

2024

Hfx No. 538745

SUPREME COURT OF NOVA SCOTIA

BETWEEN:

IN THE MATTER OF THE *COMPANIES CREDITORS ARRANGEMENT ACT*, RSC 1985, C C-36, AS AMENDED (THE “**CCAA**”)

AND IN THE MATTER OF AN APPLICATION OF BLUE LOBSTER CAPITAL LIMITED, 3284906 NOVA SCOTIA LIMITED, 3343533 NOVA SCOTIA LIMITED AND 4318682 NOVA SCOTIA LIMITED (COLLECTIVELY, THE “**APPLICANTS**”)

BRIEF OF AUTHORITIES

August 26, 2026

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IN THE MATTER OF THE COMPANIES CREDITORS
ARRANGEMENT ACT, RSC 1985, C C-36, AS AMENDED (THE
“CCAA”)

AND IN THE MATTER OF AN APPLICATION OF BLUE
LOBSTER CAPITAL LIMITED, 3284906 NOVA SCOTIA
LIMITED, 3343533 NOVA SCOTIA LIMITED AND 4318682
NOVA SCOTIA LIMITED (COLLECTIVELY, THE
“APPLICANTS”)

BRIEF OF AUTHORITIES

1. *Gerrow v Dorais*, [2010 ABQB 560](#).
2. *House v Baird*, [2019 ONSC 1712](#).
3. *Green v Bank of Montreal*, [1999 CanLII 821 \(ON CA\)](#).
4. *Re Griffon Partners Operation Corporation*, [2024 ABKB 277](#).
5. Matti Lemmens, Jakub Maslowski and Heather Cattell, “The Marshalling Plan for Junior Creditors” 22 Annual Review of Insolvency Law, [2024 CanLIIDocs 3047](#).
6. *Wolfe et al v Taylor et al*, [2020 MBCA 44](#).
7. *Allison (Re)*, [1995 CanLII 7146 \(ON CTGD\)](#).
8. *807933 Ontario Inc. v. Paddon and Associates*, [1998 CanLII 3766 \(ON CA\)](#).
9. *Williamson v Loonstra et al*, [1973 CanLII 1186 \(BC SC\)](#).
10. *Governor and Company of the Bank of Scotland v Nel (The) (T.D.)*, [1998 CanLII 9082 \(FCTTD\)](#).
11. *Strategic Acquisition Corp v Multus Investment Corporation*, [2013 ABQB 534](#).
12. *Bear Creek Contracting Ltd v Canadian Western Bank*, [2026 NLSC 13 \(CanLII\)](#).
13. *Brown v Canadian Imperial Bank of Commerce et al*, [1985 CanLII 2116 \(HC\)](#).
14. *Transamerica Life Insurance Company of Canada v Canada Life Assurance Company*, [1996 CanLII 7979 \(ON CTGD\)](#).
15. *Re Griffon Partners Operation Corporation*, [2024 ABCA 279](#).

TAB 1

Court of Queen's Bench of Alberta

Citation: Gerrow v. Dorais, 2010 ABQB 560

Date: 20100903
Docket: 0903 13412
Registry: Edmonton

Between:

Anthony Ford Gerrow

Plaintiff

- and -

**Michel Joseph Dorais, Hinton Pine Holdings Inc., Hinton Leaf Holdings Inc.,
1033543 Alberta Ltd., Hinton Sky Inc., Green Holdings Inc., Hinton Green Inc.,
Growth Partners Inc., Capitalplus Financial Inc., Zenith Capital Investment Corp.,
and Dorais Financial Inc.**

Defendants

**Reasons for Judgment
of the
Honourable Mr. Justice Don J. Manderscheid**

I. Introduction

[1] This matter arises out of three Notices of Motion involving the respective rights of a Court appointed receiver and various secured creditors and the equitable doctrines of marshalling, apportionment and subrogation. As well, this matter involves the application of the *Statute of Elizabeth (Fraudulent Conveyances Act)*, 1571 (13 Eliz. 1) c. 5, and the *Personal Property Security Act*, R.S.A. 2000, p-20. Counsel for 805251 Alberta Ltd. advised the Court that his client was not proceeding with their claim under the *Fraudulent Preferences Act*, R.S.A. 2000, F-24.

[2] Essentially this case asks whether a debtor, who owns several mortgaged properties, can transfer title of the mortgaged properties to a non-arms length corporation, have that corporation pay a portion of the debtor's debt to a primary debtor as a guarantor, and then have that corporation seek subrogation from the sale of property, depriving secondary mortgage holders on some of the property of their ability to realize on their security. It also asks whether lien and caveat holders can seek a division of the monies realized from the sale of the properties with the secondary mortgage holders.

II. Facts

[3] The material facts surrounding this matter are as follows:

1. 1033543 Alberta Ltd. (103), Hinton Pine Holdings Inc. (Hinton Pine), and Hinton Leaf Holdings Inc. (Hinton Leaf), are all Alberta corporations. With the exception of a few hours during the course of Rollover Agreements described below, the sole shareholder and director of 103, Hinton Pine, and Hinton Leaf was Michel Dorais, who died in 2009.
2. 103 purchased three commercial properties in Hinton, Alberta:
 - (a) Lots 1, 2, 3, Block 2, Plan 7823286, (Lots 1,2,3);
 - (b) Lot 4, Block 1, Plan 0325182, (Lot 4); and
 - (c) Lot 8, Block 2, Plan 0625170, (Lot 8).
3. 103 borrowed money from the Alberta Treasury Branch (ATB). The ATB indebtedness was comprised of various demand loans totalling of \$1.6 million as at September 8, 2009.
4. ATB filed a General Security Agreement against 103 at Personal Property Registry on October 15, 2008 covering all present and after acquired property of 103. ATB also registered as a continuing collateral security for the ATB indebtedness collateral mortgages up to the principle sum of :
 - (a) \$1 million dollars at the North Alberta Land Registration District Office, (LTO), against the title to Lot 4 on October 6, 2004 as instrument number 042438868.
 - (b) \$535,000.00 at LTO against the title to Lots 1, 2,3, on November 12, 2003 as instrument number 032437572.

- (c) \$500,000.00 at LTO against the title to Lot 8 on February 21, 2007 as instrument number 072103522.

7. 805251 Alberta Ltd. (805), is an Alberta Corporation. It entered into a mortgage agreement with 103, which was registered at LTO against the title to Lot 4, as instrument number 072152496 on March 16, 2007. Funds were advanced to 103 and at April 13, 2010 there was \$387,106.94 owing to 805 on the mortgage.

8. 805 filed a General Security Agreement covering all present and after acquired personal property at the Personal Property Registry against 103 on January 14, 2009.

9. Cedar Peaks Mortgage Investments Inc. (Cedar Peaks), is an Alberta corporation which entered into a mortgage agreement with 103. That mortgage was registered at the LTO against title to Lot 8 as instrument number 082 333 031 on August 9, 2008. Funds were advanced to 103 and at September 21, 2009 there was owing on that mortgage \$796,001.74.

10. Cedar Peaks filed a General Security Agreement covering all present and after acquired personal property at the Personal Property Registry against 103 on July 30, 2008.

11. On or about September 1, 2008 103 transferred title to Lots 1,2,3 to Hinton Pine, and title to Lot 4 to Hinton Leaf. Mr. Dorais caused the transfers to take place pursuant to Rollover Agreements after he obtained tax advice. The agreements did not involve cash changing hands. Mr. Dorais did not tell the creditors of 103 about the Rollover Agreements and the transfers of land to Hinton Pine and Hinton Leaf.

12. When ATB learned of the transfers, they threatened to take action unless Hinton Pine and Hinton Leaf executed Guarantees of the ATB indebtedness. The Guarantees were subsequently executed by Hinton Pine and Hinton Leaf.

13. After Mr. Dorais died, the monthly mortgage payments on Lots 1,2,3, Lot 4 and Lot 8 were not made. ATB commenced foreclosure actions in respect of each of the Lots as follows:

- (a) Lot 1,2, 3, Action No.: 0903 11949;
- (b) Lot 4, Action No.: 0903 11948;
- (c) Lot 8, Action No.: 0903 11950.

14. Cedar Peaks commenced a foreclosure action on its mortgage against Lot 8 in action number 0903 13066.

15. Anthony Ford Gerrow was appointed Receiver of all Defendants in action number 0903 13412 by Justice Bielby on August 27, 2009 for the purpose of examining the affairs of Mr. Dorais and the Defendants to determine what assets might be available to satisfy the outstanding claims of the creditors against the Defendants, Mr. Dorais and various companies owned by him including Hinton Pine.

16. The Receiver has confirmed that there are approximately \$5 million dollars in outstanding unsecured claims. In his capacity as Receiver, the Receiver has collected \$31,996.73 from the rentals of Lots 1,2,3 paid to the Receiver under an agreement between ATB and the other secured creditors and this Court. The Receiver has also collected GST on the rents payable, however in most cases because the rentals were paid by the Government of Alberta, no GST was payable. The GST collected on account of the rental payments totals \$12,257.57.

17. On September 21, 2009 Justice Bielby granted an Order Nisi in the three ATB foreclosure actions, and the properties were listed for sale under judicial listings. ATB obtained a Preservation Order for all three properties and hired a Preservation Agent, Lyle Stewart, to look after all three properties.

18. Lots 1,2,3 sold first; an Offer for \$1,200,000 was approved by Justice Bielby on November 19, 2009 and Lots 1,2,3 sold for that amount. Lot 4 sold next; an Offer for \$980,000 was approved by Justice Bielby on February 25, 2010, and Lot 4 sold for that amount. Lot 8 sold last; an offer for \$965,000 was approved by an Order of Master Wacowich dated March 22, 2010, and Lot 8 sold for that amount.

19. The Town of Hinton has a claim against the proceeds from the sale of Lot 4, and it filed a Caveat claiming an interest under an agreement to pay offsite levies dated November 30, 2007 between 103 and Hinton. The Caveat was registered against the title to Lot 4 as instrument number 092407573 on November 12, 2009.

20. D.C. Electrical Services Ltd. and Hinton Plumbing and Heating Ltd., (collectively referred to as the Lien Holders), performed work and supplied materials in regards to Lot 8. Pursuant to the *Builder's Lien Act*, R.S.A. 2000, c. B-7, the Lien Holders registered builders' liens against the title to Lot 8 as instrument numbers 092 244 946 and 092 206 728, respectively. The amount of the respective builders' liens of the Lien Holders is \$88,753.00, for D.C., and

\$6,634.00 for Hinton Plumbing.¹ Lot 8 serves as the only recourse for the Lien Holders for payment of their registered liens.

21. The ATB indebtedness was fully paid out from the rental proceeds, the sale of Lots 1,2,3, up to the mortgage amount of \$535,000.00, and the remaining indebtedness was paid out from the sale of Lot 4. The ATB indebtedness had been fully repaid by the time Lot 8 was sold.

22. There was another secured creditor, Grant Dewar, who was paid out of the proceeds and who is not a party to these Actions. After this, there still remained funds totalling \$391,275.17 resulting from the proceeds of the judicial sale of Lots 1,2,3. As mentioned above, ATB had required Hinton Pine to execute a Guarantee in favour of ATB of the ATB indebtedness of 103. ATB obtained judgment on the Guarantee against Hinton Pine and filed a Writ against the interest of Hinton Pine against the title to Lots 1,2,3 at the LTO as instrument number 092 422 087.

23. At the time Lot 4 sold, ATB was still owed \$612,398.31, plus solicitor-client costs and the preservation agent's fees. When Lot 4 sold, the lawyer for ATB received net sale proceeds of \$877,327.74 after payment of realtor fees. ATB paid out of these funds as follows:

a)	Realty Taxes on Lot 4	\$ 10,872.32
b)	ATB Indebtedness	\$612,398.31
c)	Preservation Agent account for Lot 4 and Lot 8	\$ 26,846.63
d)	ATB solicitor-client account	\$ 16,725.13
e)	ATB solicitor-client account	\$ 5,658.49
f)	Balance into Court	\$253,376.86

24. The outstanding amount on the 805 mortgage on Lot 4 at April 13, 2010 was \$387,106.94.

25. The amount outstanding on the Cedar Peaks mortgage on Lot 8 on September 21, 2009 was \$796,001.14, and as of June 4, 2010 was \$897,516.74.

¹ There is an encumbrance on title by O.K. Tire Stores Inc. registered on Lot 8, but it does not secure any indebtedness and need not be considered as per the advice of Maurice Blain, counsel for O.K. Tire Stores Inc.

26. The net proceeds of the sale of Lot 8 were \$889,334.10.
27. Paragraph 9 of Justice Bielby's September 21, 2009 Order states that the Court will consider an application for:

... the distribution of the remaining funds, whether the equitable doctrine of marshalling would apply that would affect the payment or distribution of the net sale proceeds amongst the Subsequent Encumbrancer(s) or would entitle any one or more of the Subsequent Encumbrancer(s) to be subrogated under any of ATB's mortgage security registered against any of the other Lands so as to equitably cause the sale proceeds to be distributed amongst the priority claimants to the Lands.

