriate to the particular witness

(d) Indications that the deponent has not read the affidavit

(e) Affidavits which lack the best evidence available

(f) Lack of precision and factual errors

(g) Omission of significant facts which should be addressed

(h) Disguised hearsay

See for example, Alan W. Mewett and Peter J. Sankoff, *Witnesses*, chapter 11, (Toronto: Carswell, Looseleaf).

47 An adverse inference may be drawn against a party for failure, without adequate explanation, to call a relevant witness or submit relevant evidence which would be expected to support the party's case against the other party. The court may infer that the witness was not called out of a fear that he would not have supported that party's case. The inference may be drawn notwithstanding the witnesses' availability to be subpoenaed by either party in the case: *Goldstein v. Davison* (1994), 39 R.P.R. (2d) 61 (Ont. Gen. Div.) per Ground J., citing *Murray v. Saskatoon (City) (No. 2)* (1951), [1952] 2 D.L.R. 499 (Sask. C.A.) and *Claiborne Industries Ltd. v. National Bank of Canada* (1989), 69 O.R. (2d) 65 (Ont. C.A.). See also *Medalist Holdings Ltd. v. General Electric Capital Equipment Finance Inc.* (1997), 10 R.P.R. (3d) 111 (Ont. Gen. Div.) per Greer J. and *Zelmer v. Victor Projects Ltd.* (October 31, 1995), Doc. Kelowna 16665 (B.C. S.C.) per Lowry J.

48 A proper application of these principles requires that the finder of fact be provided with, or create, a detailed overall chronology of events relevant to the facts in issue in the pleadings and to the facts on collateral issues such as credibility of the evidence. The evidence on each of these issues must also be analyzed in the context of the chronology of the facts relevant to each of the issues. I have attempted to do this.

49 I do not intend to record in this judgment all the evidence offered during 16 days of trial or referred to in three days of argument. The evidence on the numerous collateral issues includes time diaries for three years, purchase, loan and lease agreements on which Mr. Fitz-Andrews worked, accounts rendered to Prodigy or the Patels for accounting and consulting services, inconsistent computer generated payroll records, financial statements, T4 summary reports to Revenue Canada, Revenue Canada notices of assessments for 1988, 1989, 1990, 1991 and 1992 and statements of account over the period September 1992 to November 1994 respecting Prodigy, photocopy of receipts of payments ostensibly issued by Revenue Canada, documents relating to the purchase and mortgages of the Fitz-Andrews' home, the Savage and Moles partnership agreement, a summary of Mr. Fitz-Andrews' docketing, correspondence respecting his withdrawal from his partnership or its cessation, motion records on the application for an interim *mareva* injunction and certificate of pending litigation and the return of the motion for interlocutory relief, two versions of an audit engagement letter, Prodigy cheques payable to Mr. Fitz-Andrews' account at Royal Bank and the purchase or establishment and organization of various companies.

50 In assessing the evidence of Sulekha Patel, I found her to be well prepared on the two issues for which she was called to testify but, considering her share ownership and long involvement with Prodigy, totally unresponsive on cross-examination and on discovery with too many replies such as "I don't remember" to harmless questions on which she should have known the answers. Her lawyer interrupted so frequently in the discovery as to make me wonder what she was hiding. I readily acknowledge that most of his other objections respecting relevance, harassment and repetition by Mr. Fitz-Andrews were quite proper. This assessment of Mrs. Patel raises a question as to the reliability of Mr. Patel's evidence beyond the scrutiny accorded an interested and otherwise open and forthright party.

VII. The Payroll Scheme and Revenue Canada Assessments

51 Mr. Patel testified that Mr. Fitz-Andrews became involved in setting up a computer payroll program and in calculating pay and deductions in early 1992 after Prodigy's part-time payroll clerk Paul Frimpong disappeared, allegedly taking with him most of Prodigy's payroll records.

52 Mr. Fitz-Andrews denies becoming involved in setting up such a program or in calculating Prodigy's payroll and deductions. Mr. Fitz-Andrews testified that as accountant for Prodigy, he only prepared the T-4 slips and T-4 summary following the calendar year end and reviewed the internal monthly statements before they were forwarded to Prodigy's bankers.

53 Mr. Patel alleges that Mr. Fitz-Andrews was party with him in a scheme to mislead the Royal Bank into thinking Prodigy was more profitable than it really was by giving it false statements to ensure advance of a loan. Did Mr. Fitz-Andrews withhold from Prodigy's monthly statements provided to its bankers accrued liabilities for employee remittances to Revenue Canada by showing these employees as employees of Ampito and deferring the monthly payments of the withholdings to Revenue Canada? The evidence on this collateral issue is conflicting and inconclusive. Mr. Patel says the reason for Prodigy paying $25,500 to Mr. Fitz-Andrews' account at Royal Bank was for his part in developing this scheme and as a bonus for helping Prodigy achieve a profit in the fiscal year ended July 1992. Mr. Fitz-Andrews denies this allegation and asserts the payments were for professional services rendered. Mr. Patel denies liability because it has never been specifically billed.

54 In October 1992, Prodigy received assessments for employee deductions for income tax, unemployment insurance and Canada Pension Plan which had not been remitted in respect of the calendar years 1988 and 1989 totalling $24,510.03, including penalties and interest. Prodigy gave Mr. Fitz-Andrews a cheque which he delivered to Revenue Canada.

55 Within a few days after November 13, 1992 Prodigy received an assessment for unpaid employee withholdings in 1990 totalling $26,089.85 including penalty and interest. Mr. Fitz-Andrews said that following discussions with Revenue Canada he told Mr. Patel that Prodigy's file was being reviewed. Prodigy made payments often in the subsequent months.

56 In July 1993 Prodigy received a statement of account from Revenue Canada showing assessments and payments as follows:

	Total Assessed	Total Owing (Including Penalty and Interest
1990	80,717	21,394
1991	79,652	62,130
1992	2,753	3,152

57 Prodigy continued to make payments on account. In November 1993 and January 1994, a further $14,506 was assessed in respect of employee withholdings for 1991 and on February 25, 1994 a further $11,890 plus interest and taxes as assessed in respect of 1990.

58 On July 27, 1994 and November 17, 1994, following self reporting on the advice of its new accountant Joel Levitt, Prodigy was assessed in respect of 1992 a further $19,146 and $38,679 which, with penalties and interest, totalled $71,884.

59 The total withholdings assessed for 1992 were $60,578.88 plus 10% penalty plus interest from the 15th day of the month following deduction from the employees' pay.

60 Prodigy paid all amounts assessed by Revenue Canada in respect of unpaid payroll deductions by 1995.

61 I am satisfied from the Revenue Canada assessments in October and November 1992 and in 1993 that Mr. Patel caused Prodigy to withhold reporting and payment of employee payroll deductions during the period 1988 to 1993. Contrary to Mr. Patel's allegations, Mr. Fitz-Andrews had nothing to do with these activities until 1992, if at all, following the disappearance of Prodigy's part-time bookkeeper, Paul Frimpong, in late 1991.

XIII. Purpose of the Three Personal Cheques: $130,000

62 The central issue in this case is the purpose for which Mr. Patel drew three personal cheques in his office in the presence of Sulekha Patel and Mr. Fitz-Andrews. One cheque was drawn by Mr. Patel on a joint account with his wife and two were drawn on Mr. Patel's personal account. The cheques were payable to Ampito in the amounts of $30,000 dated November 17, 1992, $50,000 dated November 27, 1992 and $50,000 dated December 4, 1992. The latter cheques were said to be post dated to coincide with the maturity dates of some personally held guaranteed income certificates. The cheques were handed to Mr. Fitz-Andrews in the presence of both Patels who testified that Mr. Fitz-Andrews said that the proceeds would be paid to Revenue Canada. Mr. Patel testified that the cheques were for the withholding taxes payable on account of Prodigy employees for 1992 which he and Mr. Fitz-Andrews agreed would be transferred to Ampito's payroll, without accruing the liability on Prodigy's books, to reduce the costs and increase the revenues of Prodigy so as not to default on the loan agreement with Royal Bank. Mr. Patel further testified that the amount of the cheques was recommended by Mr. Fitz-Andrews.

63 Mr. Fitz-Andrews denies there was any such agreement between them to transfer Prodigy employees to Ampito or that the proceeds of the cheques were to be used to pay Revenue Canada. Mr. Fitz-Andrews says the purpose of the cheques was to pay the account of Ampito dated November 10, 1992 for $130,000 for consulting services during evenings and week-ends for Prodigy and the Patels noted in his diaries during 1991 and 1992. Mr. Fitz-Andrews said this work was in accordance with an oral agreement he had with Mr. Patel that such services would be billed by Mr. Fitz-Andrews to Mr. Patel.

64 I heard much evidence concerning Mr. Fitz-Andrews' participation in the negotiations and the agreed terms for the purchase of three printing presses and financing of the purchase through a loan agreement with Royal Bank in 1991 and early 1992.

1. The Ampito Account

65 Mr. Fitz-Andrews says the account was delivered to Mr. Patel on November 11, 1992. The account is headed "Ampito Investments Ltd., 1 Regan Rd., Unit 20, Brampton, Ontario", is addressed to "Narendra and Sulekha Patel" at their home and is dated November 10, 1992. The body of the account reads as follows:

> As per private agreement:
>
> > For special consulting services and preparation of special feasibility studies, cash flow projections, financial projections for 5 year period re: Prodigy Industrial Printers Inc.
> >
> > For several consultations and meetings with M.L.P. re: the negotiations and eventual purchase of three (3) printing presses valued at $4,500,000.00. Consultation commenced - one-year period - for negotiation with Royal Bank of Canada and the finalization of financing of $3,090,000.00 to purchase three (3) printing presses from Royal Bank of Canada.
> >
> > For drafting and preparation of buy-back agreement re: Royal Bank and M.L.P. to secure equipment loan.
> >
> > For negotiating three (3) year interest free loan for Prodigy Industrial Printers Inc. in the sum of $370,000.00 from M.L.P. (Japan).
> >
> > To visits to several manufacturers in U.S.A. to review equipment and to meet with company officials.
> >
> > To negotiations and finalization of purchase of two industrial condominium units from Ravpan Investments Limited - Purchase Price $240,000.00.
> >
> > To negotiations and finalization of 1 residential condominium unit at Webb Drive, Mississauga.
> >
> > To several meetings with your solicitors re: the above matters.
> >
> > TOTAL STAFF HOURS = 645 HOURS
>
> | | |
> |---|---|
> | TOTAL MY FEE | $145,000.00 |
> | COURTESY DISCOUNT | 14,500.00 |
> | NET FEE | $130,500.00 |

66 Mr. Patel denies seeing this account before the commencement of this litigation. He alleges it was prepared after the commencement of this litigation to justify appropriation of the $130,000. The account appeared in the defendants' responding materials and motion record filed December 21, 1994 following receipt on December 16, 1994 of the material used on the *ex parte* injunction motion on December 12, 1994. The responding material included vehement denials of the allegations in the plaintiffs' materials of fraud and participation in the scheme to put Prodigy employees in Ampito.

67 The account is addressed to the individuals and not to Prodigy. It is addressed to the individuals in the names used on two of the cheques and not to "Andy" Patel as he was normally addressed by Mr. Fitz-Andrews.

68 Why would the Patels want the account personally when they could not deduct it as an expense but Prodigy could?

69 The account is dated six days before Mr. Fitz-Andrews purchased the shares of Ampito for $500. When asked why he billed in the name of a company he did not yet own, Mr. Fitz-Andrews said he was not comfortable billing in his own name because of his uncertainty respecting the break-up of his partnership, this in spite of having letterhead in the name of his accounting practice at the time.

70 He later said he had a one page written agreement to purchase Ampito which was replaced by the formal share purchase agreement of November 16, 1992, the date of closing. No such preliminary agreement was produced. Further, Mr. Fitz-Andrews said he needed the money to start his new practice which was registered with Institute of Chartered Accountants of Ontario in November 10, 1992, and needed a corporation to bill the account for tax postponement purposes. He said he could not wait until his lawyers effected his instructions to incorporate his consulting firm, Fitz-Andrews and Associates Inc. ("Associates"). That company was incorporated December 4, 1992. Mr. Fitz-Andrews testified that Ampito transferred its net assets of $81,462 to Associates and Associates declared it as income in its fiscal year ending January 31, 1994.

71 The invoice used a typed address, different from the print font on the rest of the document, of "1 Regan Rd." On November 10, 1992, Mr. Fitz-Andrews' new accounting practice was located at 18 Regan Rd., Suites 28 and 29. He did not move to 1 Regan Rd. until February or March 1993. In January and February 1993, he was using stationery for his accounts and fax transmittal sheets on which were printed the address of 18 Regan Rd. However, the Toronto Dominion Bank monthly statements for Ampito for the periods ending November 30, and December 31, 1992 showing the deposits of the Patel's cheques on November 18 and 27, and December 4, 1992 show Ampito's address as 1 Regan Road. During that period Ampito's address was not on its cheques. The *Corporations Information Act* notice recording the purchase of Ampito was not filed until June 1993. It showed the Fitz-Andrews' home address as the principal place of business and a lawyer's office as the head office.

72 Ampito's income tax returns show no income for the taxation year ended April 30, 1993. Mr. Fitz-Andrews testified that he transferred the net amount remaining, after some expenses and payments to himself, to Associates in its fiscal year ended January 31, 1994 and that the tax was paid on it there.

73 The Ampito invoice charged no GST. Ampito had not registered with GST. Had it applied for and obtained a GST number it would have had to explain the invoice on a GST audit.

74 Mr. Fitz-Andrews testified that he had agreed with Carroll Meisner, his partner, to modifying the partnership agreement so as to permit him to work evenings and week-ends or "off hours" on his own account without accounting to the partnership because an employed accountant had also been permitted to do so. Carroll Meisner, who was Mr. Fitz-Andrews' partner until Mr. Fitz-Andrews set up his own practice in the fall of 1992, testified that he never agreed to amend the "whole time and attention" clause in their partnership agreement to allow Mr. Fitz-Andrews to do accounting work on his own time for his own account. While this is a collateral matter, it shows the source of obvious friction between the two former partners and Mr. Fitz-Andrews' unhappiness in the firm.

75 Mr. Meisner explained the Savage and Moles accounts rendered to Prodigy. On September 25, 1991, Savage and Moles billed Prodigy $2,100 for preparation of a review of annual statements and corporate tax returns. On December 18, 1991, Savage and Moles billed Prodigy $6,500 in respect of $3,675 docketed time in Prodigy's fiscal year ended July 31, 1991 for consulting services on the purchase of three presses from MLP and the related financing from Royal Bank. On October 5, 1992, Savage and Moles billed Prodigy for services in Prodigy's 1992 fiscal year respecting meetings with MLP and Royal Bank to review the financings: $2,850, application for an FBDB loan: $1,245; and GST matters and assessments: $1,150.

76 Mr. Meisner testified that Mr. Fitz-Andrews' hourly billing rates in 1990-1992 were $130 for accounting work and $160 for consulting work, that it was firm policy to enter docketed time into the computerized accounting system daily and that bills were sent based on docketed hours at these rates.

77 Mr. Meisner also reviewed a summary of Mr. Fitz-Andrews' billable and non-billable hours docketed in 1992 until about September 15, 1992. If projected to year end Mr. Fitz-Andrews would have docketed about 2240 hours for 1992 compared to 2266 hours docketed in 1991 when he was an employee. None of Mr. Fitz-Andrews' docketed time at Savage and Moles included the 645 hours billed by Ampito to the Patels on November 10, 1992.

78 Mr. Fitz-Andrews produced no dockets or computer records showing time docketed to Prodigy. He did present diaries for January 1, 1991 to December 31, 1993 noting appointments and the names of clients, sometimes with time recorded in tenths of hours. There are comparatively few entries for other clients. The totals of these entries in 1992 for Prodigy do not seem to match the time he docketed at Savage and Moles in May and June 1992. There are many entries, sometimes during normal working hours but generally in the evenings and on holidays and weekends, bracketing off blocks of time often in pencil, with "P.I.P." or "Prodigy" or "Andy" noted generally in ink and frequently with a similar quick hand, or "P.I.P." with a number of hours noted. In virtually all of these cases there is no description whatsoever of the work done. While different pens are used even on the same day, the same pen seems to have been used for "P.I.P." over a period of time, while the bracketed hours are often in pencil. Sometimes time was blocked off in "off hours" when there were gaps in the regular work hours.

79 Mr. Fitz-Andrews suggests no description of the work is required because it was all on the MLP purchase and the Royal Bank financing.