As of March 22, 2010 all lands described in Justice Bielby's order were sold.

III. Issues

- [4] The issues to be decided are:
- (a) Is the Receiver entitled by virtue of the equitable doctrine of subrogation to step into the position of the ATB in regards to the payment of \$391,275.17 to the ATB pursuant to the Guarantee given by Hinton Pines to the ATB?
 - (b) If the answer to the question in sub paragraph (a) above is in the affirmative, then does the equitable doctrines of marshalling or alternatively apportionment operate to defeat the Receiver's right of subrogation *vis-a-vis* any claim by 805, Cedar Peaks, the Lien Holders, the Town of Hinton, or any other secured creditors?
 - (c) If the answer to the question in sub paragraph (a) above is in the negative, then to what extent does the doctrine of marshalling or alternatively apportionment, apply to the respective claims made by 805, Cedar Peaks, the Lien Holders, the Town of Hinton, or any other secured creditors?

IV. Cases

1. Subrogation

[5] The Receiver argues that he is subrogated to ATB rights because of Hinton Pine's Guarantee of 103's indebtedness to ATB, and which indebtedness was paid and totalled \$391,275.17.

[6] Basically speaking, the equitable doctrine of subrogation allows one party to stand in the shoes of another and advance any claims that the original party may have had against another party: **Alberta (Treasury Branches) v. Alberta (Public Trustee)**, 2002 ABQB 781, 7 Alta. L.R. (4th) 110. Subrogation is simply asking something in the right of another, which in justice and equity, should be accorded to the person asking: **Goldsmith v. Stewart**, (1885) 45 Ark 149 (C.A.) 154. Application of the doctrine enables:

... the substitution of one person in place of another, whether as a creditor, or as the possessor of any other rightful claim so that he who is substituted succeeds to the rights of the other in relation to the debt or claim and its rights, remedies, or securities.

Leavitt v. C.P.R., (1897) 37 Atl 886, at 888, right column, 90 Maine 153 (C.A.).

[7] Although there is an abundance of Canadian authorities that have considered this doctrine, none appear to have analogous fact situations to this case. For this reason, and as each case is to be determined on its own particular facts, a review of the doctrine and the jurisprudence germane to its application is therefore required.

[8] A concise historical overview of the equitable doctrine of subrogation was provided in **E C & M Electric Ltd. v. Medicine Hat General and Auxiliary Hospital and Nursing Home District No. 69** (1987), 76 A.R. 281, 35 D.L.R. (4th) 80 (QB) where Lomas J. in discussing the origins of the doctrine of subrogation quoted *Halsbury's Laws of England* (4th ed.) Volume 20 para. 193 and Volume 16 para. 1438:

193. **Surety's right of subrogation.** As soon as the surety has paid to the creditor what is due to the creditor under the guarantee, he is entitled, unless he has waived them, to be subrogated ... to all the rights possessed by the creditor in respect of the debt, default or miscarriages to which the guarantee relates.

1438. **Doctrine of subrogation.** Where one person has a claim against another, in certain circumstances a third person is allowed to have the benefit of the claim and the remedy for enforcing it, even though it has not been assigned to him, and he is then said to be subrogated to the rights of the first person.

[9] The authors, Meagher, Gummow and Lehane in *Equity: Doctrines and Remedies* (2nd ed.) (Sydney: Butterworth's, 1984) at page 251 quote from ***John Edwards & Co. v. Motor Union Insurance Co. Ltd.*** [1922] 2 KB 249 at 252 discussing the origin of the doctrine:

It was derived by our English Courts from the system of Roman law...The doctrine has been widely applied in our English body of law, eg to sureties and to matters of *ultra vires* as well as to insurance. In connection with insurance it was recognized ere the beginning of the eighteenth century. In ***Randal v Cockran*** (1748) 1 Ves Sen 98; 27 ER 916, it was held that the plaintiff's insurers after making satisfaction stood in the place of the assured as to goods, salvage, and restitution in proportion for what they paid. As the Lord Chancellor (Lord Hardwicke) said: "The plaintiffs had the plainest equity that could be".

[10] Goff and Jones in *The Law of Restitution* (2nd ed) (London: Sweet and Maxwell., 1978) note that a contracting party may reserve a right of subrogation or specifically exclude or limit it. However, they note that since the 17th century, the case law has held that subrogation arises independently of, and "not by force of", contract and will be granted if it is just and equitable to do so. They conclude (at page 406):

Subrogation is the "plainest equity that could be"; its basis is a "principle of natural justice". As Buckley L.J. recently said: "The doctrine of subrogation does not ... rest on contract at all. It is an equitable doctrine".²

[11] More recently, the doctrine of subrogation was addressed by our Court of Appeal in ***Rainbird Sprinkler Manufacturing Co. (Canada) Ltd. v. Elpat Holdings Ltd.*** (1996), 187 A.R. 222, 42 Alta. L.R. (3d) 328 (CA) where the Court, in discussing the application of subrogation in terms of the position of a guarantor held that the guarantor, although not the principal debtor, was entitled to be paid as he stepped into the shoes of the creditor and was entitled to pursue its remedies and realize on its security on the basis of equitable principles. The Court went on to quote G.H.L. Fridman, *Restitution*, (2nd ed.) (Scarborough, Ont.: Carswell, 1992) at pp. 402-3 (at para. 12) :

A surety who pays off the debt to the principal creditor owed by the principal debtor is entitled to succeed to all claims which the principal creditor has against the debtor in order to prevent an unjust enrichment. The surety stands in the place of the creditor not as a matter of contract but by operation of law. Hence, he is entitled to every remedy which the creditor might have enjoyed against the

² See also Maudsley, *Hanbury's Modern Equity* (8th ed.) (London: Stevens & Sons Ltd., 1969) at page 429; Sidney Arthur Taylor Rowlatt, *Rowatt on The Law of Principal and Surety* (4th ed.), (London: Sweet & Maxwell, 1982) at page 145; George W. Brandt, *The Law of Suretyship and Guaranty* (3rd ed.) (Chicago : Callaghan & Co., 1905) at page 613.

debtor. This includes the right by subrogation to enforce every security and all means of payment.

... Thus mortgage securities held by a creditor under a mortgage must be transferred to the surety on payment of the debt. The surety, when making such payment, is presumed to keep the mortgage alive for his own bene-fit.

[12] The Court of Appeal continued at para. 13 to quote the *Mercantile Law Amendment Act*, 1856, 19 & 20 Vict., c. 97, s. 5 as also supporting the right. It states:

Every Person who, being Surety for the Debt or Duty of another, or being liable with another for any Debt or Duty, shall pay such Debt or perform such Duty, shall be entitled to have assigned to him, or to a Trustee for him, every Judgment, Specialty, or other Security which shall be held by the Creditor in respect of such Debt or Duty, whether such Judgment, Specialty, or other Security shall or shall not be deemed at Law to have been satisfied by the Payment of the Debt or Performance of the Duty, and such Person shall be entitled to stand in the Place of the Creditor, and to use all the Remedies, and, if need be, and upon a proper Indemnity, to use the Name of the Creditor, in any Action, or other Proceeding, at Law or in Equity, in order to obtain from the principal Debtor, or any Co-Surety, Co-Contractor, or Co-Debtor, as the case may be, Indemnification for the Advances made and Loss sustained by the Person who shall have so paid such Debt or performed such Duty, and such Payment or Performance so made by such Surety shall not be pleadable in bar of any such Action or other Proceeding by him: Provided always, that no Co-Surety, Co-Contractor, or Co-Debtor shall be entitled to recover from any other Co-Surety, Co-Contractor, or Co-Debtor, by the Means aforesaid, more than the just Proportion to which, as between those Parties themselves, such last-mentioned Person shall be justly liable.

[13] In the case of a mortgage, the doctrine of subrogation applies only in a situation where there is a payment that in effect discharges the earlier mortgage in circumstances where fairness justifies that the payor stand in the shoes of the first mortgagee as if he or she had taken an assignment: *Investors Group Trust Co. v. Crispino* (2006), 17 B.L.R. (4th) 282, 147 A.C.W.S. (3d) 1069 (Ont. Sup. Ct. Just.) at para. 35.

[14] Master Laycock in *Bank of Montreal v. Suitor*, 2009 ABQB 203 addressed subrogation in the context of registered security interests holders' priorities (at paras.14-15):

Secondly, the plaintiff argues that the plaintiff becomes subrogated to the position of Home Trust as first mortgagee and therefore has priority to the respondent. The Ontario Court of Appeal in *Midland Mortgage Corp. v. 784401 Ontario Ltd.* (1997), 34 O.R. (3d) 594, 12 R.P.R. (3d) 14, 102 O.A.C. 226 (Ont. C.A.) discussed the doctrine of subrogation. Firstly the court determined that the doctrine of subrogation applies to the Land Titles system. Next they accepted the

statement of law as contained in **Crosbie-Hill v. Sayer**, [1908] 1 Ch. 866 (Eng. Ch. Div.) at page 877:

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

Under the doctrine of subrogation the plaintiff has priority to the caveat for the amount advanced to retire the Home Trust mortgage but not the full amount of its advance. To the extent that the plaintiff did not receive an amount equal to the payout of the Home Trust mortgage it is entitled to those funds from the monies currently being held in trust.

[15] Equity will not permit a party to be barred recourse to the doctrine of subrogation on the basis that there may exist some technical prohibition against subrogation. In this respect, in **Harris, et al. v. Carnegie, et al.**, [1933] O.R. 844; [1933] 4 D.L.R. 760, (C.A.), Davis J.A. held that plaintiffs who acted as solicitors for both the mortgagors and mortgagees and were parties to the mortgage were persons in a position analogous to a surety and were bound, as between themselves and the mortgagees, to pay the taxes on the mortgagors' default. At paras. 5 and 6:

This is a common example of a compulsory payment to the use of another, and an action lies for moneys so paid by reason of the implied contract of indemnity. The cases are conveniently collected in Halsbury, (2nd ed.), vol. 7, p. 263, para. 365.

Upon the evidence in this case the plaintiffs paid the money under such circumstances as to entitle them to recover the amount as having been paid for the defendants' use. In any event the plaintiffs are entitled to be subrogated to the rights of the mortgagees, and the mortgagees are bound to allow the plaintiffs to use their names to enforce payment of these moneys and, this being a Division Court suit, to be determined by "equity and good conscience" (sec. 55, Division Courts Act, R.S.O. 1927, ch. 95) no technical defect should be allowed to defeat the justice of the claim.

[16] Furthermore, in **Morrison v. Canadian Surety Co.**, [1954] 12 W.W.R. (N.S.) 57, [1954] 4 D.L.R. 736 (Man.C.A.), Coyne J.A. in discussing a parties' entitlement to subrogation stated at para. 117:

Brooks Wharf and Bull Wharf Ltd. v. Goodman Bros., [1937] 1 K.B. 534, 106 L.J.K.B. 437 (C.A.) is a case where an importing firm placed valuable furs in a bonded warehouse from which they were stolen without fault of the warehousemen. The latter were called upon by the revenue authorities to pay the customs duty under the terms of their bond. Having done so, they sued to recover

the amount from the importers who were primarily liable for the duty. The court held them entitled to succeed. Lord Wright, at 545, says:

The obligation is imposed by the Court simply under the circumstances of the case and on what the Court decides is just and reasonable, having regard to the relationship of the parties. It is a debt or obligation constituted by the act of the law, apart from any consent or intention of the parties or any privity of contract.

[17] The doctrine of subrogation came into existence for the express purpose of rendering justice where an injustice would otherwise be permitted. Confirmation of this conclusion can be seen in **Morrison v. Canadian Surety Co.**, where Coyne J.A. stated at para. 114:

The term "subrogation", which in ordinary language as well as in legal parlance means "substitution", has appeared in English law for a long period. First it was applied at common law in favour of an insurer in a policy of indemnity and gradually extended to other fields. It had a wider reach in Equity. It was invented as a means to avoid injustice by enabling a person, not previously entitled, to sue in law or equity by giving him a status to assert against a person or property a claim recognized as fair and just but not maintainable as a contractual or tortious claim. It was a device necessary to avoid injustice, by imposing on the unjust, as a matter of law or equity, an obligation *quasi ex contractu* to do right where no obligation *ex contractu* existed. It was first adopted without realizing the broader conception of *quasi-contract*.

[18] The right of a party to seek equitable relief is always subject to the equitable maxim of "He who comes into equity must come with clean hands". The equitable doctrine of subrogation is no exception. In **De Jesus v. Shariff**, 2010 BCCA 121, 284 B.C.A.C. 243, Finch C.J.B.C., in discussing the conduct of a party that would justify a refusal by the Court of equitable relief cited I.C.F. Spry in *The Principles of Equitable Remedies*, (6th ed.) (at pp. 169-170) (UK: Sweet & Maxwell, 2001) at para. 86:

...it must be shown, in order to justify a refusal of relief, that there is such an "immediate and necessary relation" between the relief sought and the delinquent behaviour in question that it would be unjust to grant that particular relief. ... So it was once emphasised "that general fraudulent conduct signifies nothing; that general dishonesty of purpose signifies nothing; that attempts to overreach go for nothing; that an intention and design to deceive may go for nothing, unless all this dishonesty of purpose, all this fraud, all this intention and design, can be connected with the particular transaction, and not only connected with the particular transaction, but must be made to be the very ground upon which the transaction took place, and must have given rise to this contract".

[19] Furthermore, “under the doctrine of subrogation, all of the circumstances must be balanced, and the Court must be satisfied that no injustice will be done through the substitution of one party in the place of another via a subrogation arrangement”, **Alberta (Treasury Branches) v. Alberta (Public Trustee)**, at para. 50, Cairns J., quoting **Brown v. McLean**, (1889), 18 O.R. 533 (H.C.J.), at 536.

[20] Lastly, in **Coupland Acceptance Ltd. v. Walsh**, [1954] S.C.R. 90, [1954] 2 D.L.R. 129, the Supreme Court of Canada confirmed that the doctrine of subrogation is not confined to matters of priority between mortgages, but applies as well to the relationships between mortgages and other prejudicial instruments such as builders' liens and executions. In this respect, Kellock J., stated (at para. 6):

While s. 13(1) of *The Mechanics Lien Act*, R.S.O., 1950, c. 227, gives priority to the lien over all payments or advances made under a mortgage after registration of the lien, the section is not to be construed as affecting the right relied upon here by the appellant. The appellant does not rely upon its mortgage for priority as to the moneys here in question but upon the equitable right to stand in the place of the Kerbel mortgagees whose priority to the lien is unquestionable. The position of the lienholder remains the same as it was before the appellant intervened and it would, in my opinion, require more than is to be found in the section to bring about a result so unjust that it would, to paraphrase the language of Parker J., in the **Crosbie-Hill** case, permit the lienholder, by a mere accident, to obtain priority at the expense of people who never intended to benefit him. Had the appellant been in fact aware of the registration of the lien, it could have purchased the Kerbel mortgage, in which event no possible question could have arisen.

2. Marshalling

[21] In its simplest form the doctrine of marshalling dictates that if a creditor has two funds to draw upon to satisfy the debt, the Court will require him to take satisfaction from that fund upon which another creditor has no security. In Alberta, the seminal case on the doctrine of marshalling is **First Investors Corp. v. Veeradon Developments Ltd.** (1988), 84 A.R. 364, 47 D.L.R. (4th) 446 (Alta. C.A.). In that case, Belzil J.A., in explaining the doctrine of marshalling, noted that the leading formulation of the doctrine of marshalling as a principle of equity is that of Lord Hardwicke in **Lanoy v. The Duke and Dutchess of Athol** (1742), 2 Atk. 444. At p. 669 Lord Hardwicke held that if a creditor has two funds, he must take his satisfaction from the fund that has no lien by another creditor. He went on:

Suppose a person, who has two real estates, mortgages both to one person, and afterwards only one estate to a second mortgagee, who had no notice of the first; the court, in order to relieve the second mortgage, have directed the first to take his satisfaction out of the estate only which is not in mortgage to the second mortgagee, if that is sufficient to satisfy the first mortgage, in order to make room

for the second mortgage, even though the estates descended to two different persons.

[22] Belzil J.A. went on to adopt the formulation in *Snell's Principles of Equity*, (28th Ed), by P.V. Baker and P. St.J. Langan (London : Sweet and Maxwell, 1982) at p. 416, which provides that where there are two creditors of the same debtor, and one creditor has a right to resort to two funds for payment of his debt, and the other a right to resort to one fund only, the court will 'marshal' or arrange the funds so that both creditors are paid as far as possible. The authors of *Snell's* noted that the doctrine has several applications, but marshalling as between mortgagees is perhaps the most usual. *Snell's* continues that the doctrine of marshalling is not allowed to prejudice the first mortgagee. Relying on the Blackacre/ Whiteacre formula, *Snell's* noted:

If, for instance, a person having two estates, Blackacre and Whiteacre, mortgages both estates to A, and afterwards mortgages only Blackacre to B, either with or without notice of A's mortgage, the proper course is for A to realise his debt first out of Whiteacre and to take only the balance out of Blackacre, in order to leave as much as possible of Blackacre to satisfy B... A can therefore realise his securities as he pleases, for A is not a trustee for B. But if A pays himself out of Blackacre, B is allowed to resort to Whiteacre to the extent to which Blackacre has been exhausted by A, and to have the same priority against Whiteacre as A had.

...In the above example, B's right to marshal will be enforced not only against the original mortgagor but also against all persons claiming through him as volunteers, as where the mortgagor dies and Blackacre and Whiteacre pass to different persons. But it is not allowed to prejudice purchasers or mortgagees of one of the estates. Thus if in the above example the mortgagor had created another mortgage of Whiteacre in favour of C. B would have no equity to throw the whole of A's mortgage on Whiteacre, and so destroy C's security."

[23] Belzil J.A. also accepted the definition of marshalling from the judgment of Orde, J. in ***Ernst Brothers Co. v. Canada Permanent Mortgage Corporation*** (1920), 47 O.L.R. 362, affirmed 48, O.L.R., 57 D.L.R. 500 (C.A.) that include the following qualification at para. 22:

... This right is always subject to two important qualifications: first, that nothing will be done to interfere with the paramount right of the first mortgagee to pursue his remedy against either of the two estates; and, second, that the doctrine will not be applied to the prejudice of third parties.

[24] Belzil J.A. further noted that these definitions speak of "satisfaction" or "payment of the first mortgage debt out of marshalled "funds". In ***Canada Permanent Trust Company v. King Art Developments Ltd. et al.*** [1984], 4 W.W.R. 587, 54 A.R. 172 (CA) Laycraft, J.A. at para. 45 adopted the following definition of "satisfaction" in *Black's Law Dictionary* (at p. 643):

... the discharge of an obligation by paying a party what is due to him (as on a mortgage, lien or contract), or what is awarded to him by the judgment of a court or otherwise.

[25] The most important qualification in these definitions is that the application of marshalling cannot prejudice the "paramount" right of the first mortgagee to realize its securities and pursue its remedies as it pleases. That primary right to receive and enforce payment of its debt in money is at its election. The first mortgagee thus may seek a "Rice" order, take the land by final foreclosure, or pursue other courses of action such as simply leaving its security in force. Belzil J.A. noted in **First Investors Corp. v. Veeradon Developments Ltd.** that the consequence of this is that if the right is not to be prejudiced, it follows that the prerequisite to applying marshalling to mortgages is that first mortgage properties have all been sold and converted to money funds exceeding the amount due under the first mortgage. He continues:

In those circumstances, the first mortgagee must pay itself firstly out of the funds derived from the properties not covered by the second mortgage. Equity will not allow the first mortgage to needlessly wipe out the second mortgage by paying itself firstly out of funds derived from the properties covered by both mortgages. The first mortgagee must leave as much as possible for the second mortgagee out of funds derived from properties covered also by the second mortgage. In modern practice, the funds derived from sale will be under control of the court, and the court will marshal by simply directing payment accordingly.

[26] Belzil J.A. further noted that the underlying issue is really between the second mortgagee and the mortgagor and its assigns and there is really no contest between the first and second mortgagees, citing **Gibson v. Seagrim** (1855), 20 Beav. 614. The first mortgagee's sole interest is in receiving the money owed to it, and marshalling does not affect that interest. It does not matter to the first mortgagee which fund it receives its money from. Equity, Belzil J.A. says, assumes that a reasonable first mortgagee would want to act honourably, and not capriciously, by leaving as much as possible for the second mortgagee. He quotes North, J. in **Re Loder's Trusts (a)** [1886], The Law Times, Vol LV., N.S. 582:

This is the course which a straightforward man would take.

[27] The doctrine of marshalling is not applied only to mortgagees, and accordingly, I know of no reason why the holder of a builders' lien cannot have resort to the doctrine of marshalling: **Narduzzi v. Richardson**, 2009 BCSC 588, 54 C.B.R. (5th) 1 (at para. 29 and the cases cited therein at paras. 25-28).

[28] Of further consideration is the principle which is called "marshalling by apportionment". This particular strain of the doctrine of marshaling was aptly explained by Scarth J., in **Bancorp Investments (Fund 2) Ltd. v. Bhugra Holdings Ltd.**, 2006 BCSC 893, 23 C.B.R. (5th) 108, at para. 25 as follows:

With respect to Apportionment Mr. Justice Burnyeat writes the following at [paragraph] 12:

Apportionment

- 12 In a situation where an owner mortgages both properties in favour of the same first mortgagee but then mortgages the first property to "B" and the second property to "C", the doctrine of "marshalling by apportionment" applies:

... where each of the two funds has been assigned or charged by the debtor to a different subsequent claimant, equity interposes so as to secure that the claim of the first claimant is borne by the two funds rateably.

[Halsbury's (4th ed) Vol. 16, p. 785, para. 876.]

As between "B" and "C" in the example noted above, the loss will not lie where the first mortgagee makes it lie. The charge of the first mortgagee will be apportioned rateably between the two properties (according to their value) so that the competing interests of "B" and "C" can be adjusted.

[29] Marshalling by apportionment was further explained in **Victor Investment Corp. v. Fidelity Trust Co.**, [1975] 1 S.C.R. 251, 41 D.L.R. (3d) 65 as arising in relation to two properties held in separate hands, but subject to the one mortgage debt covering both of them. Thus under apportionment the debt was prorated according to the respective values of the two properties, in the absence of any stipulation that one of the properties would bear the burden or bear it primarily as between the two holders of the equities of redemption.

3. Statute of Elizabeth

[30] 805 submits that this case also involves the principles raised by the *Statute of Elizabeth*. It is clear from the judicial authorities that the *Statute of Elizabeth* is in force in Alberta, **Goyan v. Kinash**, [1945] 2 D.L.R. 749, [1945] 1 W.W.R. 291 (Alta. S.C.) at 753 in D L.R.

[31] Romaine J. in **Krumm v. McKay**, 2003 ABQB 437, 342 A.R. 169 provided a concise overview of the application of the **Statute of Elizabeth**, noting that the purpose of the statute and of the *Fraudulent Preferences Act* is to strike down any conveyances made with the intention to defeat creditors, except for conveyances made for good consideration and *bona fides* to persons not having notice of fraud. She noted that the legislation must be interpreted liberally, and includes any kind of transfers or conveyances made with the requisite intent no matter what the

form, citing C.R.B. Dunlop, in *Creditor-Debtor Law in Canada* (2d Ed.) (Toronto: Carswell, 1995), at page 598.

[32] Under the *Statute of Elizabeth*, a transfer made for nominal or no consideration is voidable if the debtor intended fraud. There are two categories of fraudulent intent: those in which fraudulent intent is established as a presumption of law and those in which fraudulent intent is established as a fact in evidence: Dunlop at pages 600, 601.

[33] While the *Statute of Elizabeth* includes an exception for *bona fides* transfers for consideration, it is restricted to transferees who do not have knowledge of fraud. Therefore, a creditor attempting to rely on the *Statute of Elizabeth* must establish that the transferor had the necessary fraudulent intention **and** that the transferee was privy to the fraud. (*Krumm* at para. 15).

[34] The following general principles can be gleaned from the cases:

- (a) There is no presumption of fraud in situations of transfer for value;
- (b) A creditor must prove an actual intent to defraud;
- (c) If the transferee knows that the transferor intends to defraud the creditors, the transfer will be invalidated.
- (d) In Canada, a further elaboration of the above points applies so that in cases of a transfer for consideration, there must be a "concurrence of intent" to invalidate a transfer under the *Statute of Elizabeth*. In *Mulcahy v. Archibald* (1898), 28 S.C.R. 523 the Supreme Court held that knowing the transferor's intention was found to not be conclusive of bad faith where the transferee did not receive the transfer in order to benefit the transferor. See also Dunlop at pages 607-612.
- (e) The following factors have been identified as "badges of fraud" that raise a *prima facie* case:
 - 1) the transfers were made pending the creditors' efforts to obtain judgment;
 - 2) the transfer documents contain false statements as to consideration;
 - 3) the consideration was grossly inadequate;
 - 4) there was unusual haste to make the transfers; and
 - 5) a close relationship exists between the parties to the transfers.
- (f) In *Megbiz v. Osprey Energy Ltd.*, 2006 ABQB 630, 405 A.R. 165, Master Hanebury described a similar list of badges of fraud (at para. 31, relying on Dunlop at p. 613):
 - (a) the transaction was secret;

- (b) the transfer was made pending the writ;
- (c) the deed contained self-serving provisions such as "the gift was made honestly, truly, and bona fide";
- (d) the deed contains false statements as to the consideration;
- (e) the consideration is grossly inadequate;
- (f) there is unusual haste to make the transfer; and
- (g) a close relationship exists between the parties to the conveyance

[35] In **Krumm** Romaine J. found that the most persuasive factor leading to a finding of fraud was the relationship between the debtor and the transferee. She applied the evidentiary rule governing cases of close relationship between a transferor and a transferee set out by Davies J. in **Koop v. Smith** (1915), 8 W.W.R. 1203 (S.C. C.) (at page 1205) as follows:

I think the true rule is that suspicious circumstances coupled with a 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.