80 I am not persuaded, on the balance of probabilities, that Mr. Fitz-Andrews spent 645 hours, or anything approaching it, on the work described in the Ampito account in addition to the billings by Savage and Moles for that work. In view of the evidence of the scope of Mr. Fitz-Andrews' involvement in the work described in the Ampito account, particularly in respect of projections, analysis and proposals inherently necessary for the contract for the three new presses with MLP and proposals for its financing and settling the Royal Bank financing, he possibly docketed some additional "off hours" work for Prodigy in 1991 and 1992 which was not billed by Savage and Moles. However these records are not credible.

81 Mr. Fitz-Andrews did not present in evidence his files to show details of the work he did, such as telephone memos, correspondence, draft budgets, draft business plans, draft financial projections, etc. He did have a handwritten proposal, apparently to Royal Bank, a handwritten draft "buy back" agreement for execution by MLP to facilitate Royal Bank's financing, some handwritten notes commenting on terms of an agreement, handwritten financial calculations and other handwritten documents.

82 Mr. Fitz-Andrews says he waited so long to bill this "off hours" work, going back to February 1991, because he had an agreement with Mr. Patel that this off hours work would not be billed until Royal Bank advanced the loan to be made under the loan agreement of December 2, 1991 eleven months after delivery of the three new presses from MLP in January, 1992. Mr. Patel denies there was any such agreement and he claims he thought this work was billed by Savage and Moles only.

83 If a professional person renders an account for services he or she must be prepared to justify that account with credible supporting evidence based on not only docketed hours but also other elements such as result achieved, value to client and the client's ability to pay. Mr. Fitz-Andrews' time entries lack an air of reality both in the manner of their entry and the absence of any written description of the work done. In as much as docket entries of a professional are self serving, they must contain sufficient detail of the services performed to give them an air of reality and provide a means of testing their veracity, both by internal comparison and comparison with external events such as the work product. This is equally so when the professional has a contractual, and possibly fiduciary obligation, to account to his employer and to his partner for such work. There is no evidence that Mr. Fitz-Andrews discussed the matter with Mr. Patel before rendering the account, which one might expect with an account of this size for this client.

2. Revenue Canada Receipts

84 A critical piece of evidence in this case is a photocopy of what purports to be five forms of small bilingual preprinted receipts, obviously available to tax payers for payment of taxes, each of which is filled in with handwriting to show Account Number "AQB 916905" and each of which has the impression of a rubber stamp reading in capital letters:

DEPARTMENT OF NATIONAL REVENUE

TAXATION DIVISION

(Date - stamped)

DELIVERED BY HAND

The receipts are unsigned. They contain neither the location of the Revenue Canada office nor a number to identify the location or user of the stamp.

85 The other particulars on each receipt are handwritten as follows:

Date	**Deduction Period**	**Amount**	**Date on DNR Stamp**
20.11.92	1992	29,652	Nov. 22, 1992
9.12.92	1992	14,758.12	Dec. 9, 1992
15.12.92	1992	37,697.14	Dec. 15, 1992
15.1.93	-	23,912.00	Jan. 15, 1993

Mr. Patel and Sulekha Patel testified that they pressed Mr. Fitz-Andrews for evidence that he had applied the proceeds of Mr. Patel's personal cheques to Prodigy's account with Revenue Canada. They said that Mr. Fitz-Andrews showed up at Prodigy's office in early 1993 and, in the presence of the Patels, gave the originals of these receipts to Sulekha Patel and asked her to photocopy them. She did so. They said Mr. Fitz-Andrews asked that she return the original receipts to him, which she did. The Patels said that Mr. Fitz-Andrews wrote on the bottom of the photocopy of the receipts left with them "128,644.45". The Patels testified that this photocopy was placed in Prodigy's files and that Mr. Fitz-Andrews left the office with the original receipts. The original receipts were not listed in either party's affidavit of documents or produced on discovery.

86 Mr. Patel testified that in July 1993 Revenue Canada assessed Prodigy for 1992 withholdings of $2,752.99 plus interest and penalties which Mr. Patel thought had been paid in 1992 by Mr. Fitz-Andrews. This, says Mr. Patel, was the first indication that the proceeds of the three cheques might not have been used to pay Prodigy's taxes.

87 In 1994 Mr. Patel, on the advice of his new accountant Joel Levitt, disclosed under Revenue Canada's voluntary disclosure procedure his failure to remit substantial employee withholdings in respect of 1992. Revenue Canada subsequently assessed Prodigy $57,825.89 plus penalties and interest. Mr. Patel and Mr. Levitt testified that Revenue Canada denied receiving any of the amounts noted on the five receipts. Prodigy paid the subsequently assessed taxes, interest and penalty. Revenue Canada is prevented by statute from disclosing amounts assessed against and paid by other taxpayers without their consent. There was no evidence presented as to the state of Ampito's accounts with Revenue Canada.

88 Prodigy alleges that the receipts were fabricated by Mr. Fitz-Andrews after this litigation was started to support his statement that he had fulfilled his undertaking to pay the proceeds of the three personal cheques totaling $130,000 to Revenue Canada to cover up the appropriation of the proceeds to himself.

89 Mr. Fitz-Andrews vehemently denies the Patels' allegation. He testified that he has never seen either the original receipts or the photocopy entered as an exhibit. He testified that he first saw the photocopy following the commencement of this litigation. He alleges that Mr. Patel fabricated the receipts to support his story that the proceeds of the cheques

were to be paid to Revenue Canada rather than to Ampito for Mr. Fitz-Andrews' services. Mr. Fitz-Andrews notes that the total taxes assessed for 1992 total only $60,578.88, nothing approaching $130,000, and there is no set of figures to which the $130,000 relates except for the Ampito account.

90 Mr. Fitz-Andrews further notes that all payments of taxes for Prodigy were with cheques drawn on Prodigy's account and not on the Mr. Patel's personal accounts.

91 There is no evidence before me as to who or what taxpayer has account number AQB 916905. Prodigy's account number with Revenue Canada was VHX 087883. There is in evidence a photocopy of an employee copy (No. 3) of a T-4 Supplementary for 1992 for the Patels' son, Kamlesh Patel, which Mr. Patel said he prepared from information dictated to him by Mr. Fitz-Andrews. This shows an employer No. ABQ 9-690 (a different sequence of letters) in the blacked out area of the employee copy. This is unreliable evidence as to whether this sequence of numbers is on the original of this T-4 Supplementary. This document adds nothing to the issue of credibility. The original of this document was not in evidence and Kamlesh Patel did not testify.

92 There was a three-page computer printout of "Ampito Investments Inc. YTD Payroll Journal as at December 31, 1992" showing 13 employees, including Kamlesh Patel, showing the same gross income for him as the T-4 Supplementary. There is also in evidence a copy of a similar printout of seven pages for 23 employees including the 13 employees on the "Ampito" list except that it is headed "Prodigy Industrial Printers Inc. YTD Payroll Journal as at December 31, 1992". The first three pages of the two documents are the same. The last four pages of the latter document contains ten additional names and are separately totalled. These documents are inconclusive of anything except that someone may have been fiddling with Prodigy's computer for conflicting printouts. Mr. Levitt clearly obtained the Ampito list from Mr. Patel in 1994.

93 Mr. Fitz-Andrews points out that total liability for withholdings from the 13 employees common to these printouts would be either $137,000 or $139,000 for withholding tax plus the employee portions of CPP and UIC, a further $18,000. In addition, the employer would be liable for its portion of payments for CPP and UIC. Even at the end of October this liability would have been about $^{5}/_{6}$ of the year's total of about $180,000 or about $150,000 or slightly more because of CPP usually being paid up before year end. This amount bears no direct relationship to the $130,000 in the cheques. The same is true for the 1992 withholdings assessed at $60,000.

3. Handwriting Expert

94 I find the evidence of Ms. Diane Kruger, the handwriting expert called and qualified on behalf of Mr. Patel and Prodigy, to be convincing. She testified as to the methodology of her comparison of the handwriting on the photocopy of the receipts with original and photocopied documents containing known samples of the handwriting of Mr. Fitz-Andrews. These included fax transmittal sheets, two lengthy handwritten memoranda and sheets of accounting paper containing many rough arithmetic calculations. She said this sample size was more than sufficient to form an opinion. She compared each letter, number, bracket, dollar sign and punctuation mark on the receipts with similar writings on the known documents. She acknowledged a number of differences or variations between the receipts and the known handwriting and limitations in working with photocopies. It was Ms. Kruger's opinion that it is "highly probable" that the person who wrote out the originals of the receipts was the writer of the known documents. In cross-examination she explained that she could not be certain but her opinion was stronger than merely probable. She noted none of the hallmarks of forgery, such as tremor, poor line quality, pen lifts or difference in formation. Her evidence was not shaken on cross-examination by Mr. Fitz-Andrews.

95 Mr. Fitz-Andrews offered no expert evidence to contradict that of Ms. Kruger. He argued that the documents used by the expert as known samples of his handwriting were not properly admitted in evidence. However each of these known samples was contained in Exhibit 1 which he agreed to admit as evidence at the beginning of the trial.

96 I am persuaded, on comparing the known examples of copies of Mr. Fitz-Andrews' handwriting with that on the Revenue Canada receipts and with the support of Ms. Kruger's evidence as to the authorship of the receipts, that Mr. Fitz-Andrews produced the receipts for photocopying and that the proceeds of the personal cheques were to be used by Mr. Fitz-Andrews to pay Prodigy's and Ampito's employee withholding tax liabilities. The cheques were not to pay the Ampito account for services dated November 10, 1992. No other explanation for the false receipts was offered by either Mr. Fitz-Andrews or by Mr. Patel.

97 Mr. Patel's new accountant Mr. Levitt, made some inquiries of Mr. Fitz-Andrews in August 1994 respecting the fate of the proceeds of the three personal cheques drawn by Mr. Patel in November 1992 totalling $130,000. In a telephone conversation on August 15, 1994, Mr. Fitz-Andrews told Mr. Levitt that the cheque proceeds were used to pay off invoices rendered by Mr. Fitz-Andrews. Mr. Fitz-Andrews undertook to provide copies of the invoices to Mr. Levitt. On August 22, 1994, Mr. Fitz-Andrews met with Mr. Levitt and told him the $130,000 was used for personal investments on behalf of the Patels and that Mr. Levitt should speak to the Patels to obtain supporting documentation. No supporting documentation was given to Mr. Levitt. Mr. Levitt made a handwritten note on August 22, 1994 of the essence of his conversations on August 15 and August 22.

98 Mr. Fitz-Andrews denied Mr. Levitt's evidence and said that his refusal was based on the fact that this was personal information and he was put off by Mr. Levitt's attitude. I find this a strange attitude in light of this being a conversation between two professionals acting for the same client where Mr. Fitz-Andrews' knowledge was not privileged. At this time Mr. Fitz-Andrews had had his falling out with Mr. Patel.

99 I am satisfied that the Ampito account was highly inflated, if not wholly without foundation. It cannot be justified. I am further satisfied the account was never delivered prior to the cheques being drawn in November 1992. I am satisfied that Mr. Fitz-Andrews had no right to appropriate this money to himself. He is liable to repay it to the Patels.

IX. Royal Bank Payments: $25,500

100 Prodigy claims recovery of the proceeds of the following cheques payable to Royal Bank in 1992 and deposited to Mr. Fitz-Andrews' Account:

April 10	$ 10,000
September 1	7,000
October 1	7,000
November 4	1,500
	$ 25,500

101 Mr. Patel said he paid Mr. Fitz-Andrews' account at Mr. Fitz-Andrews' direction after he told Mr. Patel that he was having trouble obtaining draws from his partnership. Mr. Patel said the $10,000 set by Mr. Fitz-Andrews was paid in April for a payroll computer programme, supervising the payroll in the months following Mr. Frimpong's departure and advising on deductions and was intended to be paid to Savage and Moles and not just Mr. Fitz-Andrews. Prodigy claims recovery because no account had been issued. Mr. Patel said the September payment was for persuading Royal Bank of the profitability of Prodigy in the audit and for a "job well done" in completing the financial statements showing a profit for the fiscal year ended July 31, 1992. He said $7,000 paid in October was related to the payroll manipulations, successful negotiation of the price of the new presses with MLP Canada and the successful financing with Royal Bank.

102 Mr. Fitz-Andrews acknowledges receipt of the payments but denies the purposes alleged by Mr. Patel. Mr. Fitz-Andrews says the purpose of the payments to him was payment for the incorporation of the four new companies, GST advice and advising Prodigy on the software to bring together the accounts for these four companies. It was not for deferral of payroll deductions payments to Revenue Canada so as to mislead Royal Bank. Mr. Fitz-Andrews denies any

part in any payroll deferral. I have found that Mr. Patel was engaged in this activity before Mr. Fitz-Andrews came on the scene.

103 Mr. Fitz-Andrews also stated that he had an arrangement with Mr. Patel to review Prodigy's monthly financial statements before they were forwarded to Royal Bank, as required by Prodigy's borrowing arrangement with Royal Bank. These payments were merely a catch up for previously missed payments.

104 Mr. Patel alleges that the reorganization of Prodigy Industrial Printing in October-November, 1992 was part of Mr. Fitz-Andrews' plan for postponing tax liabilities. The following companies were incorporated on the following dates:

October 29, 1992	Post Prodigy Finishing Inc.
October 29, 1992	Prodigy Colour Systems Inc.
November 9, 1992	Prodigy Printing Services Inc.

Mr. Patel testified that this latter incorporation was supposed to be a change of name of Prodigy Industrial Printers Inc. This was remedied, he says, on July 30, 1993 when the following articles of amendment were filed to effect changes of name:

1) Mr. Patel's original company Prodigy Industrial Printers Inc. became Prodigy Printing Services (1993) Inc.

2) Prodigy Printing Services Inc. became 1007067 Ontario Inc.

105 Prodigy Graphics Group Inc., the plaintiff in this action, was incorporated in June 1993 and was amalgamated with Prodigy in 1995.

106 I see nothing sinister in dividing Prodigy's original business into separate corporations according to function.

107 Prodigy has not established a right to claim these payments to Royal Bank from Mr. Fitz-Andrews. In view of Mr. Patel's explanation of the reasons for the payments, I see no grounds to support the claim. I dismiss the claim for the $25,500.

X. Mr. Fitz-Andrews' Accounts: $46,233

108 On April 30, 1994, Mr. Fitz-Andrews prepared a Statement of Account for Prodigy summarizing statements of account he had rendered to the various companies in the Prodigy Group totalling $58,609.25 and showing payments in 1993 of $12,386.15, leaving a balance owing of $46,233.10. The statement showed a trust balance of $25,283.04 which was appropriated to reduce the balance due to $20,940.06.

109 The accounts on the Statement of Account include one to Prodigy Colour dated April 20, 1993 (which was reduced and re-sent on May 5, 1993) for $27,500 plus GST for a total of $29,425 for organization in 1992, pro-forma statements, financing of a purchase from Crossfield, a new accounting system, discussions with Royal Bank and the lease of a property. Mr. Patel objected to the account pending a review of Mr. Fitz-Andrews' dockets and refused to pay it. Mr. Fitz-Andrews did not provide supporting evidence sufficient to support the account.

110 In determining Mr. Fitz-Andrews entitlement to the balance of $46,233.10 owing on his accounts, I am in effect assessing his accounts in the absence of detailed time dockets and on the basis of the notes contained in his appointment book and the description and product of his efforts.

111 Mr. Fitz-Andrews justified these accounts as follows:

1991	Time for Prodigy Printers (noted above)	500 hrs.
1992	Time for all companies	690 hrs.
		1190.3 hrs.

Less:				
	Ampito Account November 10, 1992 645 hrs.			
	Payments in April, September, October and November 1992 totalling $25,500 say 130 hrs.			775 hrs
	Unbilled balance			415 hrs.
Less:				
	Prodigy Colour May '93 $27,000, say 218 hrs			
	Other 1993 accounts approx. $12,800 say 65 hrs.			283 hrs.
				132 hrs.
Less:				
	Post Prodigy March '94	-	68 hrs.	
	Prodigy Graphics March '94	-	15 hrs.	
	Prodigy Paper March '94	-	3 hrs	86 hrs.
Unbilled				46 hrs.

112 This reasoning is spurious! An account should state the period covered by the account. These don't, lending themselves to this sort of carrying forward of "unbilled work in process" without notice to blindside the client in the future and to suit the convenience of the person rendering the account.

113 Further, Mr. Fitz-Andrews' reasoning relied on an allegedly docketed 500 hours, in excess of that billed by Savage and Moles and the 645 hours by Ampito which I have rejected.

114 I have considered the accounts, the dates of incorporation of the billed companies, the work described therein, Mr. Fitz-Andrews' evidence, the work product made available to me and Mr. Fitz-Andrews billing rate of $160 per hour.