[36] Romaine J. further noted that the types of close relationships covered by this rule include transactions between individuals and corporations that they control, citing **Burton v. R & M Insurance Ltd.** (1977), 5 Alta. L.R. (2d) 14, 9 A.R. 589 (T.D.); **Surkan (Trustee of) v. Niton Junction Holdings Ltd.**, [1979] 3 A.C.W.S. 570, 32 C.B.R. (N.S.) 141 (Alta. Q.B.).

[37] Badges of fraud, and the rebuttable presumptions that arise from them, apply not only where no consideration has been exchanged, but also to situations where there has been a transfer for value: **Krumm** at para. 21. There, Romaine J. noted that (at para. 21):

. . . The "presumption" created by a transfer involving a close relationship is an evidentiary rule, not a presumption of law. It is a rare case where direct evidence of an intention to defraud is available, and given the difficulty of a court "engaging in [a] metaphysical excursion into the debtor's state of mind" (Dunlop, *supra* at page 601), it is not unreasonable to shift the burden of adducing evidence to rebut a *prima facie* case to the debtor in circumstances where strong suspicions of a relationship that may give rise to collusion are apparent.

[38] Further, an intent to defraud may be inferred from all the circumstances surrounding a transaction; **Rogers Realty Ltd. v. Prysiazny** (1996), 182 A.R. 118, 61 A.C.W.S. (3d) 862 (QB) at para. 18.

[39] Various authorities have held that where the debtor receives some benefit, either direct or indirect, the *Statute of Elizabeth* may be applied to attack the conveyance. **Canada Life Assurance Co. v. 494708 Alberta Ltd.**, [1996] 1 W.W.R. 21, 173 A.R. 172 (QB) (at para. 76). **Andersen Lumber Co. v. Canadian Conifer Ltd.** (1977), 25 C.B.R. (NS) 35, [1977] 5 W.W.R.

41 (Alta C.A.), at pp. 42-43; **Krumm**, (at para. 32); **Optical Recording Laboratories Inc. v. Digital Re-cording Corp.** (1990), 1 O.R. (3d) 131, 75 D.L.R. (4th) 747 (C.A.).

[40] In order to invoke the protection of the *Statute of Elizabeth* a fraudulent transaction must be established. To do so, an intention to defraud must be proven. In this respect, the Court may look to the badges of fraud to determine if the necessary intent existed. In **Nuove Ceramiche Ricchetti S.p.A. v. Mastrogiovanni** (1988), 76 C.B.R. (N.S.) 310 (Ont. H.C.J.) Trainor J. quoted Anderson J. in **Re Fancy**:

The plaintiff must prove that the conveyance was made with the intent defined in that section. 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. Although the primary burden of proving his case on a reasonable balance of probabilities remains with the plaintiff, the existence of one or more of the traditional "badges of fraud" may give rise to an inference of intent to defraud in the absence of an explanation from the defendant. In such circumstances there is an onus on the defendant to adduce evidence showing an absence of fraudulent intent. Where the impugned transaction was, as here, between close relatives under suspicious circumstances, it is prudent for the court to require that the debtor's evidence on bona fides be corroborated by reliable independent evidence.

The "badges of fraud" referred to by Mr. Justice Anderson are those set out in *Re Dougmor Realty Holdings Ltd.*, (1966), 59 D.L.R. (2d) 432:

- (1) Secrecy
- (2) Generality of Conveyance
- (3) Continuance in possession by debtor.
- (4) Some benefit retained under the settlement to the settlor.

...

Control of the assets following the transfer remained with Mr. Mastrogiovanni. He was able to carry on the same business on the same street under almost the same name. Even he confused the names during his testimony. As a consequence, not a day's work was lost nor a day's income and he was able to do this without the burden of the accounts payable that Ceramic had incurred. His explanation, unsupported by evidence that should have been readily available, if his explanation was true, bears little resemblance to reality.

[41] A further discussion of the "badges of fraud" was stated in **Bank of Montreal v. Peninsula Broilers Ltd.**, [2009] O.J. No. 2129 (Ont. Sup. Ct.J.) where Quinn J., stated at paras. 82 and 93:

82 In cases where there are badges of fraud or suspicious circumstances surrounding a conveyance, "there is no 'onus' shift, but simply a question of legitimate explanation that may be required in circumstances of suspicion": see *Park v. Bhandari*, [2007] O.J. No. 2237, 2007 CanLII 20981 (On S.C.) at para. 38, aff'd 2008 ONCA 884 (CanLII).

93 "... the existence of one or more of the traditional 'badges of fraud' may give rise to an inference of intent to defraud in the absence of an explanation from the defendant": see *Re Fancy*, *ibid*, followed in *Ricchetti v. Mastrogiovanni*, *ibid*, and in *392278 Ontario Ltd. (c.o.b. Group Three) v. Interopeka S.A.*, *ibid*.

[42] In *Convoy Supply Alberta Ltd. v. Apex Insulation 1996 Ltd.*, 2003 ABQB 1, 119 A.C.W.S. (3d) 434, Wilson J., in discussing how the Court could ascertain an intention to defraud stated (at para.19):

The materials filed by the Plaintiff include the statement that "the credibility of Staples is not in issue." The Defendant takes the position that this puts the matter beyond all argument, that there could not be a fraudulent transaction or intent, as the Defendant Staples denies that she had any such intent. I do not agree... In my opinion, the proper way to assess her real intent is to see what the plain effect of that person's conduct was in the light of circumstances existing at the time. **One would not expect that a witness involved in this kind of a transaction would say that they intended to defraud. These cases usually depend on an examination of the known facts and the situation existing at the time.**

(Emphasis added)

V. Analysis

1. **Is the Receiver entitled by virtue of the equitable doctrine of subrogation to step into the position of the ATB in regards to the payment of \$391,275.17 made by Hinton Pine to the ATB pursuant to the Guarantee given by Hinton Pine to the ATB?**

The Position of the Parties

(a) The Position of the Receiver

[43] The Receiver submits that the right of subrogation arises by reason of the Guarantee between ATB and Hinton Pine entered on May 27, 2009. As a result, the Receiver paid ATB \$391,275.17. The Receiver further submits that the only limitation on enforcement of the right of security was contained in paragraph 6 of the Guarantee which provided "until all indebtedness of the Customer to you has been paid in full, the undersigned shall not have any right of

subrogation or to securities held by ATB unless expressly given to the undersigned in writing by the President and CEO, Chief Operating Officer or Chief Credit Officer of ATB”.

[44] The Receiver submits that the registration of security interests by 805 under the Personal Property Security Act does not provide it any form of relief, given the fact that registration of that security was not undertaken until March of 2010, following registration of a renewal by 805. At that time, 805 was aware of the Rollover transaction, and the Amending Agreement further provided for additional consideration of \$1,250.00 per month payable to the Mortgage holder, presumably as a cost of extension of the term of their Mortgage.

[45] The Receiver further submits that the relative position of both 805 and Cedar Peaks under their respective second Mortgages has not changed, and their ability to collect the full amounts owing under their Mortgages are attributable to general market conditions and the decrease in value of the property, rather than the Rollover Agreements and the transfers of the properties to Hinton Pine and Hinton Leaf.

[46] With respect to the application of the *Statute of Elizabeth* to the Rollover Agreement between 103 and Hinton Pine, the Receiver submits that the title transfers under the Rollover Agreement were done in the normal course of business and for proper consideration. The Receiver further submits that the respective securities held by 805 and Cedar Peaks remained intact and enforceable in the same manner both before and after the transactions that were the subject of the Rollover Agreements. Accordingly, the Receiver submits that by virtue of the right of subrogation, it is entitled to step into the position of ATB in regards to the payment of \$391,275.17.

(b) The Position of 805

[47] 805 submits that the Court must consider the effect of the *Statute of Elizabeth* on the Rollover Agreement between Hinton Pine and 103. 805 argues that the net effect of the Rollover Agreement was that at 8:00am on the morning of September 1, 2008, 103 owned Lots 1,2,3 and had equity in those Lots of approximately \$630,340.00, (equity which would have been available to the creditors of 103). As a result of the Rollover Agreement by noon on September 1, 2008, 103 no longer owned Lots 1, 2, 3, and had not received from Hinton Pine anything of value, which could then have been available to 103's creditors to apply against what 103 owed them.

[48] 805 further submits that in accordance with the principles of priority contained in the *Personal Property Security Act*, 103 could not cancel that evidence of indebtedness, because this in effect would be 103 giving the funds to Hinton Pine in return for Hinton Pine cancelling the indebtedness which 103 owed for redemption of the 103 shares held by Hinton Pine. Accordingly, 805 argues that this is not allowed under the *Personal Property Security Act* as ATB and Cedar Peaks have priority over Hinton Pine, and as such the \$391,275.17 which came into the hands of Hinton Pine would in fact belong to ATB under the General Security agreement and the principle of subrogation does therefor not arise in respect to that amount.

[49] Lastly, 805 submits that the Rollover transactions that were the subject of the Rollover Agreement between 103 and Hinton Pine was not *bona fides* and that the preferred shares of Hinton Pine were not good and valuable consideration exchanged for the equity in Lots 1,2,3. In this respect, 805 submits that if the owner of a corporation can strip the equity from the corporation by such a Rollover, no ordinary creditor of any corporation will ever again collect anything from a corporation because all the controlling shareholder and the directing mind of the corporation needs to do is incorporate a second company and strip out the assets of the corporation in the manner which was done by Mr. Dorais.

[50] 805 maintains that this clearly is one of the types of fraud against creditors, which the *Statute of Elizabeth* was designed to deal with and that the statute should be given broad and liberal interpretation. Accordingly, 805 submits that the Rollover transactions that were the subject of the Rollover Agreements are as a result of the *Statute of Elizabeth* invalid, and as such, the Receiver cannot, by virtue of subrogation, step into the position of ATB in regards to the payment of \$391,275.17.

(c) The Position of the Lien Holders

[51] The Lien Holders submit that assuming that the doctrine of subrogation applies to the case at bar, such doctrine should only be applied at such time as all secured creditors are paid in full. To do otherwise they submit, would cause an injustice to the duly registered lien holders who are secured creditors. The Lien Holders further submit no right of subrogation would exist on Lot 8 because:

1. the Receiver is claiming the right of subrogation with regard to Guarantee signed for Lot 8; and
2. the ATB indebtedness had been fully repaid by the time Lot 8 sold under judicial sale; and
3. ATB has not realized any of its mortgage debt out of the sale of Lot 8.

[52] As such, the lien holders argue, any right of subrogation exists only on the properties from which the mortgages were realized, and as ATB no longer had any claim against Lot 8, subrogation to their position on that debt would have no effect. The Lien Holders further submit that they, together with the Town of Hinton's caveat, are to be considered as junior creditors by virtue of their registered builders' liens and caveat, as opposed to unsecured creditors. The Lien Holders submit that subrogation within the doctrine of marshalling applies to the junior creditors, and not to third party unsecured creditors, and that the security attaches to the mortgagor's claim which can be satisfied through marshalling the funds received. Accordingly, when the secured first and second mortgages have been paid, the right of subrogation passes to the Lien Holders as the junior creditors, and after the junior creditors have been fully paid, the unsecured creditors can fit within the parameters of marshalling.

(d) Conclusion

[53] The Receiver, as the receiver for Hinton Pine, claims that by virtue of the equitable doctrine of subrogation, the Receiver is entitled to receive from the funds available, the sum of \$391,275.17. In order to determine such entitlement, it must first be determined to what extent the right of subrogation arises as a result of the Guarantee by Hinton Pine of 103's indebtedness to ATB.

[54] The Guarantee by Hinton Pine to ATB dated May 27, 2009 is entitled "Continuing Guarantee", without specific reference to a particular parcel of land or as to a stipulated sum. In this respect, the Guarantee merely states that the Guarantee by Hinton Pine is given in consideration of ATB extending credit to 103 or otherwise dealing or continuing to deal with 103. In accordance with such Guarantee, Hinton Pine guaranteed unconditionally and promised to pay to ATB all existing and future debts and liabilities of 103.

[55] Pursuant to the equitable doctrine of subrogation, absent any intention of fraud, once Hinton Pine was required under the Guarantee to permit the payment of the sum of \$391,275.17 to ATB to satisfy the debt of 103 to ATB from the sale proceeds of Lots 1,2,3, Hinton Pine would have the right to step into the shoes of ATB in regards to the \$391,275.17.

[56] But, the question now to be addressed is whether there is evidence of fraud; in other words was the Rollover Agreement between 103 and Hinton Pine a valid and enforceable transaction? If it can be established that the Rollover Agreement and the attending transfers of land offends the *Statute of Elizabeth*, the transaction will be declared void, and Hinton Pine will be denied the right of subrogation in regards to the \$391,275.17. In order to answer this question, the circumstances surrounding the Rollover Agreement and in particular, the relationship of Mr. Dorais to 103 and Hinton Pine, together with all surrounding circumstances must be reviewed.