115 I have also considered Mr. Patel's evidence on the bills and the circumstances surrounding the date of the bill.

116 The bills, inclusive of GST, are as follows:

Prodigy Colour - May 5, 1993			$ 29,425.00
Individual Tax returns - April 1993			508.25
Prodigy Printing - December 14, 1993			12,294.30
649337 Ontario Ltd. - January 20, 1994			3,076.25
Post Prodigy - March 3, 1994			10,566.23
Prodigy Paper - March 3, 1994			535.00
Prodigy Graphics - March 3, 1994			2,204.25
Total:			58,609.25
I would allow on these accounts, including G.S.T.			45,000.00
Less:			
	Payments	$12,286.15	
	Transfer from trust	1,101.46	13,487.61
Net amount owing:			$ 31,512.39

XI. Appropriation of Revenue Canada Refunds

117 Mr. Patel objects to the appropriation in February 1994 of the proceeds of two cheques totalling $24,181 from Revenue Canada payable to Prodigy as rebates of over payments. Mr. Fitz-Andrews, as the addressee for service of Prodigy by Revenue Canada, received these cheques payable to Prodigy in February 1994 and persuaded his bank to cash them and deposit the proceeds in Mr. Fitz-Andrews' "trust account". Mr. Patel discovered this appropriation in early May 1994 on receipt of Mr. Fitz-Andrews' statement of account and demanded the proceeds of the cheques.

118 Mr. Fitz-Andrews refused the request saying he was authorized to seize them by a term on page 2 of the audit engagement letter for Prodigy Printing Services (1993) Inc. for its fiscal year ended July 31, 1993 dated November 22, 1993 which stated:

> 5. It is further understood and agreed that with the filing of all corporate tax returns it is agreed that all corporate tax refunds will be applied in trust against outstanding fees for the Prodigy Group of companies in view of the substantial nature of the services provided and substantial amounts outstanding.
>
> 6. It is further understood and agreed that you will be personally responsible for any fees billed and not paid by the group of companies.

Mr. Fitz-Andrews signed at the bottom of page 2 of the letter which requests Mr. Patel to sign a copy of the letter in the space provided and return it to Mr. Fitz-Andrews. The third page contains the agreement signed by Mr. Patel dated December 17, 1993. This document was produced from Mr. Fitz-Andrews' files.

119 Mr. Patel denies signing such a letter. He produced a copy of the letter he says he signed which does not contain paragraphs 5 and 6. It is signed by Mr. Fitz-Andrews on page 2 and there is provision for signing by Mr. Patel on page 3.

120 Each declares the other's version a forgery. Mr. Fitz-Andrews says he gave Mr. Patel four letters on that day. The others did not contain either the authorization to apply tax rebates to accounts or the personal "guarantee". He suggests Mr. Patel has taken the page 2 out of one of the other letters and substituted it for the page 2 which contains the authorization and the guarantee.

121 Mr. Patel accuses Mr. Fitz-Andrews of fabricating his version of page 2, removing the shorter page 2 he says he signed and substituting the longer version with the authorization and guarantee. Mr. Patel produced copies of engagement letters which he signed in previous years which do not contain such provisions.

122 The cross-examination of Mr. Fitz-Andrews straddled a weekend. On the Friday Mr. Fitz-Andrews said he merely inserted the two clauses in his word processor's standard form. On the Monday he acknowledged talking to someone about his evidence and said he must have created a new document by retyping the page without properly justifying the right margin.

123 Clause 5 respecting appropriation of tax refunds payable to the client is highly suspect. It is unlikely Mr. Patel would have signed such a clause in November 1993 in view of his refusal to pay Mr. Fitz-Andrews account of May 5, 1993, which replaced a larger account dated April 20, 1993, until he had received satisfactory evidence of dockets to support the account.

124 The cheques were payable to Prodigy rather than Mr. Fitz-Andrews. Why would either of them expect Mr. Fitz-Andrews to be able to negotiate the cheques with his bank and appropriate them to his own account without endorsement by an authorized signing officer of Prodigy? There is no evidence that Mr. Fitz-Andrews had such an authority.

125 In view of my findings on credibility in respect of the Ampito account, I have greater confidence in Mr. Patel's evidence, generally, than I have in the evidence of Mr. Fitz-Andrews'.

126 On this issue I find that Mr. Fitz-Andrews had no authority to appropriate to himself the $24,181 represented by cheques payable to Prodigy. He is liable to pay this amount to Prodigy.

XII. Claim Against Gina Fitz-Andrews

1. As Director of Ampito

127 There is no evidence that Gina Fitz-Andrews played any part whatsoever in the preparation or rendering of the Ampito account or the receipt or disbursement of the $130,000. There is no evidence that she had any knowledge of these events. While she was the sole shareholder, a director and an officer of Ampito, she was unaware of her husband's use of his authority as a director, officer and bank signing authority and did not authorize it. She played no part in the operation of the company. It would be wholly unjust to pierce the corporate veil to make her personally liable or make her an accessory to a breach of trust: see *Transamerica Life Insurance Co. of Canada v. Canada Life Assurance Co.* (1996), 28 O.R. (3d) 423 (Ont. Gen. Div.).

2. Tracing

128 There is no evidence that any of the proceeds of the Patels' cheques for $130,000 can be traced to the payment of any part of the purchase price of the house. The use of the $75,000 G.I.C. purchased with the proceeds of the $130,000 and used as a "carrot" for the CIBC mortgage, but which was not in fact used in the purchase, cannot justify making Gina Fitz-Andrews liable for it.

129 Accordingly, I find that Gina Fitz-Andrews is not personally liable to the Patels for any part of the $130,000 or to Prodigy for the $25,500 paid to Royal Bank for Mr. Fitz-Andrews'. However, the plaintiffs allege that Gina Fitz-Andrews may be liable for the share of the property transferred to her by her husband in a deed from him to her of his interest by reason of the transaction being void under the *Fraudulent Conveyances Act*, R.S.O. 1990, c. F.29.

3. Recipient of Fraudulent Conveyance

130 On February 25, 1993, Gina and Mr. Fitz-Andrews signed an agreement to purchase for $300,000 cash the house they had been renting at 1224 Highgate Place since 1989. The purchase price was payable $10,000 down as a deposit and the balance on closing. It was conditional on the purchaser being approved for mortgage financing by Canadian Imperial Bank of Commerce ("CIBC") within 10 days. The purchase price included "existing appliances". No real estate commission was payable.

131 Gina Fitz-Andrews applied to CIBC for a mortgage of $225,000 with Mr. Fitz-Andrews to be the guarantor. Their total incomes, all out of Mr. Fitz-Andrews' practice where Gina Fitz-Andrews did some work with payables, was stated to be slightly over $100,000. Their investments consisted of a $75,000 GIC with CIBC and $9,000 with "Royal". They had a bank account of $15,000, $10,000 in the house purchase, $200,000 in Mr. Fitz-Andrews' practice and $30,000 in two cars. Mr. Fitz-Andrews owed Royal Bank $71,000 in respect of his practice. The Fitz-Andrews said they would have $75,000 cash equity in the property.

132 There is no indication whether the $71,000 indebtedness to Royal Bank was in respect of his old practice or his new practice. Cheques and bank records in late 1993 indicate his new firm was using CIBC.

133 The purchase closed on March 26, 1993 with a deed to Gina and Mr. Fitz-Andrews as joint tenants. The land transfer tax affidavit sworn by Mr. Fitz-Andrews showed the consideration as $300,000 cash.

134 There was a first mortgage by Gina and Mr. Fitz-Andrews to CIBC of $225,000. While disclosure was called for in the land transfer tax affidavit, it was not mentioned.

135 The Amended Statement of Adjustments showed:

Sale Price		$300,000.00
Deposit	$10,000.00	
Vendor Mortgage Back	30,945.16	
Last Month's Rent	1,500.00	
Adjustment for Rent Payments	33,500.00	
(Tax Adjustment calculation)		945.16
Balance Due on Closing	225,000.00	

	$300,645.16	$300,945.16

The balance due on closing was the proceeds of the CIBC mortgage.

136 The adjustment for rent paid was described by the defendants as a credit for the air conditioner they had installed, a negotiated deduction for unpaid real estate commission, credit for repairs they had made as tenants and credit for appliances they had purchased and were entitled under the lease to take with them. In as much as these adjustments were not required under the agreement, I see no legitimate reason whey they were made. If, instead of justifying $33,500 adjustment the price had been reduced by that amount, their equity and the land transfer tax payable would have been less.

137 The mortgage back, not called for under the agreement, was negotiated by Mr. Fitz-Andrews. He told the vendors he could not close without it. In view of the vendor's intent to move back to India, they were motivated vendors. This explanation by Mr. Fitz-Andrews is credible.

138 The mortgage back to the vendors was for $30,945.16 at 7.5% per year for 3 years, repayable interest only quarterly. It was from Gina Fitz-Andrews only and was guaranteed by Mr. Fitz-Andrews.

139 On March 25, 1993, Mr. Robert Filkin, solicitor for the Fitz-Andrews, wrote to Mr. Michael Bukovac, solicitor for the vendors, to confirm the terms of the second mortgage and "it not be registered". This is a risky and highly unusual position for any mortgagor to take. No explanation was offered. In fact, this mortgage was registered on August 6, 1993. On maturity in 1996 it was assigned to a corporation owed by the Fitz-Andrews family.

140 On the date of closing, March 26, 1993, Mr. Fitz-Andrews executed a transfer of the property to Gina Fitz-Andrews. The land transfer tax affidavit sworn by Mr. Fitz-Andrews states the consideration is "$2 and natural love and affection" and "no consideration passing directly or indirectly". In response to a question in the affidavit as to whether the land is subject to any encumbrance it recites only: "Yes ($225,000)". This deed was registered on April 2, 1993.

141 Mr. Fitz-Andrews testified that this deed was intended to rectify their intent prior to closing that Gina Fitz-Andrews be the registered owner of the property. Gina and Mr. Fitz-Andrews have continued to live in the house with their family.

142 There is no evidence that CIBC would be concerned with subordinate financing but perhaps Mr. Fitz-Andrews thought CIBC would object if his cost was little more than the amount of its mortgage. First mortgagees generally want a cushion of owner equity in the range of 25 to 35 per cent. The lawyer acting for the Fitz-Andrews on the purchase, Mr. Filkin, was also acting for CIBC.

143 There is no evidence why the "correcting" deed, which was signed on the same date as the deed from the vendors, was not registered until a week later.

144 Neither Mr. Filkin, nor a representative of CIBC nor Mr. Bukovac was called to testify on behalf of the Fitz Andrews.

145 The *Fraudulent Conveyance Act* provides:

> 2. Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void (sic) as against such persons and their assigns.

3. Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section.

4. Section 2 applies to every conveyance executed with the intent set forth in that section despite the fact that it was executed upon a valuable consideration and with the intention, as between the parties to it, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred, unless it is protected under section 3 by reason of good faith and want of notice or knowledge on the part of the purchaser.

146 There need only be an intention to defeat or hinder "creditors or others" of their lawful claims. There need not be an intention to defraud.

147 Mr. Fitz-Andrews acknowledged that the reason for putting title in his wife's name was because he was following the advice of his lawyer based on Mr. Fitz-Andrews' advice that he was a defendant in an outstanding lawsuit by a former landlord against Savage and Moles and because he was involved in litigation with his former partner Mr. Meisner. While not necessarily creditors yet, those parties were certainly "others" for the purpose of the Act: *Waterline Products Co. v. Lisaco Investments Ltd.* (January 24, 1991), Doc. 41431/89 (Ont. Gen. Div.) (Ont.Gen.Div.); *Gauthier v. Woollatt*, [1940] 1 D.L.R. 275 (Ont. S.C.); *Canadian Imperial Bank of Commerce v. Boukalis* (1987), 34 D.L.R. (4th) 481 (B.C. C.A.) at 487.

148 At the time Mr. Fitz-Andrews signed the deed, his creditors included the Patels in respect of the $130,000.

149 The date on which the intent is to be assessed is the date the transfer was executed: *Bank of Montreal v. Chu* (1994), 17 O.R. (3d) 691 (Ont. Gen. Div.).

150 Where proper consideration is lacking, the intent of the transferee is irrelevant; where the intent of the parties to the conveyance is to defraud creditors, the question of consideration is irrelevant: *Son v. Kim* (October 13, 1994), Doc. C5442/91 (Ont. Gen. Div.).

151 Accordingly, by reason of s.2 of the *Fraudulent Conveyances Act*, the correcting deed was void and the title reverts to Gina and Mr. Fitz-Andrews as joint tenants.

152 Even if Mr. Fitz-Andrews had not stated his intent, a court may infer intent from suspicious circumstances which are referred to as the "badges of fraud", having their origins in *Twyne's* Case *Twyne's Case* (1602), 3 Co. Rep. 80b (Eng. K.B.). These include:

(1) Transfer to a non-arms length person.

(2) Grossly inadequate consideration.

(3) The transferor remains in possession on occupation of the property for his own use after the transfer.

(4) The transferee is holding the property in trust for the transferor.

(5) There are actual or potential liabilities facing the transferor or he is about to enter upon a risky undertaking.

(6) The transferor has few remaining assets after the transfer.

(7) The transfer was effected with unusual haste.

(8) The transaction was secret.

(9) The absence of a sound business or tax reason for the transaction.

(10) Destruction or loss of relevant papers or inaccurate documents supporting the transaction.

(11) Cash is taken in payment instead of a cheque.

(12) The deed contains false statements as to the consideration.

(13) The deed gives the grantor a general power to revoke the conveyance.

(14) The deed contains the self-serving and unusual provision "that the gift was made honestly, truly and *bona fide*".

See *Canadian Imperial Bank of Commerce v. Graat* (1992), 5 B.L.R. (2d) 271 (Ont. Gen. Div.), per Granger J.; C.R.B. Dunlop, *Creditor, Debtor Law in Canada*, 2nd ed. (Toronto: Carswell, 1995).

153 The badges of fraud are of evidentiary value in determining the issue of intent but are not conclusive evidence of fraud. Fraudulent intent is a matter of fact to be determined in the circumstances of each case on the basis of the evidence as a whole: *Meeker Cedar Products Ltd. v. Edge* (1968), 12 C.B.R. (N.S.) 49 (B.C. C.A.).

154 Once the suspicious circumstances raise a *prime facie* presumption of intent to hinder, defeat or defraud a creditor, the court may find the intent unless the presumption is displaced by corroborative evidence of the *bona fides* of the debtor in the suspect transaction: *Kingsbridge Grand Ltd. v. Vacca* (December 20, 1999), Doc. 98-CV-143861, 98-CV-14960 (Ont. S.C.J.) citing *Koop v. Smith* (1915), 51 S.C.R. 554 (S.C.C.); *Applecrest Investments Ltd. v. Toronto Masonry (1986) Ltd.* (1997), 23 O.T.C. 277 (Ont. Gen. Div.); *Rinaldo v. Rosenfeld* (December 2, 1999), Doc. 98-CV-154750 (Ont. S.C.J.).

155 At the time of the correcting deed, Mr. Fitz-Andrews was being sued by a former landlord, was in litigation with a former partner that could result in an adverse costs order and was jointly liable on the mortgage to CIBC, notwithstanding the agreement that he would be a guarantor only, and was liable to the Patels to repay the $130,000. He transferred to his wife his interest in the property, on the day he acquired it, for $2 and natural love and affection. He continued to live in the house. Judging from his mortgage application to CIBC he had few other assets outside his accounting practice, on which he owed a substantial amount. The presumption of intent has been raised.

156 Mr. Fitz-Andrews argues that the deed from the vendors was supposed to be solely to his wife but his lawyer erred. While they both agreed to purchase the house the mortgage application showed Gina Fitz-Andrews would be the borrower and Mr. Fitz-Andrews would be the guarantor. Gina Fitz-Andrews' evidence confirmed that she alone was to be the purchaser but Mr. Fitz-Andrews was to be the guarantor of both mortgages.

157 My response is that a direction by the purchasers, under the agreement to purchase, to the vendors on closing to convey the property to Gina Fitz-Andrews would qualify equally with a subsequent deed to constitute a conveyance for the purpose of s. 2 of the *Fraudulent Conveyances Act*.

158 The failure of the land transfer tax affidavit to particularize the consideration or note the mortgages, the credits given in the statement of adjustments not called for in the agreement of purchase and the five month delay in registering the mortgage back to the vendors remain unexplained. Mr. Fitz-Andrews could reasonably have been expected to call the vendors, CIBC or his lawyer to provide evidence of his *bona fides*. He did not call any of them. I am entitled to draw an adverse inference respecting Mr. Fitz-Andrews *bona fides* and find the conveyance was made with an intent to delay his creditors.