[57] Mr. Dorais was the sole controlling shareholder and directing mind of 103 and Hinton Pine. The Receiver argues that the Rollover Agreement which effectively transferred Lots 1,2,3 from 103 to Hinton Pine was done in the normal course of business and for proper consideration, albeit not for cash consideration. What benefit did Hinton Pine derive from the transaction?

[58] The Receiver submits that the Rollover Agreement was required for tax purposes, and presumably to ultimately benefit Mr. Dorais as the sole shareholder of 103 and Hinton Pine. The Receiver further argues that insofar as 805 and Cedar Peaks are concerned, their security as second mortgage holders remained in the same position both before and after the Rollover transaction. If Mr. Dorais had not died and had he continued to make the required payments to ATB, arguably, it could be said that no benefit other than the Receiver's alleged tax benefits would have been obtained by Hinton Pine, 103 and eventually Mr. Dorais himself.

[59] Unfortunately, that is not what happened. Mr. Dorais did pass away, the payments were not made to ATB, and consequently, as a result of the Guarantee and the Court ordered sale of

Lots 1,2,3, on paper at least, Hinton Pine appears to be entitled to the right of subrogation in regards to the \$391,275.17. This would make these funds unavailable to 805 and Cedar Peaks. As such, 805 and Cedar Peaks are not, as suggested by the Receiver, in the same position both before and after the Rollover transaction. If this Court were to permit Hinton Pine to avail itself of subrogation, the net effect would be that Mr. Dorais, as the sole shareholder of both 103 and Hinton Pine would have managed to extricate and protect from the hands of secured and unsecured creditors the \$391,275.17.

[60] As stated previously, in **Morrison v. Canadian Surety Co.**, the Court confirmed that the doctrine of subrogation came into existence for the purpose of preventing an injustice to a party who is required to pay another's indebtedness, provided that under the circumstances the Court decides it is just and reasonable, having regard to the relationship of the parties.

[61] In this case, the relationship of Mr. Dorais to 103 and Hinton Pine raises in my mind two of the badges of fraud:

1. The consideration is grossly inadequate; and
2. a close relationship exists between the parties to the conveyance; see: **Megbiz v. Osprey Energy Ltd.**, at para.31.

[62] I therefore find myself in a situation similar to that which existed in **Krumm**, where Romaine J. concluded that the most persuasive factor that lead to a finding of fraud was the relationship between the parties. Taking into consideration the law as set out by Romaine J. in **Krumm**, and in particular those cases which involved transactions between individuals and corporations that they controlled, I find that there exists sufficient suspicious circumstances, coupled with a close relationship, to raise a *prima facie* case justifying an inference of an intent to defraud: **Koop v. Smith**, at page 1205.

[63] This conclusion is arrived at given the absence of a legitimate explanation from the Receiver. As stated previously, the Receiver argues that the Rollover Agreement was done in the normal course of business, for proper consideration, and in particular, for tax reasons. However, the end result of the Rollover Agreement is to permit the primary assets of 103 (Lots 1,2,3) to be removed from the secured and unsecured creditors of 103. As a result, once ATB was aware of the Rollover Agreement, it took immediate steps to obtain the Guarantee from Hinton Pine. To permit Hinton Pine to be subrogated to the \$391,275.17 in priority to secured creditors would be inequitable.

[64] For that reason, I find that the Rollover Agreement and the attending transfers of land offends the *Statute of Elizabeth*, with the effect that the transaction is declared void. Hinton Pine is therefore denied the right of subrogation in regards to the \$391,275.17.

[65] With respect to the application of Rule 359, as Lots 1,2,3 have been sold pursuant to Court Order any discussion of its application to the case at bar is redundant. Given my

conclusion in regards to Hinton Pine being denied the right of subrogation to the \$391,275.17, the provisions of the *Personal Property Security Act* become as well inapplicable to the issue of subrogation.

[66] As the question contained in subparagraph (a) has been answered in the negative, there is no requirement by this Court to address the issue in subparagraph (b).

2. To what extent does the doctrine of marshalling or alternatively apportionment, apply to the respective claims made by 805, Cedar Peaks, Hinton Plumbing and Heating Ltd, D.C. Electric Ltd., the Town of Hinton, or any other secured creditors?

The Position of the Parties

(a) The Position of the Receiver

[67] With respect to the equitable doctrine of marshalling, the Receiver submits that it need not take a position with respect to the issue of marshalling.

(b) The Position of 805

[68] With respect to the application of the equitable doctrine of marshalling, 805 submits that after Lots 1,2,3, had been sold and ATB had taken all of the money from the sale of Lots 1,2,3 (with the exception of those funds paid to Mr. Dewar), there was remaining owing to ATB, \$612,398.31, (this amount was satisfied by ATB out of the sale proceeds of Lot 4), plus the solicitor client costs and the accounts of the Preservation Agent for Lot 4 and Lot 8, (referred to as the "Post Lots 1,2,3 sale ATB indebtedness"). In respect of the 5% payment of \$12,257.57 and the Government of Alberta occupancy costs of \$31,996.73 collected and held by the Receiver, 805 submits that the doctrine of marshalling should be applied and those amounts should be applied against the ATB indebtedness reducing the Post Lots 1,2,3 sale ATB indebtedness to \$617,374.26 for the purposes of marshalling by apportionment.

[69] As 805 had a valid registered second mortgage against Lot 4, and Cedar Peaks had a valid registered mortgage against Lot 8, 805 submits that this is a classic case of marshalling by apportionment and that this Court should direct that the Post Lots 1,2,3, sale ATB indebtedness be apportioned between Lot 4 and Lot 8 proportionate to their respective values. 805 submits that the rateable proportions would be that Lot 4 should bear 50.39% of the Post Lots 1,2,3 sale ATB indebtedness and Lot 8 should bear 49.61% of that indebtedness. 805 then submits that this Court should then apportion the Post Lots 1,2,3 sale ATB indebtedness, by apportioning \$311,067.72 to Lot 4 and \$306,306.47 to Lot 8. The net sale proceeds from the sale of Lot 4 is \$915,005.42. 805 submits that if the Court then deducted the \$311,067.72 apportioned against Lot 4, this would leave \$603,937.70 to satisfy the second mortgage held by 805. The net sale

proceeds from the sale of Lot 8 is \$889,334.10. 805 submits that if the Court then deducted the \$306,306.47 apportioned against Lot 8, this would leave \$583,027.63 to satisfy the second mortgage held by Cedar Peaks, together with any surplus from Lot 4. In this regard, 805's proposal is as follows:

ATB took from lot 4	\$661,628.56
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Subtract off the common area costs recovered	\$31,996.73
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Subtract off the 5% amount recovered	<u>\$12,257.57</u>
--------------------------------------	--------------------

Notionally ATB took from lot 4	\$617,374.26
--------------------------------	--------------

Apportionment between lots 4 and lots 8 of the ATB amount

Proportionate to the values of lots 4 and lots 8:

Lot 4 proportionate value	$\frac{\$980,000}{\$980,000 + \$965,000}$	=	$\frac{980,000}{1945,000}$	=	.503856
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Lot 8 proportionate value	$\frac{\$965,000}{\$1945,000}$	=		=	.4961439
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ATB from lot 4	\$617,374.26	x .503856	=	\$311,067.72
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ATB from lot 8	\$617,374.26	x .4961439	=	\$306,306.47
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Net values

Lot 4: \$915,005.42 - \$311,067.72 =	\$603,937.70
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Minus 2 nd mtge 805251 Alta. Ltd. -	<u>\$423,379.00</u>
--	---------------------

Surplus

Lot 8: \$889,334.10 - \$306,306.47 = available to Cedar Peaks	\$583,027.63
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Add surplus from lot 4 =	<u>\$180,558.70</u>
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to Cedar Peaks	\$763,586.33
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Reconciliation

2nd mtge 805: \$423,379 + \$763,586.33 to Cedar Peaks = \$1,186,965.30 =

Total available funds after ATB paid in full	\$1,186,965.20
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[70] With respect to whether Cedar Peaks would be allowed to prejudice the interest of Hinton in respect of their offsite levy (protected by Caveat registered against title to Lot 4), 805 submits that Hinton is not entitled to take advantage of the principles of marshalling because it filed its

Caveat after the second mortgage had been filed. Under the Alberta Torrens system, Hinton should then be subordinate to such second mortgage.

[71] With respect to the builders' liens filed by the Lien Holders against Lot 8, 805 submits that these builders' liens are not entitled to take advantage of the principles of marshalling, because there are insufficient funds to satisfy the two second mortgages on Lot 4 and Lot 8 and the builders' liens will receive nothing from the sale proceeds of Lot 8.

(b) The Position of the Lien Holders

[72] The Lien Holders submit that in order to ensure the most equitable division of the monies realized by the sale of the subject properties, the doctrine of marshalling should be applied. Further, they submit that as the doctrine is an equitable one and cannot be used to garner inequitable results, all of the funds available from the sale of all three properties should be used to pay off firstly, ATB, secondly, the 2nd mortgages, and thirdly, the Lien Holders. Further, the Lien Holders concede that as lien holders, they cannot be treated on par with a mortgage holder, and it is therefore not their argument that their respective builders' liens would have any priority over the mortgage holders. However, they submit that as registered lien holders, they are entitled to, in a secondary position, have the funds marshalled in a way that ensures that as many of the secured creditors as possible can take advantage of the monies received by the court.

[73] With respect to the doctrine of apportionment, the Lien Holders submit that such doctrine is a sub-issue of the doctrine of marshalling, and is an equitable remedy which cannot be used to achieve an inequitable result. Accordingly, the Lien Holders submit that it is unnecessary to apply the doctrine of apportionment as all primary and second mortgagors can be fully repaid without using apportionment. The Lien Holders submit that if the monies were apportioned as suggested by 805, an inequitable result would occur in that the lien and caveat holders would be left with no recourse or payment. The Lien Holders further submit that if the doctrine of marshalling is applied without apportionment, there will be more proceeds for those who only have recourse in the proceeds of Lot 8, and that the doctrine of marshalling will create excess funds in the sale of Lots 1, 2, 3 and Lot 4. Therefore to be equitable, the Lien Holders submit that the excess funds must be used to satisfy the secured creditors of Lot 8 before they are distributed to the Receiver on behalf of the unsecured creditors.

[74] With respect to unsecured creditors, the Lien Holders submit that the doctrine of marshalling does not apply in favour of an unsecured creditor. The Lien Holders further submit that as their respective builders' liens represent work done by the Lien Holders to increase the value of the properties this unpaid work is reflected in the amount received from the sale. Accordingly, to allow the Receiver to receive funds on behalf of unsecured creditors ahead of the secured Lien Holders would be inequitable.

(c) Conclusion

[75] The present case represents a classic situation warranting judicial intervention and application of the equitable principles of marshalling by apportionment. In this respect, the present fact situation fits squarely within the example of marshalling by apportionment quoted by Scarth J. in **Bancorp investments (Fund 2) Ltd. v. Bhugra Holdings Ltd.** (at para. 25):

In a situation where an owner mortgages both properties in favour of the same first mortgagee but then mortgages the first property to "B" and the second property to "C", the doctrine of "marshalling by apportionment" applies:

... where each of the two funds has been assigned or charged by the debtor to a different subsequent claimant, equity interposes so as to secure that the claim of the first claimant is borne by the two funds rateably.

[Halsbury's (4th ed) Vol. 16, p. 785, para. 876].

As between "B" and "C" in the example noted above, the loss will not lie where the first mortgagee makes it lie. The charge of the first mortgagee will be apportioned rateably between the two properties (according to their value) so that the competing interests of "B" and "C" can be adjusted.

[76] With respect to the Lien Holders' claims and their right to avail themselves of marshalling, I recognize that equitable doctrines are not restricted to mortgagees, and in the appropriate circumstances marshalling applies to holders of a builders' liens: **Narduzzi v. Richardson**. Furthermore, it must be remembered that marshalling is subject to two important qualifications: first, that nothing can interfere with the paramount right of the first mortgagee to pursue his remedy against either of the two estates; and, second, that the doctrine will not be applied to the prejudice of third parties: **Ernst Brothers Co. v. Canada Permanent Mortgage Corporation** at 367-8.

[77] In **Narduzzi v. Richardson**, Burnyeat J. said (at para. 26):

I also take into account the decision in **807933 Ontario Inc. v. Allison (Trustee of)** (1998), 38 O.R. (3d) 337 (Ont. C.A.), where the court stated that there were two criteria to be met before marshalling would be available:

The first criteria is that there must be a creditor or mortgagee who has access to two properties of a debtor to which he or she can resort for payment of the amount owing. ... The second criteria is that there must be a creditor ranking behind or inferior to another creditor or mortgagee of a common debtor with a claim against one of the properties available to the superior creditor or mortgagee. Such an inferior creditor can invoke the assistance of equity to cause or marshal the superior creditor or mortgagee to satisfy the

mortgage debt from the property against which the inferior creditor has no recourse so that the property will be available to the inferior creditor, or if this is impossible, or unfair to the superior creditor, equity may allow the inferior creditor to stand as the superior creditor in relation to the property against which the inferior creditor otherwise has no recourse.

[78] I cannot accept the Lien Holders' argument that the doctrine of marshalling with apportionment should not be applied. They argue that it is unnecessary to apply apportionment because all primary and second mortgagees can be fully repaid without using it. If you calculate the combined net sale proceeds from the sale of the properties, less the combined totals of ATB, 805 and Cedar Peaks indebtedness, the end result is that, whether by marshalling or marshalling with apportionment, there is simply not enough monies available from such sales to satisfy the mortgagees, let alone, the mortgagees plus the lien and caveat holders.

[79] In order to apply the equitable doctrines of marshalling and apportionment, this Court must give full recognition of the Torren's system of land registration, as incorporated into the *Land Titles Act*. That being so, because the interests of the Lien Holders and Hinton were registered after the second mortgages of 805 and Cedar Peaks, it would be wrong to permit a subsequent encumbrancer to share equally with all prior encumbrancers other than the primary creditor, ATB. If this were a situation where all secured creditors could be paid from the proceeds of the sale of the subject properties, or the interests of the Lien Holders and Hinton were the only secured creditors registered on title to such properties, then, it would be appropriate to apply the doctrine of marshalling. However that is not the case here.

VI. Conclusion

[80] Accordingly, the proposal by 805 for application of the doctrine of marshalling with apportionment as above stated, is acceptable and is to be implemented. The Receiver is hereby ordered to pay into Court the 5% payment and the Government of Alberta occupancy costs collected and held by the Receiver. The total of these funds shall be considered as having been already collected by ATB and are to be considered as proceeds of the sale of Lot 4 and Lot 8. Should counsel require further direction in regards to the implementation of this proposal, and the relevant calculations, they may come back for further direction.

[81] If the parties cannot agree on costs, costs may be spoken to within sixty (60) days of this decision.

Heard on the 4th day of June, 2010.

Dated at the City of Edmonton, Alberta this 3rd day of September, 2010.

Don J. Manderscheid
J.C.Q.B.A.

Appearances:

Gregory C. Empson
Gregory C. Empson Professional Corp.
For Anthony Ford Gerrow

Brian Doherty
Doherty Schuldhaus LLP
for the Applicant 805251 Alberta Ltd.

Robert Bishop
Bishop & McKenzie LLP
for Cedar Peaks Mortgage Investments Inc.

Kelsey Becker Brooks
Reynolds, Mirth, Richards & Farmer
for the Town of Hinton

Douglas H. Shell
Davis LLP
for Alberta Treasury Branch

James R. McClelland
Johnson McClelland Murdoch
for D.C. Electric Services Ltd. and Hinton Plumbing and Heating Ltd.

Maurice Blain
Nikitiuk & Blain
for O.K. Tire Stores Inc.

TAB 2

CITATION: House v. Baird, 2019 ONSC 1712

COURT FILE NO.: C-1092-09

DATE: 2019-03-15

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:

TYLER HOUSE BY HIS LITIGATION
GUARDIAN GAIL HOUSE, THE ESTATE
OF TITUS HOUSE, GAIL HOUSE and
TITUS HOUSE JR.

- and -

DONALD BAIRD, ROBERT SCOTT
MURRAY and THE CORPORATION OF
THE TOWNSHIP OF WILMOT

)
)
) Allan Rouben & Richard Campbell, Counsel
) for Tyler House, Plaintiff
)
)
)

)
)
) Jeramie Gallichan & Daniel Veinot, Counsel
) for Donald Baird, Defendant (Plaintiff in
) Court File No. C-141-11)
)
)

) Greg Robson, Counsel for the Non-Party,
) Nordique Insurance
)
)

) Gary Flaxbard, Counsel for Dawn Samms &
) Darryl Samms (Plaintiffs in Court File No.
) C-570-10)
)
)

) **HEARD:** August 17 & December 10, 2018

The Honourable Justice Catrina D. Braid

REASONS ON MOTION

I. OVERVIEW

[1] Tyler House was driving a car with the consent of the owner, Donald Baird. House lost control, and the vehicle was hit by another car. As a result of the accident, Adam Samms lost his life. House and Baird were seriously injured. At the time of the accident, Baird and House each had insurance with policy limits of \$1 million.

[2] Baird and the Samms family brought actions against House, Scott Murray (the driver of the other car) and the Township of Wilmot. The Samms family settled their claim for \$200,000, and Baird settled his claim for \$500,000.

[3] House sued Baird, Murray, and the Township, and the action proceeded to trial. House obtained judgment against Baird in the amount of \$1.4 million.

[4] House has brought a motion seeking directions regarding the distribution of insurance funds and regarding his right to garnish Baird's settlement.

[5] In these reasons, I shall address the following issues:

- A. The legal framework for distribution of insurance funds
- B. Whether the equitable remedy of marshalling is available
- C. Enforceability and ambiguities in the Baird settlement
- D. Whether House can garnish the Baird settlement funds

[6] For the reasons set out below, I find that the doctrine of marshalling is not applicable. State Farm must pay out the funds on a *pro rata* basis, and Nordique must pay the remaining amounts to Baird and the Samms family. House shall be entitled to garnish 20% of the Baird settlement.

II. FACTS

[7] A tragic accident occurred on February 25, 2009, involving four young men who were close friends. House was driving Baird's vehicle when the vehicle went out of control and was struck by a vehicle driven by Murray. As a result of the accident, Adam Samms lost his life. Baird was seriously injured. House was catastrophically injured, with his most severe injury being a diffuse axonal closed head injury.

[8] The Baird vehicle was insured by State Farm with third-party liability limits of \$1 million. In these reasons, I shall refer to this insurance policy as "the State Farm policy."

[9] House was insured by Nordique Insurance with third-party liability limits of \$1 million. In these reasons, I shall refer to this insurance policy as "the Nordique policy."

[10] Baird and the Samms family brought actions against House, Murray, and the Township. The Samms family settled their claim for \$200,000, and Baird settled

his claim for \$500,000. In those settlements, the plaintiffs agreed that, in the event that there is a shortfall in the available insurance limits, the amount of the settlements would be pro-rated with the plaintiffs in the other actions. The parties also agreed that the defendants would be bound by the liability findings as determined at the trial of the action brought by House.

[11] House sued Baird, Murray, and the Township, and the action proceeded to trial. The claim against Murray was settled in advance of trial. On February 26, 2015, Justice Kent released his judgment and dismissed the claim against the Township of Wilmot. It is notable that, had the House claim against the Township been even partially successful, there would not have been any issue relating to insurance policy limits.

[12] Justice Kent approved the settlement of the claim made by House against the defendant Murray and ordered Murray to pay \$675,000 in damages to House.

[13] Justice Kent found that Baird's vehicle had overinflated and bald tires, which created a risk that control of the vehicle could not be maintained. The court found that House made no adjustment to his speed to suit conditions, and he was driving while distracted. Because liability was apportioned equally between House and Baird, the court ordered that House is entitled to recover 50% of his assessed damages from Baird.

[14] House obtained a judgment against Baird in the amount of \$1,405,439.10, after the 50% apportionment and a reduction for a settlement with Murray.

[15] The parties have failed to reach an agreement on the distribution of the insurance proceeds. House has brought a motion seeking the following:

- i. Advice and direction from the court regarding the interpretation and application of ss. 258 and 277 of the *Insurance Act*, R.S.O. 1990 c. I.8 in determining priorities and entitlement to insurance monies available to the parties.
- ii. A declaration, in accordance with the equitable doctrine of marshalling, that the House claim rank in priority to the Baird and Samms claims.

- iii. A declaration that the Baird settlement monies received are not exempt from attachment or execution and confirming House's right to garnish those funds directly from the insurance companies.

III. ANALYSIS

A. The Legal Framework for Distribution of Insurance Funds

[16] The limits on Baird's State Farm policy are \$1 million. The insurers take the position that the State Farm policy is required to respond to the three claims on a *pro rata* basis. A portion of the \$1 million would be paid out to each of House, Baird, and the Samms family. In this scenario, the Samms family and Baird would recover the shortfall from House's Nordique policy and would be fully indemnified; House would be left with a shortfall of almost \$668,000 as he is not entitled to recover from his own policy. House argues that this distribution of the funds is incorrect.

[17] A person who has a claim against an insured may recover payment of the judgment against the insured's motor vehicle policy: see *Insurance Act*, s. 258(1).

[18] Under s. 277(1) of the *Insurance Act*, the owner's policy responds first to claims arising from an accident. An owner's insurance policy is first loss insurance in respect of liability arising from the use or operation of an automobile owned by the insured. Insurance under any other motor vehicle liability policy is excess insurance only. A motor vehicle liability policy insures the owner or the driver of an automobile: see *Insurance Act*, ss.1, and 277(1).

[19] House was an insured person under the State Farm policy because his liability arises solely out of the use or operation of the Baird vehicle. This makes the State Farm policy first loss insurance. The Nordique policy is insurance attaching under any other valid motor vehicle policy and is, therefore, excess insurance in relation to the State Farm policy.

[20] The limits on the State Farm insurance policy are \$1 million. Given the fact that the aggregate amount owing to all the plaintiffs exceeds the State Farm policy

third-party liability limits, State Farm must pay its policy limits on a *pro rata* basis (without ranking any of the claims above the other) as follows:

- i. Damages owed by Baird to the Samms family;
- ii. Damages owed by Baird to House;
- iii. Damages owed by House to the Samms family; and
- iv. Damages owed by House to Baird.

[21] The State Farm policy has insufficient limits to satisfy all claims, and House will still owe money to the Samms family and Baird. House has recourse to the insurance policy issued to him by Nordique Insurance to satisfy the remaining claims. Pursuant to s. 277(1), the Nordique policy is excess insurance to the State Farm policy and will be called upon to pay amounts that House owes to others, in excess of what is paid to them by the State Farm policy.

[22] First loss insurance means that House must first look to Baird's insurance policy coverage since he was driving Baird's vehicle at the time of the accident. He may only look to his own policy for additional coverage if his policy limits exceed those of Baird's policy. Since the limits are the same, House cannot obtain the shortfall from his own policy.

[23] House argues that the State Farm policy should not be called upon to make payment to Baird for his own independent claim for damages against House. In support of that argument, he relies on *Enterprise Rent-a-Car Canada Ltd. v. Meloche Monnex Financial Service Inc.*, 2010 ONCA 277, 102 O.R. (3d) 87.

[24] I do not accept this argument. The *Enterprise Rent-a-Car* case deals with the meaning of "insurance available" in the context of a leased vehicle and it is, therefore, distinguishable. This argument also ignores the first loss insurance provisions as set out in s. 277(1) of the *Insurance Act*.

[25] House also relies on the decision in *Benson v. Walt*, 2018 ONCA 172, to support the proposition that the Baird and House policies should be required to

make payment of the independent claims of the other. However, the decision does not stand for that proposition.

[26] In that case, Walt was driving with the consent of the owner of the car. Pursuant to s. 277(1), the first policy to respond is the policy insuring the owner of the vehicle involved in the accident. If the driver is not the owner of the car involved in the accident, the driver's own automobile insurance policy will not apply until the insurance under the owner's policy has been exhausted: see *Benson v. Walt*; and *Avis Rent A Car Systems Inc. v. Certas Direct Insurance Co.*, (2005) 197 O.A.C. 214.

[27] Finally, House argues that s. 277 of the *Insurance Act* does not apply, and the damages should not be pro-rated because he did not consent to the Minutes of Settlement in the other actions. However, his consent is not required. The proper application of s. 277 requires that the damages be pro-rated as between House, Baird and the Samms family.

[28] The OAP 1 Standard Insurance Policy does not differentiate between the obligation of the State Farm policy to indemnify Baird and House. They are both considered insured for purposes of the liability provisions of the State Farm policy. The OAP 1 states that the insurer will make payment on behalf of all of the insured persons, up to the limits of the policy for any one incident. House is an insured under the State Farm policy and, therefore, State Farm is obliged to indemnify House for damages payable to Baird.

[29] In *Scale Estate v. The Cooperators Insurance*, 2018 ONSC 363, the court held that the *pro rata* approach should generally prevail in the case of automobile insurance, and the rule should not be departed from except in special circumstances. I am not satisfied that any special circumstances exist that would justify departing from the *pro rata* principle for first loss automobile insurance.

[30] The Baird and Samms settlements reflected the fact that State Farm, as first loss insurer, considered the need to pro-rate claims between multiple parties.

The facts of this case are similar to the facts in *Insurance Corp. of British Columbia v. Kushneriuk*, 2004 BCCA 440, in which there were multiple claimants, with the most seriously injured claimant only able to receive funds from the first loss insurer. In that case, the British Columbia Court of Appeal found that no special circumstances existed to depart from the usual *pro rata* principle.

[31] In his factum, House submitted that, in the event there is a shortfall, he should be entitled to recover the balance of his judgment under the provisions of the OPCF 44R Endorsement of his own insurance policy. This argument was abandoned by counsel during submissions in court, which was an appropriate concession.

[32] An underinsurer's obligation to pay does not arise until the total amount of insurance held by the tortfeasor at the time of the accident is less than the family protection coverage liability limit. This is true regardless of the number of eligible claimants injured or killed. Access to the underinsurance coverage is not available even if the injuring party's insurance might be apportioned among several plaintiffs, thereby creating a potential payment of less than \$1 million for each plaintiff: see *Van Bastelaar v. Bentley*, 2011 ONCA 660.