159 Again, the result is the same. The amending deed is void.

XIII. Claims for Failure to Disclose on the Motion for Mareva Injunction

160 Mr. Fitz-Andrews alleged that the evidence in the affidavits used to obtain the certificate of pending litigation on the house and the *ex parte mareva* injunction freezing his assets, misstated and omitted material facts. It failed to

make full and frank disclosure on the *ex parte* application: *Chitel v. Rothbart* (1982), 39 O.R. (2d) 513 (Ont. C.A.). Accordingly he says he is entitled to claim damages based on the plaintiffs' undertaking in the affidavit of Mr. Patel dated November 29, 1994.

161 Generally, if the plaintiff obtaining an injunction is unsuccessful at trial, an inquiry as to damages will result, unless there are special circumstances respecting compliance with the undertaking. Such special circumstances would exist where the plaintiff can make out an equitable defence to the claim for damages based on the defendant's conduct and the plaintiffs' *bona fides*. The defendant's conduct might raise an issue of estoppel, a delay amounting to laches, other prejudice to the plaintiff, and whether the defendant comes to court with clean hands. The damages are to be assessed on the same basis as damages for breach of contract including causation, remoteness, forseeability and mitigation: See *Nelson Burns & Co. v. Gratham Industries Ltd.* (1987), 23 C.P.C. (2d) 279 (Ont. C.A.) and the annotation thereto by Paul Bates.

162 Even if there had not been a trial, innocent non-disclosure or the mere omission of a significant single fact will not necessarily warrant dissolving an injunction. The non-disclosure or misstatement must be such as was material to the decision and either would have made the decision doubtful or may have affected the outcome of the motion: *Waites v. Alltemp Products Co.* (1987), 19 C.P.C. (2d) 185 (Ont. Dist. Ct.) (Ont.Dist.Ct.).; *Edmonton Northlands v. Edmonton Oilers Hockey Corp.* (1994), 23 C.P.C. (3d) 72 (Alta. C.A.) (Alta.C.A.) affirming (1993), 23 C.P.C. (3d) 49 (Alta. Q.B.); *Pulse Microsystems Ltd. v. SafeSoft Systems Inc.* (1996), 47 C.P.C. (3d) 360 (Man. C.A.); *Girsberger v. Kresz* (1998), 19 C.P.C. (4th) 57 (Ont. Gen. Div.).

163 In this case Mr. Patel did not disclose his involvement in the scheme of withholding taxes dating back to 1988 and clearly suggested that Mr. Fitz-Andrews was party to a scheme to do so since 1989. That is information material to the exercise of a judge's discretion in granting the injunction. It may have affected the outcome.

164 Mr. Fitz-Andrews pointed out numerous other omissions or misstatements which I do not think were material. There were numerous other allegations which were consistent with my findings particularly with respect to the misapplication of the $130,000 and the misappropriation of Revenue Canada cheques.

165 In this case the defendants filed responding affidavits within five days after being notified of the injunction but did not proceed to a timely cross-examination. The injunction was varied in early 1995 to allow payment of $10,000 to Mr. Fitz-Andrews and substitution for it of a $50,000 letter of credit and payment into court of the $25,283 he held in trust. The proceedings were adjourned pending cross-examinations. Mr. Fitz-Andrews parted company with his lawyers and was ill for some time. However bitterly contested interlocutory proceedings continued.

166 In January 1999, Mr. Fitz-Andrews obtained an order permitting cross-examination of Mr. Patel on his November 29, 1994 affidavit.

167 Mr. Fitz-Andrews brought motions on October 25, 1999 and again on January 18, 2000 to set aside the *mareva* injunction and the certificate of pending litigation. Both were denied on the basis of an imminent trial. The latter was also based on the refusal or failure to move "forthwith".

168 Mr. Fitz-Andrews has failed to provide evidence of his damages. He said in opening that (a) he had trouble borrowing money; and (b) could not maintain a bank account personally but had to do is financing through his wife. In closing he said the injunction and litigation damaged his reputation with banks and obtaining client referrals from them. No particulars were offered in evidence. No cross-examination was based on it.

XIII. Summary

169 I order as follows:

(a) I order Mr. Fitz-Andrews to repay to the Patels the $130,000 paid in November - December 1992.

(b) I dismiss Prodigy's claim for the $25,500 paid to Royal Bank.

(c) I order Prodigy to pay to Mr. Fitz-Andrews $31,512.39 on the accounts rendered to Prodigy.

(d) I order Mr. Fitz-Andrews to repay to Prodigy the proceeds of the tax refunds totalling $24,181 received in February 1994.

(e) I dismiss Mr. Fitz-Andrews counterclaim for damages.

(f) I declare the conveyance of Mr. Fitz-Andrews' interest in the house to Gina Fitz-Andrews on March 26, 1993 void.

(g) I dismiss the claim against Gina Fitz-Andrews.

(h) Interest is payable on all amounts at the rate of 5% per year from the first day of the month following their receipt or the dates of the accounts.

170 Costs may be addressed in written submissions.

Action allowed; counter-claim dismissed.

TAB 8

COURT FILE NO.: 1424/99
DATE: 20021223

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:	
XDG LIMITED	I. Duncan and M. Van Bodegom, for the Plaintiff XDG Limited
	A. Speciale, for the Plaintiff William Green Roofing Ltd.
Plaintiffs	
- and -	
1099606 ONTARIO LIMITED and GENERAL ELECTRIC CAOUTAK CANADA INC.	L. Ricchetti, for the defendant General Electric Capital Canada Inc.
	No one appearing for 1099606 Ontario Limited
Defendants	
	HEARD: July 9-12, 2002

THE HONOURABLE MR. JUSTICE D.J. GORDON

[1] A trial of this consolidated contraction lien action was directed to determine the priority as between the lien claimants and the mortgagee with respect to certain lands in the City of Kitchener described as the “Dielcraft property”.

BACKGROUND

[2] 109606 Ontario Limited ("109") was incorporated on 30 November 1994. In December 1994 it purchased the Dielcraft property for $1,515,000. The property was leased to Euro United Corporation ("Euro United"), commencing 1 April 1995 for the purposes of storing raw material and finished product.

[3] Mr. Sam Rehani was the sole director, officer and shareholder of 109. He was also the controlling shareholder and president of Euro United.

[4] In 1998 and 1999 the lien claimants provided services and material to the Dielcraft property. Various contractors were involved, commencing with certain demolition work to the ultimate renovation, being the raising of the building roof. In the fall of 1999 the contractors left the job site as they were not being paid by 109. Claims for lien were registered on title commencing in October 1999.

[5] Euro United, and related companies operating under a similar name in different jurisdictions, was financed by General Electric Capital Canada Inc. ("GECC") pursuant to a credit agreement dated 13 November 1998. By the end of March 1999 GECC determined Euro United was in a default position regarding certain covenants in the credit agreement. In April 1999 an amendment to this agreement resulted in 109 providing a guarantee and mortgage on the Dielcraft property in favour of GECC regarding the indebtedness of Euro United.

[6] Euro United temporarily corrected its default position, but by August 1999 GECC determined there were significant problems. On 24 November 1999 GECC demanded payment from Euro United and 109. In December 1999 KPMC Inc. was appointed interim receiver of

Euro United and 109. In June 2000, both companies were declared bankrupt and KMPG Inc. was appointed trustee of their estates. Sale of the property by the trustees was authorized in January 2002.

[7] The sale proceeds are held by KPMG Inc. pending the outcome of this litigation. There are insufficient funds to pay the lien claimants and the mortgage holder.

ISSUES

[8] Pursuant to the order of Sills J., granted 17 December 2001, the statement of issues identified the following:

1. Section 20 of the Ontario *Corporations Act*. Is the mortgage invalid or void as against the plaintiffs as a result of contravening section 20 of the Ontario *Business Corporations Act*?

2. Section 4 of the *Assignments and Preferences Act* and section 2 of the *Fraudulent Conveyances Act*.

   Is the mortgage invalid or void as against the plaintiffs as an unlawful assignment or preference or as a fraudulent conveyance?

3. Section 78 of the *Construction Lien Act.*

   (a) Was the mortgage registered prior to the time when the first lien arose in respect of the subject improvement, and, if so, to what extent does the mortgage have priority under section 78 of the Construction Lien Act?

   (b) Was the mortgage registered as a subsequent mortgage, and, if so, to what extent does the mortgage have priority under section 78 of the *Construction Lien Act*?

ANALYSIS

(i) Section 20, *Business Corporations Act*

(a) 109 and GECC

[9] Euro United was involved in the manufacture and sale of plastic injection mould products, such as patio furniture. Some of their product was supplied to large retail stores in Canada and the United States. According to Mr. Paul Feehan, Senior Vice President of GE Capital Commercial Finance, Inc., a related company to GECC, Euro United was growing rapidly. Mr. Feehan, who was involved in the underwriting of Euro United's financing by GECC, reported the growth in sales went from $10,000,000 in 1996 to $102,000,000 in 1998.

[10] The Canadian Imperial Bank of Commerce was the lending institution providing financing to Euro United. GECC, acting as agent for a syndicate of lenders, including itself, provided new replacement financing in November 1998 consisting of a revolving line of credit in the notional amount of $127,000,000 and a term loan of $50,000,000. The line of credit authorized from time to time was based on a formula pertaining to receivables and inventory.

[11] Mr. Feehan, and others at GECC, conducted a due diligence investigation of Euro United from July to November 1998. The new financing terms were set out in the credit agreement dated 13 November 1998. GECC acquired security on the assets of Euro United.

[12] GECC was aware of Euro United leased the Dielcraft property from the outset. A Landlord's Waiver and Consent, signed by Mr. Rehani on behalf of 109 and Euro United, dated 16 November 1998, was one of the documents in the security package. A copy of the lease was attached to this document indicating an annual rent to be paid by Euro United in the sum of $700,000 on a net net basis commencing 1 April 1996 and ending 31 March 2002. GECC was also aware Mr. Rehani controlled both companies.

[13] By the end of March 1999, less than five months after the advance on the credit agreement, GECC became aware Euro United was in a default position. Amongst other items, Euro United had overstated its receivables, resulting in an overadvance on the line of credit of $15,300,000. In addition, Euro United had paid Mr. Rehani $525,000, apparently with respect to his shareholder loan, and purchased and mortgaged their head office property in Oakville, both items lacking the required consent of GECC. At this point in time, GECC's exposure was $89,900,000 on the line of credit and $50,000,000 on the term loan.

[14] Mr. Feehan, and others involved in the financing, met with Mr. Rehani on 5 April 1999. Mr. Rehani offered to add his real estate, the Dielcraft property, as collateral and indicated its value to be $7,000,000 to $8,000,000. There was an indication equity investors might become involved in Euro United. Mr. Feehan said GECC wanted to resolve the existing financing problems and move forward in their relationship with Euro United. He also acknowledged GECC wanted to buttress its existing security to cover Euro United's indebtedness.

[15] On 6 April 1999 Mr. Feehan reported to his superior, setting out the issues and possible solutions. In addition to taking security on the Dielcraft property, he recommended a two percent bonus on the indebtedness and a $200,000 fee to charged to Euro United as well as acquiring an option to purchase equity on favourable terms. Mr. Feehan testified GECC had not yet concluded to retract its financing, that Euro United was thriving and although it had significant management and administrative problems, he felt GECC should "take the risk" and provide bridge financing.

[16] Nevertheless, in his written report dated 5 April 1999, he told his superior:

> "Therefore we recommend that GECC choose the least disruptive solution because it allows Advent to work towards our quickest and easiest exit (i.e. Lehman). In addition, GECC is receiving additional boot collateral and is getting paid for its risk with an equity opportunity in the future."

[17] Upon receipt of approval from his superior, Mr. Feehan submitted a written proposal to Mr. Rehani on 9 April 1999. It was accepted the same date.

[18] The security documentation was prepared and signed by 14 April 1999, within five days of the accepted proposal. The mortgage was registered on 15 April 1999. The documentation appears to have been prepared by the solicitors for GECC, McMillan, Binch, although it is noted Euro United and 109 were represented by Bennett Jones. Mr. Rehani signed all documentation for 109, including the guarantee for $11,5000,000 and the mortgage for $300,000,000. Numerous declarations and other documents were also executed by Mr. Rehani, including an insolvency certificate.

[19] Mr. Feehan stated the amounts described in the guarantee and mortgage were determined by GECC's solicitors. The $11,500,000 stated in the guarantee resulted from Mr. Rehani's representation the value of 109's assets was $12,000,000 with only $100,000 in liabilities. The $300,000,000 referred to in the mortgage was to cover loans of the syndicated loan agreement although Mr. Feehan was not clear on this explanation.

[20] The GECC proposal dated 9 April 1999 permitted it to conduct a due diligence investigation. For some unexplained reason, GECC chose not to make any inquiry with respect to 109. According to Mr. Feehan, GECC relied exclusively on the representations of Mr. Rehani.

[21] In due course, GECC receive the executed security documents from its solicitors. There was no reporting letter regarding certification of title with respect to the Dielcraft property. Mr. Feehan indicated a certification was required and mistakenly assumed it was provided by the solicitors for 109.

[22] GECC did not request financial statements from 109, nor did they conduct a credit check. They were unaware 109 had never filed income tax returns. GECC did not inspect the Dielcraft property nor did they obtain an appraisal.

[23] The proposal contained a provision whereby GECC would release its mortgage if 109 obtained another mortgage, so long as the proceeds therefrom of at least $4,000,000 were contributed to Euro United as equity and applied to reduce the line of credit with GECC. This item was not included in the amending agreement.

[24] Mr. Feehan said his only concern was the Dielcraft property be worth at least $4,000,000. He was not concerned with Mr. Rehani's representations as to the property value, nevertheless, no inquiry was made to appraise the property.

[25] City Management & Appraisals Ltd. provided an appraisal report dated 3 April 2000 to KPMG Inc., in which they estimated the market value, as of 1 June 1999, at $3,190,000. This valuation appears to be accepted by the parties as the market value on 15 April 1999. The stated value, however, may be high as the appraiser also estimated market value as of 1 April 2000 to be $5,000,000, yet the property only sold for $2,896,000 in January 2002. There may have been intervening market conditions affecting the sale price although no evidence was presented.

[26] Mr. Feehan also said GECC had no reason to question the representations made by Mr. Rehani although he offered to explanation. Without due diligence, it is equally reasonable to say GECC had no reason to believe those representations.

[27] The declarations and certificates signed by Mr. Rehani, on or before 14 April 1999, as part of the security documents required by GECC contained numerous errors or, perhaps, deliberate false statements, examples of which are as follows:

(a) there was no change in the financial condition 109 which would have a material adverse effect on its ability to pay GECC and all rental payments where current when, in fact, Euro United had not paid its rent for at least four months and, therefore, 109 had no income;

(b) no material or services had been provided to the property, nor contracts signed, nor estimates given or, alternatively, all amounts have been paid in full and no liens have arisen within the meaning of the *Construction Lien Act* when, in fact, 109 had entered into substantial contracts in excess of $3,000,000 to renovate the building, work had started in August or September 1998, there were monies owing to one contractor, and, accordingly, liens had arisen;

(c) there were no encumbrances against the assets of 109 when, in fact, Engel Canada had an outstanding debenture or general security agreement;

(d) the value of assets was inflated and liabilities were not disclosed;

(e) 109 was up-to-date in filing income tax returns when, in fact, 109 had never filed a return since incorporation in 1994 and, further, there was significant, income tax owing.

[28] All of these errors or misrepresentations would have been discovered on a due diligence investigation. GECC and its related companies are well known in the commercial finance business. They specialize in large commercial loans starting at $5,000,000. They are a sophisticated lending institution. Failure to perform a due diligence investigation of 109 is inconsistent with GECC's normal practice.

[29] On 27 April 1999 Mr. Feehan was informed 109 and Euro United had increased the rental payment required from $700,000 to $1,400,000 per annum. No explanation was requested. Mr. Feehan was still unaware rent was not being paid.

[30] Equity investors contributed $70,000,000 to Euro United over the two months following 15 April 1999 and the overadvance was paid off by 25 May 1999. GECC, however, did not release its mortgage on the Dielcraft property.

[31] In August 1999 Euro United requested an overadvance of $300,000. GECC refused. Mr. Feehan said Euro United was growing rapidly without the proper financing to support the growth. In fact, this was similar to the comment he made in April 1999.

[32] Mr. Feehan stated GECC discovered the construction project on the Dielcraft property in November 1994 when Mr. Rehani made mention of it, he says, for the first time.

[33] On 24 November 1999 GECC demanded payment from Euro United and 109. The end result was the bankruptcy of these companies and the ultimate sale of assets by the trustee.

(b) Subsection 20(1), *Business Corporations Act*

[34] Subsection 20(1) of the Ontario *Business Corporations Act*, as at the relevant time of the events, said:

> "20(1) Financial assistance by corporation –
> Except as permitted under subsection (2), a corporation with which it is affiliated, shall not, directly or indirectly, give financial assistance by means of a loan, guarantee or otherwise,

> (a) to any shareholder, director, officer or employee of the corporation or affiliated corporation or to an associate of any such person for any purpose; or,
>
> (b) to any person for the purpose of or in connection with a purchase of a share, or a security convertible into or exchangeable for a share, issued or to be issued by the corporation or affiliated corporations,
>
> where there are reasonable grounds for believing that,
>
> (c) the corporation is or, after giving the financial assistance, would be unable to pay its liabilities as they become due; or
>
> (d) the realizable value of the corporation's assets, excluding the amount of any financial assistance in the form of a loan and in the form of any secured guarantee, after giving the financial assistance, would be less than the aggregate of the corporation's liabilities and stated capital of all classes."

[35] The parties acknowledge 109 and Euro United were affiliated corporations and the guarantee and mortgage provided by 109 constituted financial assistance within the meaning of subsection 20(1).

[36] The purpose of subsection 20(1), in part, is to prevent the dissipation of corporate assets that might otherwise prejudice the financial position of creditors and shareholders: see: Wayne D. Gray, *Corporate Guarantees*, 1999, Law Society of Upper Canada, Continuing Legal Education Lectures.

[37] The initial determination is the amount of the financial assistance. The guarantee says $11,500,000, the mortgage says $300,000,000. There is some merit in relying on the amount stated in the mortgage, insofar as the mortgage is central to the issue in this litigation; however, I am of the view such is misleading. The explanation provided for this sum bears little, if any, relationship to the actual credit agreement amendment. Further, 109's liability is from the guarantee, the mortgage only providing collateral security.

[38] GECC suggests the financial assistance is limited to $4,000,000, relying on its 9 April 1999 proposal which allowed for such payment, but on strict conditions. This provision was not inserted in the amendment to the credit agreement, the guarantee or any of the security documents delivered on 14 April 1999. Further, GECC has always claimed entitlement to the full amount of the guarantee, namely $11,500,000, as confirmed by its demand letter on 24 November 1999 and, as well, Mr. Feehan's testimony at trial.

[39] Accordingly, I find the amount of financial assistance was $11,500,000.

[40] The test in subsection 20(1)(c) and (d) is an objective one, that is, were there reasonable grounds on 15 April 1999.

[41] The practical difficulty regarding a review of the financial problems of Euro United and 109 is that much of the evidence relates to subsequent events. Their ultimate bankruptcy, however, cannot be relied upon as the basis for finding a breach of this statutory provision. There are, however, a number of matters that existed on 15 April 1999 and are relevant to this issue. The evidence established the following facts:

(i) 109 had no income as Euro United had not paid its rent for at least four months;

(ii) the only prior source of income for 109 had been rental payments from Euro United which it relied on to meet its obligations;

(iii) 109 had an outstanding debt to Engel Canada, subsequently calculated by KPMG to be $279,913, as at 30 June 1999;

(iv) 109 had never filed income tax returns and there was income tax owing, subsequently calculated by KPMG to be $1,441, 200 as at 30 June 1999;

(v) similarly, there was goods and services tax owing by 109, subsequently calculated by KPMG to be $26,618 as at 30 June 1999;

(vi) it is reasonable to assume 109 had other ongoing expense in the normal course of business, particularly if Euro United was also not paying the property related expense;

(vii) 109 had $102,275 on deposit in its bank account;

(viii) the property was valued at $3,190,000;

(ix) other assets of 109 were described as rent owing from Euro United and monies owing from its shareholder, Mr. Rehani, but there was no evidence these were tangible assets;

(x) 109 had entered into construction contracts in excess of $3,000,000, much of it for future work, and, although contractors had been substantially paid to date, there were holdback monies owing to one contractor;

(xi) the GECC mortgage prevented the property being used by 109 as security to fund the construction project.

[42] On 15 April 1999, 109 was not paying, nor was able to pay, its outstanding liabilities. It had no income and significant debt had accumulated. Even if Euro United had been paying rent, there would be insufficient income to pay liabilities. The construction project, commenced some months prior, would require substantial funding which could not come from income. The guarantee and mortgage to GECC compounded the situation by preventing use of the property as security for funding to pay liabilities.

[43] In addition, the value of 109's assets on 15 April 1999, excluding the amount of the financial assistance, was less than its outstanding liabilities. The construction expense alone was equal to or exceeded the property value. The outstanding income tax liability suggests it was only a matter of time before failure would occur.

[44] In my review of the evidence, it appears 109 failed the solvency and the balance sheet tests without having to take into account the financial assistance provided in the guarantee and mortgage, although it is possible 109 might have been able to meet most of its liabilities if Euro

United was paying its rent and it could mortgage the property to fund the construction. Neither event occurred, nor was there evidence to suggest it would occur.

[45] Nevertheless, consideration must given to whether there were reasonable prospects of GECC calling on the guarantee as of 15 April 1999. In this regard, the comments by Farley J. in *Clarke v. Technical Marketing Associates Ltd. Estate* (1992) 8 O.R. (3d) 734 (Gen. Div.) at p. 750:

> "It does not seem to me that the words 'after giving the financial assistance' under either s. 44(1)(c) or (d) mean that the tests have to be applied on the assumption that the corporation giving the guarantee has had to make payment. The guarantee has been given as financial assistance when it was entered into and not when it might actually be called upon (or as if it had been called upon). Thus a guarantee would no appear to impinge upon the 'cash flow' requirement contemplated by s. 44(1)(c) if given on a naked basis.
>
> However, one has to go back to the lead-in words 'where there are reasonable grounds for believing that'. This implies that one must form a reasonable opinion based on the facts of each case to see what the likelihood would be of the guarantee being called upon in the future so as to constitute it a 'liability' which must be paid as part of the 'liabilities as they become due' (s. 44(1)(c)."

[46] The guarantee had only just been signed and, therefore, it might be said 109, Euro United and GECC were optimistic the financial problems at Euro United had been resolved, however, a more detailed analysis is required. GECC was buttressing its security, as acknowledged by Mr. Feehan. Within two months, equity investors inject $70,000,000 into Euro United and the overadvance is paid in full. The basis for the extra security appears resolved yet GECC does not release 109.

[47] Despite Mr. Feehan's expressed optimism on 15 April 1999, it is clear GECC wanted more security as they were contemplating further default by Euro United. This is the only

conclusion that can be drawn from Mr. Feehan's report on 5 April 1999 "our quickest and easiest exit". There was no acceptable evidence to the contrary and, therefore, I conclude the guarantee must be considered a liability in the solvency test under subsection 20(1)(c). It is also included on the basis it prevented 109 mortgaging the Dielcraft property to fund the construction project.

(c) Subsection 20(3), *Business Corporations Act*

[48] Subsection 20(3) of the Ontario *Business Corporations Act*, as at the relevant time of the events, said:

"(3) Validity of Contract – A contract made by a corporation in contravention of this section may be enforced by the corporation or by a lender for value in good faith without notice of the contravention."

[49] GECC seeks to rely on this safe harbour provision.

[50] It is apparent, on the evidence, GECC did not have actual "notice of contravention." The question is whether it can rely on the representations of Mr. Rehani and its failure to perform a due diligence investigation or, as stated in the subsection, was GECC "a lender for value in good faith."

[51] 109 received no benefit from the guarantee and mortgage. The sole purpose of these documents, as said by Mr. Feehan, was so secure past indebtedness of Euro United. Monies may have been advanced by GECC to Euro United after 15 April 1999 but such was merely a continuation under the revolving letter of credit. Given the subsequent injection of funds by equity investors and the payment of the overadvance, GECC's failure to release 109 clearly demonstrates the purpose of this additional security to cover past indebtedness of Euro United.

Therefore, in my view, GECC was not "a lender for value" within the meaning of subsection 20(3) as it relates to the financial assistance.

[52] Further, failure to conduct a due diligence investigation cannot be used to establish "good faith" in the circumstances of this case. GECC made no attempt to investigate 109 which was inconsistent with their corporate practice as demonstrated in their inquiry in 1998 with respect to the Euro United application for financing. Here, a property inspection would, in a matter of minutes, reveal the construction project on the Dielcraft property and caused further inquiry. The normal request for financial statements would have led to finding the income tax liability. GECC also knew Mr. Rehani was responsible for several covenant breaches which ought to have raised concerns about his honesty.

[53] In this regard, I adopt the comment by Huband J.A. in *Petro-Canada v. Jojef Ltd.*, [1992] M.J. No. 575 (Man. C.A.) where, at p. 2, he said:

> "There is merit in the argument that Petro-Canada cannot turn a blind eye toward the obvious. Moreover, Petro-Canada must be judged, not on the basis of an unsophisticated lender, but as one whose business it is to extend credit on the basis of guarantees. Petro-Canada is aware of the hazards of relying on a guarantee which proves unenforceable by virtue of sec. 42(1). It cannot claim the benefit of sec. 42(3) by ignoring the obvious and neglecting to ask questions."

[54] *Upper Mapleview v. Stolpe Homes (Veterans Drive Inc.)* (1979), 36 B.L.R. (2d) 31 (Gen. Div.), is comparable in many respects to the case at bar. In discussing this issue, Swinton J. also indicated the defendant "should not be held to the same standard of sophistication as Petro-Canada".

[55] GECC is a sophisticated financial institution that well knows the necessity of a due diligence investigation. As such, it cannot rely on the suggestion a solvency certificate satisfies the test. GECC knew enough about the relationship between 109, Euro United and Mr. Rehani that necessitated further inquiry. The evidence clearly indicated GECC made no inquiry, not even a property inspection or search of title, and, further, there was an urgency in completing the transaction.

[56] In this regard, the statement by Carthy J.A. in *Assad v. Economical Mutual Insurance Group*, [2002] O.J. No. 2356 (O.C.A.), at p. 4, is appropriate:

> "Suspicions combined with blindness adds up to an absence of good faith."

[57] Mr. Wayne Gray, in his paper *Corporate Guarantees*, supra, offered this conclusion, at p. 3-39:

> "Thus a prudent lender should not expect to rely on the safe harbour provision. Instead, it will take all steps available to it to ensure that it not only has on notice of the contravention but that it can also, if necessary, produce compelling evidence to a court that the lender addressed its mind to the statutory requirements and reasonably satisfied itself that the corporation providing the financial assistance was not contravening the provisions of its incorporation statute. Unless the lender takes appropriate steps so that it can adduce such evidence should the issue arise in litigation, it will risk encountering significant enforcement difficulties if its primary security from the borrower should become insufficient to meet the borrower's obligations."

[58] GECC took no steps and, therefore, has no evidence to demonstrate its good faith. Reliance on Mr. Rehani's representations and failure to conduct a due diligence investigation was, in my view, willful blindness by GECC.

(d) Summary

[59] In summary, I find 109 failed both the solvency and balance sheet test under subsections 20(1)(c) and (d) and, further, GECC cannot rely on the sale harbour provision of subsection 20(3). Accordingly, I find the mortgage from 109 to GECC is void as against the plaintiffs, as a result of contravention of section 20, *Business Corporations Act*.

(ii) Section 2, *Fraudulent Conveyances Act*
Section 4, *Assignment and Preferences Act*

[60] Although Mr. Rehani did not testify, it is likely he was optimistic, on 15 April 1999, Euro United and 109 would be successful business ventures. Optimism, however, is not evidence of good intentions. The mortgage to GECC, if it stands up, has the actual effect of defeating creditors. An objective analysis of the circumstances is necessary to determine if either, or both, of these statutory provisions apply.

(a) Section 2 *Fraudulent Conveyances Act*

[61] Section 2 of the *Fraudulent Conveyances Act* says:

> "Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns."

[62] The financial circumstances of 109 were identified previously. In April 1999 Mr. Rehani, sole director, officer and shareholder of 109, knowing the financial situation, caused 109 to guarantee the indebtedness of Euro United, a company of which he was the president and controlling shareholder, and to provide collateral mortgage security on its only real asset. Mr. Rehani's actions were facilitated by the willful blindness of GECC. Mr. Rehani was not truthful. He deliberately misrepresented the situation to GECC. GECC failed to make any inquiry.

[63] At issue, therefore, is whether there was an intent to defeat or delay creditors, such as the lien claimants, some of whom had already commenced work on the Dielcraft property by 15 April 1999. There was no direct evidence of intent, however, as West J. said in *Home Savings & Loan Corp. v. Matthews* (1995), 49 R.P.R. (2d) 79 (Gen. Div.), at p. 87, "Intent can be inferred from the surrounding circumstances."

[64] Over the years, the case law has referred to suspicious circumstances demonstrating "badges of fraud": see, for example *Solomon v. Solomon* (1997), 16 O.R. (2d) 769 (H.C.J.) and *Prodigy Graphics Group Inc. v. Fitz-Andrews*, [200] O.J. No. 1203 (S.C.J.).

[65] The evidence established the following, which may be appropriately considered in this analysis:

(i) the conveyance by 109 was in support of a related party, Euro United;

(ii) Mr. Rehani controlled both corporations;

(iii) 109 received no consideration;

(iv) the property conveyed was all of 109's real assets;

(v) 109 had existing and substantial debt such as for income tax, for creditors and was incurring future and substantial liability for creditors regarding the construction project;

(vi) the conveyance was completed with considerable haste, within five days;

(vii) disclosure to GECC was incomplete and in error which could have been discovered upon investigation;

(viii) Mr. Rehani had already committed acts of dishonesty regarding payment on his shareholders loan and acquisition and mortgaging of other property without the consent of GECC;

(ix) The conveyances exceeded the property value;

(x) Euro United was in financial difficulties, having defaulted on the credit agreement within five months of the advance; and,

(xi) There was good reason for GECC and Mr. Rehani to consider Euro United and 109 were insolvent, or about to be.

[66] As Cameron J. said in *Prodigy Graphics*, supra, at p. 22:

> "The badges of fraud are of evidentiary value in determining the issue of intent but are not conclusive evidence of fraud. Fraudulent intent is a matter of fact to be determined in the circumstances of each case or the basis of the evidence as a whole: *Meeker v. Cedar Products v. Edge* (1968), 12 C.B.R. (N.S.) 49 (B.C.C.A.).
>
> Once the suspicious circumstances raise a prima facie presumption of intent to hinder, defeat or defraud a creditor, the court may find the intent unless the presumption is displaced by corroborative evidence of the bona fides of the debtor in the suspect transaction: *Kingsbridge Grand Ltd. v. Vacca*, [1999] O.J. No. 4914 citing *Koop v. Smith* (1915), 51 S.C.R. 554; *Applecrest Investments Ltd. v. Toronto Masonry (1986) Ltd.*, [1997] O.J. No. 436; *Rinaldo v. Rosenfeld*, [1999] O.J. No. 4665."

[67] In *Petrone v. Jones* (1995), 33 C.B.R. (3d) 17 (Gen. Div.), Wright J. at p. 20 provided this comment:

> "In the absence of any direct proof of intention, if a person owing a debt makes a settlement which subtracts from the property which is the proper fund for the payment of those debts, an amount without which the debts cannot be paid then, since it is the necessary consequence of the settlement that some creditors must remain unpaid, it is the duty of the judge to direct a jury that they must infer the intent of the settler to have been to defect or delay his creditors. (*Sun Life Assurance Co. v. Elliott* (1900), 31 S.C.R. 91). …
> Further: even if the plaintiff did not intent to defeat, hinder or delay their creditor but effected the transfer with a view to defeating, hindering or delaying potential future creditors his defence would still fail."

[68] There are strong suspicious circumstances, or badges of fraud, as noted previously. Mr. Rehani knew of the construction project and the cost of same. He knew Euro United was not paying rent to 109. He knew 109 required the property to be mortgaged for the construction

project expense as rent, if paid, was insufficient. He knew 109 already had significant liabilities, particularly for unpaid income tax. In spite of this knowledge, he caused 109 to pledge its only asset to GECC to secure Euro United's existing indebtedness. The only logical inference is that Mr. Rehani used 109 to support the financial difficulties of Euro United and, in so doing, used the property from which the contractors would look for payment.

[69] Therefore, there is, in my view, a prima facie presumption of intent to defeat current and future creditors. GECC is unable to rebut this presumption as they failed to conduct a due diligence investigation and, therefore, had no knowledge, but should have, of the true circumstances on 15 April 1999.

[70] Section 7 of the *Act* says:

> "3. Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge the intent set forth in that section."

[71] 109 received no consideration for the conveyance. In *Courtesy Chevrolet Oldsmobile Ltd. v. Dhaliwal* (1987), 67 C.B.R. 72 (O.S.C.), Austin J. at p. 79 indicated:

> "The jurisprudence makes it clear that where there is no 'good consideration', then the intent of the transferor alone is relevant."