[33] In this case, the Nordique policy coverage cannot be called upon to pay the unsatisfied portion of House's judgment against Baird as the liability limit of coverage under the OPCF 44R (\$1 million) does not exceed the total amount of the Baird insurance.

B. Whether the Equitable Remedy of Marshalling is Available

[34] House argues that the court should order that the proceeds of the State Farm policy be marshalled so that House receives the full amount of the State Farm policy limits. Baird and Samms would then be in a position to access the Nordique policy. House argues that the equities of the situation support the application of the remedy of marshalling so that House not be deprived of his recovery.

[35] Marshalling is a principle that permits equity to be done between two or more creditors, each of whom are owed debts by the same debtor, but one of whom can only enforce his claim against one security or fund, while the other can resort to more than one. This will prevent a creditor who can resort to two funds, from defeating another creditor who can resort to only one of them.

[36] Historically, the doctrine arose in cases involving real property mortgages, but has expanded to personal property security and bankruptcy. Counsel were unable to provide any caselaw in which the doctrine of marshalling was invoked in the context of s. 277 of the *Insurance Act*.

[37] The limits of the doctrine of marshalling are not well defined, as equity gives it flexibility, adaptability, and utility. Equity also gives it its uncertainty and lack of clear boundaries: see Bruce MacDougall, “Marshalling and the Personal Property Security Acts: Doing Unto Others...” (1994) 28 U. Brit. Colum. L. Rev. 91 at 91.

[38] There are three primary reasons why marshalling cannot be invoked in this case. I shall address each reason under a separate heading below:

i. There is Not a Common Debtor and Two Creditors

[39] A number of common law rules have developed in the application of marshalling, although its equitable nature enables courts to craft relief appropriate to each case. There are five preconditions for marshalling:

- (a) two creditors;
- (b) one common debtor;
- (c) two funds of the debtor with the superior creditor having access to both and the inferior creditor to but one;
- (d) no interference with the choice of remedy of the superior creditor; and
- (e) no prejudice to third parties.

See *Green v. Bank of Montreal* (1999), 128 O.A.C. 324

[40] House has not specified who he considers the debtors to be, for purposes of the marshalling argument. In the case at bar, the debts arise from either the judgment or settlements flowing from the negligence of different defendants. If the defendants are the debtors, State Farm is obligated to indemnify the defendants to the extent of \$1 million, but it cannot be said that State Farm is a debtor of the plaintiffs under the third-party liability insurance of the defendants.

[41] If the debtor is either Baird or House, it cannot be said that there are two funds at the “debtor's disposal” as the funds available under the insurance policies of House and Baird are not under their control. Rather, these are potential funds, which are only available to certain plaintiffs if they are not able to obtain full recovery of the balances owing to them through the State Farm policy. Even if the debtor is House (who arguably may be indemnified by two insurance policies), the doctrine of marshalling is invoked for the benefit of a creditor and not a debtor.

ii. Marshalling Cannot Defeat Clear Statute

[42] The equitable doctrine of marshalling cannot be applied to overcome the unambiguous wording of the *Insurance Act*. The *Act* does not preclude marshalling, but the doctrine, on its own, cannot overcome well-established legal principles.

[43] Equity is based on judicial discretion. Where applied, equitable remedies are flexible; their award is based on what is just in all the circumstances of the case. They are malleable principles intended to serve the ends of fairness and justice: see *Soulas v. Korkontzilas*, [1997] 2 S.C.R. 217; and *Canson Enterprises Ltd. v. Boughton & Co.*, [1991] 3 S.C.R. 534.

[44] The maxim ‘equity follows the law’ applies in this situation. The maxim seeks to avoid inconsistent approaches from the application of equity rules and common law principles. Where there is a conflict, common law principles prevail. The maxim most clearly applies to principles of law derived from statutes: see *Canadian Imperial Bank of Commerce v. Saskatchewan Lawyer's Insurance Association Inc.* (1990), 140 Sask. R. 114 (Q.B.).

[45] Accordingly, in the face of clear statutory provisions, equitable remedies cannot apply. Equitable remedies may co-exist alongside statutory provisions where statutory language permits. However, I am not satisfied that equitable remedies should be applied in this case in light of clear legal principles, and in light of the fact that the doctrine of marshalling is in clear conflict with the provisions of the *Insurance Act*, related legislation, and caselaw.

iii. A Claimant's Access to Other Insurance Funds is Irrelevant

[46] In the case of *Insurance Corp. of British Columbia v. Kushneriuk*, 2004 BCCA 440, the British Columbia Court of Appeal held that the existence of additional insurance available to satisfy the claims of some of the plaintiffs is an irrelevant consideration.

[47] In *Kushneriuk*, the moving party made an argument similar to the marshalling argument advanced by House. In that case, the motions judge decided that the most seriously injured of the three claimants should take 100% of the available first loss insurance proceeds rather than share with other claimants on a *pro rata* basis (which was effectively a form of marshalling). The Court of Appeal found that it was an error for the motions judge to consider other insurance coverage available to some claimants and to direct that the claimant who did not have access to the other insurance coverage should be paid out in full in priority to the other claimants. The most seriously injured plaintiff was only entitled to her *pro rata* share of the first loss insurance funds.

[48] While the factual circumstances may be compelling, the equitable principle House seeks is unavailable to him. I find that the doctrine of marshalling does not apply. The funds must be paid to the claimants on a *pro rata* basis. The Court does not have discretion to order that the funds be paid on a different basis.

C. Enforceability and Ambiguities in the Baird Settlement

[49] House submits that the Baird settlement has not been approved by the court and is, therefore, unenforceable. House was a person under disability at the

time of the settlement and was represented by a litigation guardian. Court approval of the settlement is required pursuant to Rule 7.08 of the *Rules of Civil Procedure*, R.R.O 1990, Reg. 194. For reasons that are unclear, no one has sought court approval of the Baird settlement.

[50] For purposes of this motion, I shall treat the Baird settlement as enforceable, for the following reasons:

- a) The Baird settlement tracks the language of the Samms settlement, including the *pro rata* distribution between the plaintiffs. The Samms settlement was approved by the court.
- b) All parties were represented by counsel at the settlement meetings, including defence counsel for House.
- c) Although House's plaintiff counsel was not present at the settlement meetings, he was advised of the Baird settlement. He did not raise any objections and stated that the quantum of the settlement was reasonable.
- d) House has not moved to set aside the Baird settlement, which was reached almost five years ago.
- e) The paragraphs of the Baird settlement stating that the plaintiffs in all actions would be paid on a *pro rata* basis is consistent with the *Insurance Act*. These paragraphs were designed to avoid the outcome in the *Scale Estate* decision.

[51] The Baird settlement is silent with respect to apportionment of damages. After hearing initial submissions from the parties, the court provided the parties with an opportunity to provide evidence establishing a breakdown of the heads of damages included in the Baird settlement.

[52] Baird's counsel, Bernard Verbanac, filed a supplementary affidavit. In addition, Nordique's counsel, Brian Smith, filed an affidavit. House primarily objects to the affidavit of Mr. Smith and argues that it breaches the parol evidence rule. The court permitted the affidavit to be filed, with its weight to be determined at a later point.

[53] The parol evidence rule precludes admission of evidence outside the words of the written contract that would add to, subtract from, vary, or contradict a contract that has been wholly reduced to writing. The rule precludes, among other things, evidence of the subjective intentions of the parties. The rule developed from the desire to have the nullity and certainty in contractual obligations. One of the exceptions to the parol evidence rule is that, where there is ambiguity in the written contract itself, extrinsic evidence may be admitted to clarify the meaning of the ambiguous terms: see *Sattva Capital Corp. v. Creston Moly Corp.*, [2014] 2 S.C.R. 633; and *C.J.A. Local 579 v. Bradco. Construction Ltd.*, [1993] 2 S.C.R. 316.

[54] The Baird settlement contains terms that are arguably ambiguous terms. This falls into the exception to the parol evidence rule, and extrinsic evidence is admissible to clarify the meaning of the written settlement.

[55] The affidavits addressed two areas of potential ambiguity in the Baird settlement:

i. Whether Nordique Agreed to Pay any Shortfall to all of the Plaintiffs

[56] In response to a question from the court, counsel for House argued, for the first time, that paragraph 6 of the Baird settlement should be interpreted to mean that Nordique agreed to pay any shortfall in the insurance proceeds to all of the plaintiffs, including House, after State Farm had paid out its policy limits.

[57] The affidavit of Mr. Smith speaks to his understanding, as Nordique's counsel, of the meaning of the word "plaintiffs" in paragraph 6 of the Baird settlement. Counsel states that this paragraph was never intended to include House. I give this portion of the affidavit little weight. Counsel's own intentions do not really assist me in interpreting the ambiguous language of the agreement.

[58] However, other extrinsic evidence and additional considerations lead me to conclude that the word "plaintiffs" in paragraph 6 includes only the Baird plaintiffs, and cannot be interpreted as a promise by Nordique to pay any shortfall in damages to all of the plaintiffs. I have considered the following:

- a) House made submissions on this motion that the House plaintiffs were not parties to the Baird negotiations and settlement, and he did not have counsel at the settlement meeting. He stated that he does not agree with the Baird settlement, and Nordique breached its duty of care toward him when it entered into that settlement. House has always taken the position that the Baird settlement is detrimental to his position as plaintiff in this litigation.
- b) Because of s. 277 of the *Insurance Act*, Nordique has no obligation in law to pay any shortfall in damages to House. There would be no reason for Nordique to give such an unlimited, gratuitous promise to pay damages to House once the State Farm policy limits were exhausted. In addition, Nordique received no contractual consideration from House for such an agreement.
- c) None of the parties interpreted paragraph 6 to include House as one of the plaintiffs. House appealed the trial ruling dismissing his claim against the Township (seeking indemnification from the Township). He argued the doctrine of marshalling before me and stated that House would have a substantial shortfall if I did not direct that State Farm pay House in priority to the other plaintiffs. It would make no sense for House to take these steps if he believed that paragraph 6 meant that he would be fully paid by Nordique.

[59] Although the word “plaintiffs” in paragraph 6 of the Baird settlement is arguably ambiguous, I have considered the wording of the entire agreement and the surrounding circumstances. All of the parties conducted themselves according to the interpretation that paragraph 6 did not include a promise by Nordique to pay any shortfall in damages to all of the plaintiffs. I interpret paragraph 6 to reference the Baird plaintiffs only.

ii. Heads of Damages Included in the Settlement

[60] The affidavit of Mr. Verbanac addresses the heads of damages in the Baird settlement. The affidavit provides some context to the settlement discussions,

which assists me in exercising my discretion in apportioning the damages for the purpose of the garnishment hearing. I shall address this further below.

D. Whether House Can Garnish the Baird Settlement Funds

[61] Even though there is a shortfall in the insurance proceeds available to House, he still has the right to collect the remaining damages from Baird personally. House has issued two Notices of Garnishment, seeking to garnish insurance proceeds payable to Baird. One Notice has been issued with State Farm as the Garnishee and the other with Nordique as the Garnishee. House seeks a declaration that any insurance funds that Baird is set to receive from the settlement are not exempt from attachment or execution. On the other hand, Baird submits that the settlement funds are not subject to garnishment.

[62] Pursuant to Rule 60.08(16) of the *Rules of Civil Procedure*, the court has the discretion to determine rights, liabilities or any matter in relation to the garnishment. The Baird settlement set damages at \$500,000. It does not define the heads of damages breakdown. Baird acknowledges that it is his onus to show that the settlement is exempt from garnishment.

[63] Since Rule 60.08(16) grants the court discretion to determine any matter, I shall exercise my discretion to determine the distribution of settlement funds in order to determine what portion, if any, can be garnished. There is no settled approach to how the categories of damages should be allocated to out of court settlements. Where settlements are not broken into constituent components, the court may allocate the settlement into the heads of damages as best it can. This entails examining any evidence of the settlement negotiations.

[64] I have reviewed the affidavit of Baird's counsel. Baird's Pre-Trial Memorandum suggested that Baird was entitled to approximately \$2.9 million, which was divided as follows: 7% for general damages; 49% for future care costs; 41% for past and future income loss (Baird was not receiving income replacement benefits at the time); and 3% for the *Family Law Act* claim.

[65] Baird's counsel acknowledges that the parties treated the \$500,000 settlement as an all-inclusive figure. He has no knowledge of how the defendants arrived at the figure and/or what (if any) specific heads of damages were considered in arriving at the sum of \$500,000. He states that he advised his clients to accept the \$500,000 offer as he believed it to be an appropriate amount, taking into account Baird's injuries, future care costs, potential future income loss, loss of competitive advantage, and the potential risks associated with trial.

[66] The absence of any apportionment of the heads of damages in the settlement (in particular, the quantum of future income and/or future care costs) benefited Baird. This allowed Baird to maximize his claim for income replacement benefits through his statutory accident benefit entitlements.