[72] Further, GECC cannot rely on section 3 for the same reasons as with respect to subsection 20(3) of the *Business Corporations Act*. Willful blindness is not good faith.

[73] The plaintiffs argue a conveyance from 109 to Euro United for no consideration would be void under section 2 and, as the conveyance from 109 to GECC has the same effect, it should also be void. I agree. Substance, not form, is the determining factor.

(e) Section 4, *Assignments and Preferences Act*

[74] Subsection 4(1) of the *Assignments and Preferences Act* says:

> "4(1) Subject to section 5, every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects, or of bills, bonds, notes or securities, or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made by a person when insolvent or unable to pay the person's debts in full or when the person knows that he, she or it is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice creditors, or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced."

[75] Subsection 4(1) includes a solvency test. As previously noted, under section 20, *Business Corporations Act*, 109 was, in my view, insolvent on 15 April 1999. 109 was also insolvent as defined in subsection 2(1) of the *Bankruptcy and Insolvency Act*: see also *Robinson v. Countrywide Factors Ltd.* (1977), 23 C.B.R. (NS) 97, at p. 136 (S.C.C.).

[76] On 15 April 1999, 109 had no income and had existing liability for income tax and other debts. Construction work had commenced and there was an outstanding debt to one contractor. 109's liabilities exceeded its assets. The conveyance to GECC compounded 109's insolvency.

[77] The evidence supports a prima facie case for insolvency of 109 and there is, therefore, a presumption of intent to defeat creditors, as noted in the analysis under the *Fraudulent Conveyances Act*. No evidence was presented to rebut the presumption.

[78] Subsection 5(5)(d) of the Act says:

> "Nothing in this Act,
>
> …
>
> (d) invalidates a security given to a creditor for a pre-existing debt where, by reason or on account of the giving of the security, an advance of money is made to the debtor by the creditor in the belief that the advance will enable the debtor to continue the debtor's trade or business and to pay the debts in full."

[79] No advance was made to 109. The pre-existing debt was Euro United's. There was no evidence to suggest any advance to Euro United would enable 109 to continue its business and pay its debts in full. Indeed, the evidence showed otherwise as confirmed by subsequent events. GECC, therefore, cannot rely on subsection 5(5)(d).

(f) Summary

[80] In summary, I find the mortgage from 109 to GECC is void as against the plaintiffs, as a result of contravention of section 2 of the *Fraudulent Conveyances Act* and section 4 of the *Assignments and Preferences Act*.

(iii) Section 78, *Construction Lien Act*

[81] Subsection 78(1) of the *Construction Lien Act* says:

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

Other subsections provide exceptions to this general priority in favour of construction liens. It is, therefore, necessary to determine if the mortgage to GECC is prior or subsequent to the construction liens.

[82] In *Boehmers v. 794561 Ontario Inc.* (1993), 14 O.R. (3d) 781 (Gen. Div.), affirmed (1995), 21 O.R. 771 (O.C.A.), Killeen J. said:

> "Section 78(1) is the overarching principle of the regime of the Act for the determination of priorities. It is, if you will, the central interpretative principle for the adjudication of conflicts of this type before the court in this case. Surely, it necessarily implies that, in cases of conflicts, as here, the burden must be on the mortgagee to persuade the court that it somehow falls clearly within a specified exception to the generalized priority of the liens."

[83] The comment by Rosenberg J. in *697470 Ontario Ltd. v. Presidential Developments Ltd.* (1989), 69 O.R. (2d) 334 (Div. Ct.) is also of assistance where, at p. 337, he said:

> "Accordingly, while the Act may merit a liberal interpretation with respect to the rights it confers upon those to whom it applies it must be given a strict interpretation in determining whether it does in fact apply: *Clarkson Co. Ltd. v. Ace Lumber Ltd.* (1963), 36 D.L.R. (2d) 554 (S.C.C.)"

[84] Before proceeding to consider whether the mortgage was prior or subsequent, a preliminary finding is necessary as to whether there was one improvement or several improvements. "Improvement" is defined in the *Act* as:

> "(a) any alteration, addition or repair to, or
>
> (e) any construction, erection or installation on any land and includes the demolition or removal of any building, structure or works or part thereof, and 'improved' has a corresponding meaning."

[85] Various contractors provided services and materials for 109 at the Dielcraft property at different times. 109 entered into specific contracts with Jannick Electric Limited ("Jannick"), Aim Waste Management Limited ("Aim") and XDG Limited ("XDG"). Numerous subcontractors were also involved.

[86] In the summer of 1998 Mr. Raymond El Jamal, vice-president of Euro United and general manager of 109, began inquiring of contractors and consulting engineers as to renovations of the building located on the Dielcraft property. Several contractors expressed an interest and

provided quotations for various components of the intended project. Contracts were then negotiated with the successful firms.

[87] Jannick was on site in early September or perhaps August 1998 to disconnect electrical services. Aim commenced demolition work on 15 September 1998. Negotiations with XDG continued to January 1999 at which point Mr. El Jamal presented XDG with a draft contract. Giffel's Associates Limited ("Giffels"), 109's consulting engineers, prepared the contract in final form based on the terms as already negotiated. Although the written contract is dated 15 April 1999, it is on the same terms as negotiated and agreed to and, therefore, I find the contract between 109 and XDG was orally entered into in early January 1999.

[88] XDG employees and others were on site on 7 June 1999, however, actual work was commenced on 3 March 1999 when Mr. Wayne Nosal of Design Plus started to prepare the architectural drawings. XDG employees also commenced work on its metal fabrication drawings on the same day.

[89] The ultimate goal of the project was to raise the roof on the building, a large undertaking. XDG was to perform that actual work, however, demolition and electrical disconnection was required before they could commence work on site. In my view, therefore, this appears to be one project, or improvement, not several, as suggested by GECC.

[90] Additional evidence confirms this observation. Aim was initially approached by another contractor in July 1998 to provide a quote for part of the project. 109 eventually contracted directly with Aim on 10 September 1998. Jannick's proposal to 109, dated 28 August 1998,

stated it was "…to assist you in raising of your roof…". Also, the minutes of meeting on 19 November 1998, prepared by Giffels, refers to one project with numerous components.

[91] Accordingly, I find there was one improvement. A comparison can be found in the situation in *Moffatt & Powell Ltd. v. 682901 Ontario Ltd.* (1992), Kirsch's C.L.C.F., 61.3 (Gen. Div.) where Misener J. said:

> "The 'construction' (and therefore the 'improvement') that Kuco undertook on the lands in question here was the erection of a three-storey residence for the elderly that contained 66 separate suites. All 16 lien claimants contracted with Kuco to perform work or services or to supply materials of that 'construction' (and therefore for that 'improvement'). Therefore, all performed work or services in respect of the same 'construction'—and therefore the 'same improvement."

Section 15 of the *Act* says:

> "15. A persons' lien arises and takes effect when the person first supplies services or materials to the improvement."

[92] Jannick was on site to disconnect electrical services, likely in August 1998, however, the evidence was not clear. Aim was on site to commence demolition on 15 September 1999. Therefore, the first lien arose at least by 15 September 1998 and, accordingly, the mortgage from 109 to GECC was a subsequent mortgage, and I so find.

[93] Subsections 78(5) and (6) of that *Act* say:

> "78(5) <u>Special priority against subsequent mortgages</u>—
> Where a mortgage affecting the owner's interest in the premises is registered after the time when the first lien arose in respect of an improvement, the lien arising from the improvement have priority over the mortgage to the extent of any deficiency in the holdbacks required to be retained by the owner under Part IV.
>
> (6) <u>General priority against subsequent mortgages</u>—
> Subject to subsections (2) and (5), a conveyance, mortgage or other agreement affecting the owner's interest in the premises that is registered after the time when

> the first lien arose in respect of the improvement, has priority over the liens arising from the improvement to the extent of any advances made in respect of that conveyance, mortgage or other agreement, unless,
>
> (a) at the time when the advance was made, there was a preserved or perfected lien against the premises; or
>
> (b) prior to the time when the advance was made, the person making the advance had received written notice of a lien."

[94] As previously stated, the mortgage was provided as collateral security with respect to the prior indebtedness of Euro United. No advance was made to 109 nor did 109 benefit in any manner whatsoever. The statutory provisions refer to amounts advanced, not amounts secured: See *561861 Ontario Ltd. v. 1085043 Ontario Inc.* (1998), Kirsh's C.L.C.F. 78.50 (Gen. Div.)

[95] In *Marsil Mechanical v. A Reissing-Reissing Enterprise Ltd.* (1996), Kirsh's C.L.C.F. 78.40 (Gen. Div.), Klowak J. said:

> "In considering the definition of 'advance' it seems to me that, for purposes of the *Construction Lien Act*…it must mean when the owner, or the owner's delegate, acquires actual control of the money."

[96] Accordingly, I find there was no advance under the mortgage from 109 to GECC and, therefore, the lien claimants have priority pursuant to section 78 of the *Construction Lien Act*.

CONCLUSION

[97] KPMG Inc., trustee in bankruptcy of 109, filed a statement of defence in this action but did not participate in the trial for obvious reasons. Representatives of 109 and Euro United were not called as witnesses by the participating parties. The issues dealt with the relationship between those corporations and GECC and, as well, the lien claimants. The plaintiffs were able to establish their case based upon the documents and oral testimony.

[98] In many respects, GECC required testimony of representatives of 109 and Euro United. Although there was sufficient evidence for the findings made, there is a strong argument to also rely on findings of adverse inference as against GECC for failure to call these witnesses.

[99] One theme was central to all issues in this litigation; that is, GECC's failure to perform its usual and customary due diligence investigation with respect to 109. There was no satisfactory answer for this neglect. GECC is a sophisticated lending institution. It normally performs due diligence. Was its failure to do so an oversight or was GECC scrambling to gain additional security for a customer they knew was on the edge of failure?

[100] It would be unconscionable and inequitable to allow a mortgagee to obtain priority based upon its willful blindness or negligence. Even the simplest of investigations would have revealed the construction project and led GECC to make further inquiry. They would easily have determined Mr. Rehani was not being truthful.

[101] A due diligence investigation would, in my view, have led GECC to decide against mortgage security on the Dielcraft property.

[102] A trial of issues was directed to determine the priority as between the lien claimants and the mortgagee. There were secondary issues that arose during the trial pertaining to the validity and quantum of some liens. Those issues were beyond the scope of the trial.

[103] In result, the plaintiffs are entitled to a declaration the lien claimants have priority over the mortgage from 109 to GECC, subject to proof as to validity and quantum of the liens for which a further trial, if necessary, is directed.

[104] If the parties cannot agree on the issue of costs, written submissions are required. The party seeking costs shall serve such submissions within 28 days of the release of this decision. The responding party shall have 14 days to serve submissions and a further 7 days is allowed for reply. All written submissions are to be filed by the last day for reply.

_____

D.J. GORDON J.

Released: December 23, 2002

TAB 9

Ontario Supreme Court
Mutual Trust Co. v. Stornelli[1]
Date: 1996-05-14

Mutual Trust Co.

and

Stornelli et al.

XLO Investments Ltd.

and

Hurontario Management Services et al.

Court File Nos.: 92-CQ-047294 & 92-CU-060159

Ontario Court (General Division), Sharpe J. November 29, 1995 and May 14, 1996[2].

S. Cumming, for plaintiff, Mutual Trust Company.

S. Braithwaite, for plaintiff, XLO Investments Limited.

S. Dewart and R. Muir, for defendants, Granab Inc. and Hurontario Management Services.

[1] SHARPE J. (orally):—I will now give judgment in these two actions which were tried together before me. Both actions attack the conveyance of the home of the defendants, Ivy Stornelli and Luigi Stornelli, to the defendant Granab Inc., referred to in this trial as the "All Saints property," as being contrary to both the *Fraudulent Conveyances Act* and the *Assignments and Preferences Act.*

[2] In the XLO Investments Limited action there is also an attack on a mortgage on the All Saints property held by the defendant in that action, Hurontario Management Services Inc., and as well a claim for damages for conspiracy arising out of the refinancing and restructuring of the XLO security in 1991.

[3] The defendants Ivy and Luigi Stornelli did not defend these actions. They have been noted in default. Neither testified at the trial.

[4] The evidence before me is that Mr. Stornelli is a tailor by profession but an active speculator in real estate and that indeed he is a somewhat sophisticated real estate investor with a lengthy history of buying and selling properties, both on his own account through corporate entities and in various partnerships with other investors.

[1] Notices of appeal filed in the Ontario Court of Appeal (Court File No. C23530).

[5] The other defendants, Granab Inc., Hurontario Management Services, acted through Grant Kerr. Mr. Kerr is a solicitor and has been a member of the bar since 1971. He also is a very active real estate investor and developer, an activity he has engaged in since 1964, primarily in the Mississauga and west-end area. It is clear that he has years of experience and a wealth of knowledge in this area.

[6] Mr. Kerr indicated that he had known the Stornellis for some twenty years and that he saw Mr. Stornelli socially. While he had had no business dealings with Mr. Stornelli, he had frequently acted for Mr. Stornelli as a solicitor in connection with various of Mr. Stornelli's purchases and sales of real estate. Indeed Mr. Kerr had acted on the purchase of the All Saints property in 1988 and he also acted when there was a transfer of that property to Ivy Stornelli in 1991, which I will describe shortly.

[7] Mr. Kerr has an interest in several corporate entities involved in the real estate industry. The defendant Granab Inc. is a family holding company. Mr. Kerr and his wife are the two shareholders in that company. Hurontario Management Services Limited is a licensed mortgage broker and Mr. Kerr has a 20 per cent interest in that company. Another Hurontario company involved in this matter, Hurontario Real Estate Inc., is a licensed real estate agent and Mr. Kerr has a 49 per cent interest in that company. Its role is often to assist Mr. Kerr's various companies in marketing properties, collect commissions, act as agent on powers of sale. Mr. Kerr was the only witness called by the defendant.

[8] The plaintiff, Mutual Trust Company, had held a mortgage on a commercial property owned by the Stornellis at 83 Lakeshore Road East in Mississauga. Ivy Stornelli was a covenantor on that mortgage; Luigi Stornelli was guarantor. The principal amount of the mortgage was $325,000. The evidence is that that mortgage was in default in September 1991 with some $350,000 owing. Mutual took steps to collect and summary judgment was obtained in April of 1992. The property was sold in October of 1992 for the sum of $285,000. Accordingly, Mutual has a deficiency still owing to it in the amount of approximately $100,000 when one includes interest fees and other expenses taken in connection with the sale.

[9] It was conceded in argument and in evidence that Mutual took reasonable efforts to collect its debt but that those efforts have yielded little, if anything, and that it has not been able to enforce the judgment against either Ivy or Luigi Stornelli.

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[2] Received June 19, 1996.

[10] The plaintiff, XLO Investments Limited, at the relevant time was a licensed mortgage broker which invested in mortgages on behalf of clients. The mortgages were held in the name of XLO on behalf of or as trustee for these investors. XLO originally held two mortgages on the All Saints property. It gave a $200,000 mortgage to assist in the purchase of the property in 1988. In 1990 it gave a second mortgage in the amount of $50,000 which was later increased to $100,000, so that there was a total of $300,000 in mortgages held by XLO on the All Saints property. That debt was restructured in 1991. I will come to the details of that, but the result was that XLO was partly paid at that time. The balance owing went immediately into arrears and there is still an amount of $142,000 outstanding that XLO has not been able to collect, As a result of the restructuring of the debt, Mrs. Stornelli is liable for that amount.

[11] The Stornellis purchased the property in question in April 1988 at a price of $335,000. As I have indicated, the purchase was partially financed by a $200,000 mortgage arranged by XLO. Title at the time was taken in the name of Mr. Stornelli's company, Luigi Stornelli Limited. In 1991 title to that property was transferred to Ivy Stornelli. The evidence is that this was apparently done for tax reasons.

[12] In October of 1991, the Stornellis sought to rearrange their mortgage financing on the house. They arranged a first mortgage with First Line Trust, the terms of which provided that $185,000 would be advanced; that there be no other mortgage on the property; and that there be no principal or interest payable for three years. In other words, the mortgage is what was described in evidence as a reverse mortgage in that it provided for no ongoing payments and the amount owing under the mortgage accordingly increased each month, the evidence is, by approximately $2,000 per month. As a result of that, XLO was paid $185,000 on its mortgage and it agreed to take a second mortgage in the amount of $100,000 on the 83 Lake Shore property. Mrs. Stornelli was covenantor and Mr. Stornelli guarantor.

[13] There was also a fourth mortgage in the amount of $40,000 on another commercial property owned by the Stornellis at 85 Lakeshore. The title to that property was held by Luigi Stornelli Investments Limited. Mrs. Stornelli and Mr. Stornelli were both guarantors on that mortgage. The Stornellis went into immediate default on these mortgages shortly after this was arranged in October of 1991, and the evidence before me is that XLO is still owed some $140,000, plus interest. As I have indicated, XLO did advance a conspiracy claim alleging that

the restructuring arrangement that I have just described was fraudulent and that Hurontario Management and the Stornellis and the other defendants in that action were parties to that conspiracy.

[14] It is clear that in late 1991 the Stornellis were experiencing significant financial problems. The real estate market was falling and, as I have indicated, they were in default on both the Mutual mortgage and on their obligations to XLO.

[15] In December of 1991 they decided to list the All Saints property and they did so with Century 21 Miller Real Estate at an asking price of $399,000. There is no evidence that any offers were received.

[16] On January 10th the Mutual Trust statement of claim in its mortgage action was served and Mr. Stornelli went to see Mr. Kerr. It is clear that Mr. Stornelli was having financial difficulties at that time. It is also clear from the evidence that Mr. Kerr was aware of this, not only from his conversation with Mr. Stornelli but also because two days prior he had signed a power of sale on behalf of Hurontario with respect to the mortgage it held on the 85 Lake Shore property.

[17] Mr. Kerr's evidence is that Mr. Stornelli asked him if Hurontario or one of Mr. Kerr's clients or companies would be interested in a mortgage on the All Saints property. Mr. Kerr says that he told Mr. Stornelli he would look into that. At the same time, it is clear that they discussed the Mutual Trust statement of claim and mortgage action. Mr. Kerr referred Mr. Stornelli to his law firm's litigation department with respect to a defence in that action.

[18] Mr. Kerr's evidence was that shortly thereafter, having reviewed the situation with the people at Hurontario, he reported to Mr. Stornelli that the best he could do would be a $45,000 mortgage providing for prepaid interest for a year and after deduction of that prepaid interest and fees, there would be a net pay out to Mrs. Stornelli, who was the covenantor, of $36,000. Mr. Kerr says that the conversation at that point turned to the possibility of a sale of the property.

[19] It was his evidence that the Stornellis decided that they wanted to sell the property and they asked Mr. Kerr if he would be able to assist them. He testified that he knew of none of his clients who would be interested in the property but that he decided he would buy it for himself. At one point in his evidence he said he was contemplating moving into the house

because of a marital split-up. At a later point in his evidence he said that he really was buying the property for resale.

[20] Mr. Kerr's evidence is that he thought the property at this time was worth between 280 and $290,000. He looked at the various encumbrances on the property. He was concerned about the First Line mortgage because he felt there would be a substantial penalty in connection with that mortgage. He considered the Hurontario mortgage that had been agreed to, and his evidence is that he put what he described as a take it or leave it offer to the Stornellis of $262,000. He says that he told them to get independent legal advice and the next day the Stornellis agreed to this sale.

[21] It is clear that Mr. Kerr's evidence is that he was buying this property because he thought he could make a profit. That agreement of purchase and sale was signed on January 28th, the same day the second mortgage to Hurontario Management Services Inc. of $45,000 was registered. Two days later, Mr. Kerr's law firm filed a notice of intent to defend in the Mutual Trust action, and on February 10th, the transaction closing the sale of the All Saints property to Mr. Kerr's company, Granab Inc., was closed.

[22] The details of that transaction are that there was, as I have indicated, a stated purchase price of $262,000. The statement of adjustments was submitted in evidence and it indicates that a commission was paid to Mr. Kerr's real estate company, Hurontario Real Estate, in the amount of approximately $17,000. Mr. Kerr admitted that this was a high commission and he also admitted that this provided him with a reduced cost base on the property for tax purposes.

[23] The Stornellis were not credited on this transaction for the $6,300 advance payment that had been deducted from the advance on the Hurontario mortgage. Mr. Kerr's evidence is that that was simply an error that no one noticed until the discovery in this action. The evidence indicates that the land transfer tax and certain disbursements were paid from an account in Mr. Kerr's firm which was the trust account for the Stornellis. Again, Mr. Kerr says this was a mistake and his evidence is that the money was not the Stornellis' but money that came from him. The arrangement also provided for a lease back of the property to the Stornellis at a rent of $1,850 per month. The first and last month's rent was taken from what is described as the proceeds of the sale.

[24] Mr. Kerr in his evidence denied that there was any other benefit to the Stornellis. His explanation of the transaction is simply that they felt very pressed, that they wanted to relieve themselves of the obligation they held on the mortgages on the property. There was, he agreed, however, no assumption agreement, nor was there any indemnity, and it is clear that the Stornellis remained liable on both mortgages.

[25] On the same day the transaction to Granab closed, the Stornellis' statement of defence to the Mutual Trust action was served. Some time thereafter Mutual Trust served a motion for summary judgment, and at that point Mr. Kerr's firm went off the record. The summary judgment motion went undefended and summary judgment was granted in favour of Mutual Trust on April 2nd, 1992.

[26] Mr. Kerr's evidence was that in July, Mr. Stornelli came to him indicating that he was having difficulty paying the rent and thought that he should move to a smaller property. At that point, Granab listed the property for sale using the same agent the Stornellis had used, Miller Real Estate, and at the same asking price, namely $399,000.

[27] At the end of July an offer was received from Mr. Appleton in the amount of $340,000. Mr. Kerr's evidence was that he was anxious to sell the property. However, he did sign that offer back at $389,000. There was nothing further until August 19th when a second offer came, this time in the name of Mrs. Appleton. The offer at that point was in the amount of $368,000. There were a series of offers and counter-offers and finally the price settled on was $375,000. Mr. Kerr was able to agree to that price, he said, because the agent agreed to forgo $5,000 commission.

[28] The transaction was permitted to proceed notwithstanding the certificates of pending litigation obtained in these actions in connection with the property by virtue of orders of Justice Garton and Justice Moldaver. These orders provided that the certificates of pending litigation could be lifted; that the proceeds of the transaction after discharge of the mortgage and after payment of the usual fees and disbursements be paid into court. The transaction did close on October 9th and an amount of $77,512.14 was paid into court pursuant to the orders of Justices Garton and Moldaver.

[29] I turn to an analysis of the claims that have been advanced here. I will deal first with the conspiracy claim, which I should indicate was also pleaded in the Mutual Trust action.

However, counsel made it clear in that action that he was not pursuing that claim. It does remain before me in the XLO action, although I think it fair to say that it was not strongly pursued.

[30] In my view, there is no evidence upon which a finding of a conspiracy could be made. Mr. Kerr denied any knowledge of the First Line deal. There is no evidence to suggest that he was implicated in that deal; no evidence linking either him or his companies, and accordingly I find no basis upon which to support a finding of conspiracy or the claim for damages on that account.

[31] With respect to the attack on the sale of All Saints and XLO's attack on the Hurontario mortgage, as I have indicated, both the *Assignments and Preferences Act* and the *Fraudulent Conveyances Act* are relied on. The relevant provisions of those two statutes are as follows. The *Assignments and Preferences Act,* R.S.O. 1990, c. A.33, s. 4(1) provides as follows:

> 4(1) Subject to section 5, every gift, conveyance, assignment or transfer, delivery over or payment of goods, chattels or effects, or of bills, bonds, notes or securities, or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made by a person when insolvent or unable to pay the person's debts in full or when the person knows that he, she or it is on the eve of insolvency, with intent to defeat, hinder, delay or prejudice creditors, or any one or more of them, is void as against the creditor or creditors injured, delayed or prejudiced.

[32] The relevant provisions of the *Fraudulent Conveyances Act,* R.S.O. 1990, c. F.29, are sections 2, 3 and 4 which provide as follows:

> 2. Every conveyance of real property or personal property and every bond, suit, judgment and execution heretofore or hereafter made with intent to defeat, hinder, delay or defraud creditors or others of their just and lawful actions, suits, debts, accounts, damages, penalties or forfeitures are void as against such persons and their assigns.
>
> 3. Section 2 does not apply to an estate or interest in real property or personal property conveyed upon good consideration and in good faith to a person not having at the time of the conveyance to the person notice or knowledge of the intent set forth in that section.

4. Section 2 applies to every conveyance executed with the intent set forth in that section despite the fact that it was executed upon a valuable consideration and with the intention, as between the parties to it, of actually transferring to and for the benefit of the transferee the interest expressed to be thereby transferred, unless it is protected under section 3 by reason of good faith and want of notice or knowledge on the part of the purchaser.

[33] The ingredients of these claims that I have to consider are, with respect to the *Assignments and Preferences Act,* whether Ivy Stornelli was insolvent within the meaning of that Act and with respect to both Acts, whether there was an intent to defeat, hinder, delay or prejudice creditors on her part in connection with this transaction.

[34] With respect to the *Fraudulent Conveyances Act,* I also have to consider whether Granab Inc. has a defence under the terms of sections 3 or 4. Granab asserts that it gave good consideration in good faith without any knowledge of any intent on the part of Ivy Stornelli to defeat creditors.

[35] I will deal first with the XLO attack on the Hurontario mortgage. In my view, there is no basis upon which this transaction can be set aside or voided under these provisions. The evidence is that the money was placed by an independent investor. The money was advanced and security was given, and I see simply no basis upon which that mortgage can be set aside.

[36] I come then to what really forms the focus of the trial and that is the validity of the sale of the All Saints property. I will look first at the question of insolvency and the application of the *Assignments and Preferences Act.* It will be noted that the definition of insolvency in the statute is a broad one. The statute covers the situation where a person is either, in its words, “insolvent” or “unable to pay the person’s debts in full or when the person knows that he, she or it is on the eve of insolvency”.

[37] In my view, it can be inferred from the evidence, and the plaintiffs have established, on a balance of probabilities that Ivy Stornelli was insolvent within the meaning of the Act at the time of this transaction. It is clear that both the Stornellis were pushed to the wall at the time this transaction was entered into. There is evidence that they were in default on the

mortgages to XLO and Mutual since the fall of 1991 and that power of sale proceedings had been taken on the Hurontario mortgage.

[38] In my view, the evidence established that they had ceased to meet their obligations and liabilities at this time. There is as well the after the fact evidence that Mutual made reasonable efforts to collect on the debt and it could not. I am satisfied that once Mrs. Stornelli disposed of the All Saints properties, there was really nothing left to satisfy her creditors.

[39] Counsel for the defendants argues that more detailed evidence of insolvency was required; that there should be some detailed assessments or statement of the assets and liabilities of Mrs. Stornelli, and that the evidence was insufficient. Counsel also contended that as the plaintiffs, Mutual and XLO, shortly before this point thought that they were well secured and that they would be paid and that as everyone was surprised with the rapid decline of properties, that it does not lie in their mouths to say that Mrs. Stornelli was insolvent. Counsel also relies on the evidence that Mutual did not follow up on a rather oddly worded letter Mr. Kerr wrote regarding the possible sale of the Lake Shore property as indicating that at this time they thought everything was well secured. In my view, neither of these two arguments is valid and I reject both.

[40] With respect to the question of the nature of evidence required, counsel cited the case of *Re Van der Liek* (1970), 14 C.B.R. (N.S.) 229 (Ont. S.C.), a decision of Mr. Justice Houlden. In that decision, Mr. Justice Houlden states—and this is the passage counsel referred to—that [at p. 231]:

> The court will not presume insolvency. It must be proved and if it is not, then the application must be dismissed.

[41] However, if one reads on in the decision, Mr. Justice Houlden says this, and I am quoting from the same page at 231:

> The usual method [of how to prove insolvency] is to call two or three creditors whose claims were overdue at the date of the preference. It might be possible for the trustee to prepare a balance sheet to show insolvency within the meaning of s. 2(j)(iii) but from my own experience, the records of a bankrupt are usually in such a state that this is very difficult and the method I have suggested is usually the most convenient way of establishing insolvency.

[42] Here we have evidence of two creditors whose claims were not being met and were not being paid at the time of this transaction and I am satisfied that adequate evidence has been offered.

[43] With respect to what was or was not in the minds of the plaintiffs as to the likelihood of their debts being paid by the Stornellis, it is my view that what is really at issue here is not what was in their minds but what was in the minds of Mr. Stornelli, Mrs. Stornelli and Mr. Kerr. It is clear that they were in a much better position to assess that situation than were the plaintiffs.

[44] It is clear that they were not meeting their obligations, and it is clear that they entered a very strange transaction at this point. From all of that evidence it is my view that adequate proof of insolvency has been made to satisfy the test set out in the *Assignments and Preferences Act*

[45] The second issue, and this applies both to the *Assignments and Preferences Act* and to the *Fraudulent Conveyances Act,* is whether this transaction was done with an intent to defeat the claims of creditors. Again, it is my view that the plaintiffs have satisfied the burden on them to establish that the intent of Ivy Stornelli in entering into the transfer of the All Saints property to Granab Inc. was to defeat the claim of her creditors. It is true that there is no direct evidence of intent, but it is clear from the case law that evidence of such intent can be inferred from the circumstances. In this case there are several bases upon which that inference can be drawn.

[46] The plaintiffs rely on the cases of *Sun Life Assurance Co. of Canada v. Elliott* (1900), 31 S.C.R. 91 (S.C.C.), and *Freeman v. Pope* (1870), 5 Ch. App. 538 (Ch. C.A.) at 541, for the proposition that if the consequence of a transaction is to put the property beyond the reach of creditors and hinder or defeat their claims, the Court may apply what really amounts to a common sense presumption that the parties are presumed to intend the natural consequences of that act.

[47] Now, it is also clear that from subsequent case law that that is rebuttable if there is evidence of an honest purpose, and the cases which say that are *Mandryk v. Merko* (1971), 19 D.L.R. (3d) 238 (Man. C.A.), a decision of the Manitoba Court of Appeal, and *Holbrook v. Cedpar Properties Inc.* (1986), 62 C.B.R. (N.S.) 18 (Ont. H.C.J.), a decision of Justice White.

[48] In my view, no such credible evidence has been offered here. The circumstances of this transaction are so unusual that an explanation is called for. It is my view, and I find, that the transaction is inexplicable for any other reason than that it was undertaken to defeat the claims of Mrs. Stornelli's creditors. The transaction clearly did not satisfy the purpose that Mr. Kerr said it had in his evidence. The result of the transaction was not to relieve either Mr. or Mrs. Stornelli of their obligations under the mortgage. There were, as I have said, no assumption agreement or assignments; they remained legally liable. Moreover, the result of the transaction was to significantly worsen the Stornellis' cash flow situation for the following reasons.

[49] Under the mortgage they had arranged, they could have stayed in the house without making any payments for a fairly substantial period. As a result of this transaction, they became obliged to pay rent to Granab Inc. in the amount of $1,850 per month. In effect, the result of the transaction was that Mrs. Stornelli got nothing for a property that had a very substantial equity. Moreover, if this was a serious business transaction, it is simply incredible to me that the Stornellis would not have noticed the failure to credit them with $6,300 in prepaid interest on a mortgage that was being completed virtually at the same time. Moreover, it is hard to imagine why they would have incurred the cost of that mortgage, the brokerage and legal fees, plus the prepaid interest if this was all part of a genuine transaction, as suggested by the defendants. It is my view that the transaction itself and what it yielded to the Stornellis was so unusual and so difficult to understand that it called for an explanation.

[50] The Stornellis, as I have indicated, were not called as witnesses. There is a well-known rule of evidence that an adverse inference can be drawn when a witness with direct knowledge of the facts is not called when that witness was available and could have been called and no explanation has been given as to why the witness was not called.

[51] In argument, counsel for the defendants suggested that I should draw an adverse inference against the plaintiffs because the Stornellis were not called. He submitted that the reason that the inference should go against the plaintiffs rather than against his client was that the plaintiffs bore the burden of proof on the issue of intent. I do not accept that argument and I refer to the book, Sopinka and Lederman, *The Law of Evidence in Civil Cases* (Toronto: Butterworths, 1974). I am referring here to the first edition, 1974. This subject does not

appear to be dealt with in the second edition, but I do refer to the first edition at page 537 where the authors state as follows, and I quote:

> The rule is not restricted in its application to the plaintiff or other party who has the ultimate burden of proof. Failure on the part of a defendant to testify or to call a witness, once a *prima facie* case has been made out against the defendant, may be the subject of an adverse inference.

[52] In my view the circumstances of this transaction raise a prima facie case. It is entirely understandable why the plaintiffs would not call the Stornellis. They are, after all, codefendants who have been sued. The plaintiffs are alleging wrongdoing on their part. If this were a legitimate transaction, as suggested by the defendants, I would expect the defendants to call the other parties to that transaction, the Stornellis, to explain why it was legitimate and what exactly its purpose was. The Stornellis were not called and I am entitled to draw an adverse inference from that fact as to their intent.

[53] I would also refer, as basis for the inference I have drawn, to what is called in the case law “the badges of fraud.” I rely here on a discussion of this subject in Sprigman, *Fraudulent Conveyances and Preferences* at pages 13-15 and following.

[54] The circumstances of the present case feature several of these so-called badges of fraud. First, this appears to have been the conveyance of all the property owned by Ivy Stornelli. Second, she remained in possession of the property despite the conveyance. The effect of the transaction was really to allow the Stornellis to stay living in their house while sheltering it from the reach of their creditors.

[55] Third, the conveyance was made directly in the face of the Mutual Trust statement of claim. Mutual Trust was clearly closing in on the Stornellis. In my view, it is straining credulity beyond the breaking point to consider that the almost exact proximity of time of the service of the statement of claim, the filing of a very thin defence and the conveyance to Granab were mere coincidence. It is clear that an inference can be drawn that the statement of claim and the imminence of almost certain judgment in that action were what prompted this conveyance.

[56] Fourth, the deed here makes false statements as to the consideration. The stated price in the deed and the other documents is $262,000, but that price is substantially inflated. A significant part of it was made up of the $17,000 commission Hurontario Realty received and,

as I have indicated, $6,300 of prepaid interest should have been deducted. The actual amount is more like 238 or $240,000 when these amounts have been deducted.

[57] Fifth, there was a very close relationship between Mrs. Stornelli and Mr. Stornelli and Mr. Kerr. This was not an arm's length arrangement. It was a transfer by a client to a corporation owned and controlled by a solicitor, and that solicitor bore a fiduciary relationship to his client.

[58] Sixth is the question of inadequacy of consideration. The purchase by Granab Inc. was described by counsel for the defendant as a "highly leveraged purchase." In my view, this is a charitable description. The fact of the matter is Granab Inc. gave virtually nothing for this property. At best, it appears that there was a $1,000 deposit and that the Granab may have paid the land transfer tax and certain disbursements. Even Mr. Kerr recognized in his evidence that there was a substantial equity here. He said he would not have bought it if he did not think he could turn a profit.

[59] It is my view that his evidence that he estimated the price at the time of the transaction between 280 and $290,000 is not credible. The value of this property, in my view, was substantially higher, as evidenced first by the actual sale of the property in August. The defendants throughout the trial took the position that the best test of the value of a property is what a willing buyer will pay.

[60] Secondly, appraisals submitted by the defendant which were prepared for this litigation indicate an estimated value of $320,000 in January and $310,000 in August, the date of the purchase, significantly higher than Mr. Kerr's appraisals. I note that these were drive-by appraisals based on comparative sales, and Mr. Kerr is an extremely experienced and sophisticated dealer in real estate in this area and that this information would have been the sort of information he would have had.

[61] Third, Mr. Kerr's own actions indicate that he in fact valued the property at more than $280 or $290,000. When he listed the property he used the asking price of $399,000, he says, because it had been listed for that. But he also said that he was looking for a quick sale on the property and it is surprising that he would list the property at $399,000 if he really thought it was only worth $280 or $290,000. There is also the fact that he signed back an offer of $340,000. Again, if he really thought the value was $280 or $290,000, it is hard to

imagine why he would risk signing back an offer that was that much over what he says he thought the property was worth.

[62] Accordingly, it is my view that looking at what Granab gave for the property, which was virtually nothing, what it got, which was a very substantial asset, the consideration was grossly inadequate. When we look at the other side of the transaction to what Mrs. Stornelli received, it is clear that she received basically nothing.

[63] The statement of adjustments indicates a payment to her of $1,500, but she had to pay legal fees on the transaction. There is no evidence of what they were, but that was the amount that Mr. Kerr's firm charged in the transaction, and accordingly it would be surprising if she was left with anything more than a few hundred dollars.

[64] As I indicated, she was given no relief from the legal obligation on the covenant and guarantee and she incurred an obligation to pay rent. Accordingly, it is my view that the consideration here was grossly inadequate, given the overall effect of this transactions. From all of those "badges of fraud," I infer an intent to defeat the claims of creditors.

[65] I then come to the final point under the *Fraudulent Conveyances Act,* and that is does Granab Inc. have a defence sections 3 or 4 of that Act? I have just dealt with the question of sufficiency of consideration. There is also the question of good faith or want of knowledge of intent on the part of Granab. This clearly requires me to make a finding as to Mr. Kerr's credibility.

[66] Counsel urges me to decide the case on the basis that as an officer of the court, I should accept his evidence. I regret to say that I simply cannot accept that submission. Considering all of the evidence, the details of the transaction which I have already reviewed, as well as Mr. Kerr's demeanour in the witness-box, I find that his evidence was less than candid and that it was simply not believable on many points.

[67] Mr. Kerr's denial that he knew the Stornellis were insolvent is simply not credible. He himself had just signed powers of sale of their other property. He clearly knew about the Mutual Trust action. He clearly knew that the Stornellis were being severely pushed, and he wrote a letter on January 21, 1992 when getting a release of another agent's commission to allow his company to secure commission referring to their financial difficulties.

[68] I find his evidence that he thought the 85 Lake Shore property would produce sufficient proceeds to cover the Mutual Trust action not credible. It is surely odd that he would be so very wrong in connection with that estimate in one direction and so very wrong in the other direction as to the actual value of the All Saints property. I am simply not satisfied that Mr. Kerr was offering his candid views as to the values of these properties, and that is clearly relevant with reference to his opinion as to the solvency of Mrs. Stornelli.

[69] Secondly, for reasons already given, Mr. Kerr's defence in his evidence of the transaction as a legitimate business arrangement not intended to defeat creditors is simply not credible. The effect of the transaction did not accomplish the purpose Mr. Kerr said it had, namely, to relieve the Stornellis of their obligations under the mortgage, as they remained liable, and it substantially worsened their cash flow position in that they were now obliged to pay rent to stay in a house they could have remained in without any payment, given the terms of the mortgages.

[70] I also find his explanation that the omission or failure to credit the Stornellis with the $6,300 was simply a mistake implausible if this were in fact a genuine transaction. It is also odd to say the least that Mr. Kerr would have used the Stornelli trust account if in fact this were a genuine transaction. I also find it hard to give credit to his evidence as to the manner in which he and his firm handled the defence to the Mutual Trust action. He testified that he thought the Stornellis had a defence to that action and yet he also testified that he did not know what happened or why his firm had gone off the record. He testified that he never discussed the situation with his partner, nor did he try to follow up the question of their defence. This is difficult to give credence to. Accordingly, it is my view that given the nature of this transaction, the inference I have drawn with respect to the intent of Mrs. Stornelli in carrying it through, the findings I have made as to Mr. Kerr's credibility with respect to his knowledge and on the basis of the inadequacy of the consideration given, that no defence has been made out under sections 3 or 4 of the *Fraudulent Conveyances Act.*

[71] The defence also argues that it must be shown that the debtor received or retained some benefit from the transaction. Counsel cites the cases of *Mulcahy v. Archibald* (1898), 28 S.C.R. 523 (S.C.C.), and *Re Panfab Corp. Ltd.* (1970), 15 C.B.R. (N.S.) 20, 17 D.L.R. (3d) 382 (Ont. H.C.J.). Counsel relies on the passage from the *Mulcahy* case at 529 which is as follows:

> …it has been decided over and over again that knowledge on the part of such a transferee of the motive or design of the transferor is not conclusive of bad faith or will not preclude him from obtaining the benefit of his security. So long as there is an existing debt and the transfer to him is made for the purpose of securing that debt and he does not either directly or indirectly make himself an instrument for the purpose of subsequently benefiting the transferor, he is protected and the transaction cannot be held void.

[72] In my view, that case and the *Panfab* case are distinguishable from the situation before me. In the first place, it is clear that in both cases good and valid consideration was given. In both cases there was a debt that was either being paid or secured and that all that was happening is that a creditor was being paid for something he was owed or being secured with respect to money lent. Those cases were in effect preference cases and it was not a situation of a debtor putting property beyond the reach of his creditors.

[73] The situation here is very different. This is not a situation of an alleged preference. This is a situation where I have found the consideration was inadequate and, moreover, that the purpose of the transaction was to put the property beyond the reach of creditors. In that situation, applying the language of the statute, it is my view that there is no requirement for proof of a tangible benefit being retained by the debtor if the circumstances of the statute have been satisfied, and I have found that they have been.

[74] Moreover, if I am wrong in that regard and a benefit has to be found, it is my view that it would not be at all unreasonable to infer that there must have been some benefit, either explicit or implicitly promised to the Stornellis. I make that inference despite Mr. Kerr's denial that the Stornellis received any benefit. A transaction of this kind by sophisticated business people is simply not explicable on any other ground. Moreover, if it were necessary to find a benefit retained, it is also possible to find another benefit; namely, the Stornellis got to remain in the house that they would almost certainly have been put out of had the transfer not taken place. The transaction had the effect of allowing them to remain there while shielding the house from their creditors.

[75] Accordingly, for the foregoing reasons, I find that the transfer of the All Saints property did contravene the provision of section 4 of the *Assignments and Preferences Act* and as well that it was a fraudulent conveyance within the meaning of section 2 of the *Fraudulent*

Conveyances Act. It follows from that and from the orders that were made by Justices Garton and Moldaver that the proceeds now in court should be made available to satisfy the claims of the plaintiffs.

May 14, 1996.

RULING AS TO COSTS

[76] Grant Kerr, a solicitor, is the directing mind of the defendant, Granab Inc. Evidence at trial established that Granab was a holding company and that Kerr and his wife were the only two shareholders. In my reasons for judgment, I found that the impugned conveyance from Ivy Stornelli to Granab Inc. was in contravention of the *Fraudulent Conveyances Act* and the *Assignments and Preferences Act* and that the net proceeds of that conveyance, having been paid into court pursuant to interlocutory orders, should be paid out to the plaintiff creditors of Ivy Stornelli.

[77] It is clear that Kerr designed and carried out the impugned transaction on behalf of Granab and that had the scheme succeeded, he would have benefited personally. Granab pleaded the defence of good faith and want of notice or knowledge of the circumstances making this a fraudulent conveyance and relied on Kerr's evidence in that regard. Counsel for Granab was instructed in these proceedings by Kerr. Counsel urged me to accept Kerr's evidence on the basis that Kerr was "an officer of the court". This proved to be a highly inappropriate appeal to Kerr's alleged integrity. In my reasons for judgment, I found that Kerr's conduct in this proceeding fell far below the standard expected of an officer of the court. I rejected Kerr's evidence as being less than candid and not believable on the crucial points in issue.

[78] The plaintiffs are plainly entitled to their costs of the action, but ask that I make an order requiring Kerr to pay those costs personally.

[79] While it is exceptional to order costs against a non-party, there is jurisdiction to do so in certain circumstances. In my view, an order that Kerr personally pay the costs of this action may be justified on two related grounds.

[80] First is the "straw man" principle established in *Re Sturmer and Town of Beaverton* (1912), 2 D.L.R. 501 (Ont. Div. Ct.) (at 506 per Middleton J.):

> …the Court always had the power to award costs against the real applicant when the motion was made by him in the name of a man of straw for the purpose of avoiding liability. The Courts were never so blind as to be unable to see through the flimsy device nor so impotent as to be unable to act.

[81] *Sturmer* has been followed in a number of reported cases, most recently in *Smith v. Canadian Tire Acceptance Ltd.* (1995), 36 C.P.C. (3d) 175 (Ont. Ct. (Gen. Div.)); affirmed C.A. Nov. 8, 1995; see also *Ridgely (in trust) v. Ridgely Design Inc.* (1991), 3 O.R. (3d) 695 (Ont. Ct. (Gen. Div.)); *Yared Realty Ltd. v. Topalovic* (1981), 45 C.P.C. 189 (Ont. H.C.J.); *Assaf v. Koury* (1980), 16 C.P.C. 202 (Ont. H.C.J.).

[82] In all of the cases to which I have been referred, the order requiring a non-party to pay costs has been made against an individual who initiated proceedings, using a “straw man” plaintiff as a shield to costs. Can the same principle be applied where the order is sought against an individual who stands behind a “straw man” defendant?

[83] In most cases, the answer is bound to be no. Defendants do not initiate litigation, and the rationale of *Sturmer* and the cases which follow it turns on controlling those who invoke the process of the court but seek by deception to shield themselves from that very process. Moreover, in the case of corporate litigants, the distinct identity of the corporation from its shareholders, even in the case of a “one man company” will ordinarily be respected: *Rockwell Developments Ltd. v. Newtonbrook Plaza Ltd.* (1972), 27 D.L.R. (3d) 651 (Ont. C.A.); *Quabbin Hill Investments Inc. v. Rowntree* (1993), 19 C.P.C. (3d) 113 (Ont. Ct. (Gen. Div.)); *R.L. Wilson Engineering and Construction Ltd. v. Metropolitan Life Insurance Co.* (1988), 32 C.P.C. 76 (Ont. H.C.J.).

[84] However, in my view, the circumstances of the present case do justify the order sought. While the action was not brought by Kerr in the name of Granab, he did initiate the transaction which required these proceedings and that transaction was directly related to the process of this court. That transaction, I have found, was intended to defeat the process of the court in that its effect was to put assets beyond the reach of a judgment creditor. In my view, it is a logical and permissible extension of the *Sturmer* principle to hold that those who use a “straw man” to defeat the process of the court and thereby provoke litigation may be held liable for the costs of such litigation.

[85] Even if the *Sturmer* principle alone were insufficient to warrant the order sought, there is a second and related reason for ordering for costs against Kerr. It is Kerr's position that only Granab can be held liable as the named party to this suit and that the separate corporate identity of Granab must be respected. However, there is authority for piercing the corporate veil in circumstances such as those present before me. In a recent decision of the Ontario Court of Appeal, *Gregario v. Intrans-Corp.* (1994), 18 O.R. (3d) 527 at 536, 115 D.L.R. (4th) 200 (Ont. C.A.), Laskin J.A. stated that a corporation may be found to be the alter ego of its beneficial owner, resulting in liability of the owner, "to prevent conduct akin to fraud that would otherwise unjustly deprive claimants of their rights." *Lockharts Ltd. v. Excalibur Holdings Ltd.* (1987), 47 R.P.R. 8 (N.S.S.C.T.D.) considers the application of the principle that a company is a legal entity distinct from its shareholders in relation to conveyances intended to defeat creditors. After a detailed review of the authorities, Davison J. concludes as follows (at p. 19):

> A Judge should not "lift the veil" simply because he believes it would be in the interest of "fairness" or of "justice"… On the other hand, the Courts have the power, indeed the duty, to look behind the corporate structure and to ignore it if it is being used for fraudulent or improper purposes or as a "puppet" to the detriment of a third party.
>
> …
>
> The purpose of the corporate entity was not to defraud or mislead others including creditors and shareholders and in my opinion where a company is being used for this purpose the "veil" should be lifted and a remedy made available to the victims of such conduct.

[86] It is clear from the findings I have made in this case that Granab was the alter ego of Kerr and that Kerr caused Granab to engage in "conduct akin to fraud that would otherwise unjustly deprive claimants of their rights." It follows that Kerr should not be able to shelter behind Granab to avoid liability for the costs of this action.

[87] I have been asked to fix the costs of the action. In my view the bill of costs submitted by counsel for Mutual Trust is a reasonable one, although pursuant to the order of Garton J. lifting the certificate of pending litigation and ordering the net proceeds paid into court, there are to be no costs of that motion. Accordingly, I fix the costs of Mutual Trust at $12,895 for fees and disbursements of $1,473.89.

[88] In the XLO action, it is submitted that Hurontario Management Services should be awarded costs in view of the failure of the claim against it. However, Hurontario is another company in which Kerr has a substantial interest and it was represented throughout by the same counsel. Moreover, the claim against Hurontario was not, as noted in my reasons, strongly pursued. In my view, the appropriate course is to make a modest reduction to the costs of XLO on account of the failure of its claim against Hurontario. The draft bill of costs of XLO asks for a larger amount than was sought in the Mutual Trust action. I can see no basis for fixing costs in a higher amount, and in light of the Hurontario claim, I fix the costs of XLO in that action at $12,000 for fees and disbursements of $907.58.

[89] For the foregoing reasons, the plaintiffs are entitled to judgment for those costs against both Granab Inc. and Grant Kerr.

Judgment for plaintiffs.

Court File No. CV-18-598657-00CL

DONALD DAL BIANCO	and	**DEEM MANAGEMENT SERVICES LIMITED and THE UPTOWN INC.**
Applicant		Respondents

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

Proceeding commenced TORONTO

RECEIVER'S BRIEF OF AUTHORITIES

(motion for directions regarding the third mortgage and other relief, returnable November 21, 2019)

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