[67] Baird's accident benefits matter was settled on August 2, 2017, for a total of \$500,000. The accident benefits settlement was structured with 50% as income replacement benefits and 50% for medical and rehabilitation benefits.

[68] Baird's accident benefits claim settled four months before the notices of garnishment were served on State Farm, and Baird has received a lump sum accident benefit payout. The garnishment hearing before me relates to a request to garnish funds that Baird stands to receive from his settlement of the court action.

[69] At the time of settlement, Baird's counsel clearly considered income loss to be a substantial portion of any court settlement. This position is reflected in the apportionment of damages as set out in the Pre-Trial Memorandum. It is also reflected in the fact that counsel considered it to be beneficial to Baird that the settlement be an all-inclusive figure.

[70] In all the circumstances, I find that it is appropriate to designate 50% of the Baird settlement for general damages, future care costs, and the *Family Law Act* claim. I find that this portion of the settlement should be exempt from garnishment, for the following reasons:

- a) Garnishment is an equitable remedy. As such, the court has jurisdiction to exempt personal injury damages for pain and suffering from garnishment under Rule 60.08(16). The parties agree that damages for pain and suffering are not subject to garnishment: see *Mullin v. R-M & E Pharmacy* (2005), 74 O.R. (3d) 378 (S.C.).
- b) Damages that are personal in nature (such as damages for pain and suffering, future care, and housekeeping) are not ordinarily subject to seizure by creditors: see *Conforti (Re)*, 2015 ONCA 268.

[71] I designate the remaining 50% of the settlement as income loss. The question of what portion of income loss can be garnished requires further analysis.

[72] Baird agrees that, if a portion of the settlement is found to be lost income or loss of competitive advantage, it can be garnished. However, he argues two possible ways in which the court should limit the garnishment of the lost income.

[73] First, Baird attempts to draw an analogy to caselaw dealing with future income loss awards in the bankruptcy context. He submits that the court should apportion funds for lost income from the date of settlement to the date of his notional bankruptcy discharge, relative to Baird's estimated remaining work life. He argues that the court should consider how much of a bankrupt's income would be available to creditors when determining what portion of the settlement should be garnished.

[74] In the bankruptcy context, future income funds can be pro-rated from the discharge rate over the estimate of debtor's working life. Lost future earning capacity has also been considered to be a replacement for earned income, and thus, falls under s. 68 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3. As such, it does not accrue fully to the trustee: see *Conforti (Re)*.

[75] I do not accept the submission that the lost wages portion of the settlement should be pro-rated in this fashion. The bankruptcy cases are distinguishable from the case before the court. There are different policy

considerations that apply in the context of a bankruptcy. Courts have applied the *Bankruptcy Act* in a manner that is consistent with the “fresh start” principle. The *Act* is not intended to require payments by the bankrupt to the estate after the bankrupt's discharge. To require payment of any of the amount of future loss of wages to the estate would bring about this result. Accordingly, while the future loss amount may be property, it is not property that may be acquired by or devolved on the bankrupt before his discharge: see *Re Anderson*, 2004 ABQB 349, 358 A.R. 183 .

[76] The *Creditors' Relief Act*, 2010, S.O. 2010, c. 16, Sched. 4, does not contain the same provisions as the *Bankruptcy and Insolvency Act*. The purpose of the *Creditors' Relief Act* is to allow creditors to collect overdue debt without resorting to legal action. It allows all creditors to gain from the benefit of a proceeding, effectively extinguishing the priority of the execution creditor who first seized property: see *I.J.T. Holdings Ltd. v. Saskatchewan (Sheriff of the Judicial Centre of Moose Jaw)* (1998), 171 Sask. R. 273 (Q.B.).

[77] As a secondary argument, Baird submits that the *Wages Act*, R.S.O. 1991, c. W.1, applies to damages for lost income and that at least 80% of the portion that is considered wages should be exempt from garnishment. The *Wages Act* states that payments from insurance that is intended to replace income lost because of disability shall be deemed to be wages. 80% of a person's wages are exempt from seizure or garnishment. A judge may order that the exemption be increased or decreased if satisfied that it is just to do so, having regard to the nature of the debt owed to the creditor, the person's financial circumstances, and any other matter the judge considers relevant: see s. 7.

[78] The parties were unable to find caselaw to assist with the issue of whether insurance settlements are considered to be “wages” under the *Wages Act*. However, there are principles found in the caselaw that provide some assistance:

- i. Income replacement benefits under the SABS are wages within the meaning of the *Wages Act*: see *Lease Truck Inc. v. Serbinek*, [2008] O.J. No. 4700 (S.C.).
- ii. Periodic payments to a doctor under OHIP are not wages. The court can consider the debtor's monthly expenses and designate a portion of OHIP payments as exempt from garnishment, pursuant to Rule 60.08(16): see *Hongkong Bank of Canada v. Slesers* (1992), 7 O.R. (3d) 117 (S.C.).
- iii. Damages for wrongful dismissal are wages within the meaning of the *Wages Act*: see *Landry (Re)* (2000), 135 O.A.C. 381 (C.A.).

[79] Although not dealing with the *Wages Act*, the analysis in the decision of *Re Conforti* provides some analogous direction. In discussing the operative legal framework under the *Bankruptcy Act*, the court held examples of payments that are encompassed by the s. 68(2)(a) definition of total income include lost wages and disability payments.

[80] When considering the garnishment of income, the court should strike a balance between the interests of the creditors in obtaining an expeditious payment in full of the amounts owed to them and the ability of debtors to continue to earn money that will be used to discharge their debts and support themselves and their dependents: see *Dhaliwal v. Ontario (Ministry of Health and Long Term Care)*, [2002] O.J. No. 4717 (S.C.).

[81] It is not a requirement of the *Wages Act* or the caselaw that wages can only be received in the form of periodic payments or only from an employer. I find that the *Wages Act* applies to the lost income portion of the Baird settlement. Even if I am wrong about the application of the *Wages Act*, I would apply a similar analysis under Rule 60.08(16) and deem a portion of the funds to be exempt from garnishment.

[82] In this case, no one disputes that Baird was seriously injured in the accident, which may limit his ability to earn an income in the future. The lost income portion of the settlement will allow Baird to support himself and his dependents (if

any). However, Baird has not provided his own affidavit setting out to what extent he is unable to work in the future or whether he has other assets or income available to him. It is notable that Baird has already been paid lump sum income replacement benefits from his insurer that cannot be garnished from the insurer.

[83] Both the *Wages Act* and Rule 60.08(16) give the court discretion to decrease the exemption from garnishment. I find that it is appropriate that 60% of the lost income portion of the Baird settlement should be exempt from garnishment. Since half of the settlement is entirely exempt, the net result is that 80% of the entire settlement is immune from attachment and execution. House may garnish 20% of the Baird settlement from State Farm and Nordique.

IV. ORDERS

[84] For all of these reasons, the court makes the following orders and directions:

1. The State Farm policy limits of \$1 million is first loss insurance and shall be apportioned on a *pro rata* basis to satisfy settlements and judgments against House (as a defendant in the Baird and Samms actions) and against Baird (as a defendant in the House and Samms actions). The judgment of House in this action shall be pro-rated with the judgment in the Samms action C-570-10 and with the settlement in the Baird action C-570-10.
2. After the State Farm policy has paid out its policy limits on a *pro rata* basis, the Nordique policy shall then pay the remaining additional damages to Baird and to the Samms family, up to the policy limits of \$1 million.
3. House shall be entitled to garnish 20% of the settlement funds payable by State Farm and Nordique to Baird.
4. The parties shall mutually agree on the quantum of payments within 30 days or such other time period as agreed to by all interested parties.
5. In the event that the parties cannot agree on the pro-rated figures within 30 days, the parties shall submit written submissions within 60 days of this ruling and I will determine the pro-rated amounts. If further direction is required from the court on any other issue, the parties may provide me with written submissions within the same time frame. The court may direct a further attendance, if required, to address the issues in dispute.

V. COSTS

[85] Nordique and Baird have been more successful than House on this motion. The Samms family took no position, but attended to ensure that their interests were protected.

[86] In the event that the parties cannot agree as to costs, they are directed to provide written submissions. The submissions shall be no longer than two typed

pages, double-spaced, in addition to any relevant Bill of Costs and Offers to Settle. Nordique, Baird, and the Samms family shall provide costs submissions first and House shall respond two weeks later. In light of the fact that further submissions may be required, the parties shall agree on a timetable for costs submissions and file that timetable with the court.

Braid, J.

Released: March 15, 2019

CITATION: House v. Baird, 2019 ONSC 1712
COURT FILE NO.: C-1092-09
DATE: 2019-03-15

ONTARIO

SUPERIOR COURT OF JUSTICE

B E T W E E N:

TYLER HOUSE BY HIS LITIGATION
GUARDIAN GAIL HOUSE, THE ESTATE
OF TITUS HOUSE, GAIL HOUSE and
TITUS HOUSE JR.

- and -

DONALD BAIRD, ROBERT SCOTT
MURRAY and THE CORPORATION OF
THE TOWNSHIP OF WILMOT

REASONS ON MOTION

CDB

Released: March 15, 2019

TAB 3

COURT OF APPEAL FOR ONTARIO

FINLAYSON, WEILER and MOLDAVER JJ.A.

B E T W E E N :

IRVING GREEN, IRVING GREEN	)	S. Harvey Starkman, Q.C. and
IN TRUST and BOSTON	)	Kevin Fisher for the appellants
CONSTRUCTION INC.	)	
	)	
(Appellants)	)	
	)	
-and-	)	
	)	
BANK OF MONTREAL and THE	)	Irving Marks and Adam Babker,
CORPORATION OF THE TOWN OF	)	for the respondent Bank of
Montreal	)	
AJAX	)	
	)	N. Cameron Murkar, for the
(Respondent)	)	respondent The Corporation of the
	)	Town of Ajax
	)	
	)	Heard: November 18, 1999

On appeal from the judgment of Sachs J. dated February 26, 1999.
FINLAYSON J.A.:

[1] This is an appeal from the summary judgment of the Honourable Madam Justice Sachs dated February 26, 1999, wherein she awarded the Bank of Montreal ("Bank") \$212,152.05 and upheld the assignment to the Bank by the Corporation of the Town of Ajax ("Town") of a portion of its municipal lien created under a subdivision agreement for a plan of subdivision in the Town.

[2] The appellants were the original owners of the properties in issue in this action. They sold the property to a developer and took back a mortgage as part of the purchase price. The appellants, the developer, the Town and the Bank executed the subdivision agreement. The Bank had provided the developer with credit facilities amounting to \$15,000,000. The credit included commercial letters of credit totalling \$3,500,000 issued by the Bank to the Town to provide guarantees for the performance by the developer of his obligations under the land servicing arrangements. The security arrangements of all the parties consisted of the following:

- i) the Bank held a \$15,000,000 first charge pursuant to a debenture on the residential portion of the subdivision referred to as the housing lots;
- ii) the appellants had a collateral second mortgage on the housing lots for \$700,000;
- iii) the appellants had a first mortgage over the portions of the property known as the school block, the apartment block and

the
commercial block;

iv) the Town was given a first lien over all of the property as security for any obligation of the developer under the subdivision agreement. Both the Bank and the appellants agreed to postpone and subordinate their respective security interests to the lien of the Town.

v) the Bank received a conditional assignment by the developer of all contracts and agreements including a profit sharing agreement the developer had with two builders.

[3] The developer became insolvent and defaulted on its obligations to the Bank and on its mortgage to the appellants. A receiver was appointed. The appellants exercised their power of sale under their mortgage that covered the school block and agreed to sell the property to the School Board. One of the problems that emerged was that the developer had stock piled topsoil on the school block and this had to be removed. The question arose as to who was to assume the burden and the cost of removing the topsoil.

[4] The Town made a demand on the developer to remove the top soil and to grade and seed the school block and stated that if this was not done, it would call on the letters of credit provided by the Bank to complete the necessary work. The Bank then agreed to complete the grading of the school block and in exchange the Town agreed to assign to the Bank its first charge over the school block.

[5] The effect of this assignment was that the Bank had acquired the first security interest of the Town in the school block and on the closing of the sale to the School Board, it insisted upon being reimbursed for the cost it had incurred in carrying out the obligations of the developer with respect to the school block. In order to close the sale, the parties agreed that the amount in dispute would be paid into a trust account pending the determination of the right of the parties.

[6] The appellants initiated this action for a declaration that the transfer of the Town's municipal lien to the Bank was of no force or effect. The respondents moved for summary judgment to dismiss the appellants' action with costs and for the release of the monies paid into trust sufficient to pay out what was now the Bank's lien on the school block.

[7] The appellants' position was that the Bank's actions in obtaining a transfer of the Town's lien was merely an attempt to shift the Bank's financial obligations to the appellants, for the Bank had provided the Town with irrevocable and unconditional letters of credit and agreed to pay the Town for the same obligations which the Bank sought to enforce against the appellants.

[8] The motions judge found that the Town had the authority to enter into the subdivision agreement and to assign its lien created thereby to the Bank. No serious complaint was made in

this court as to these findings. To the extent that the issues were raised in the factum of the appellant, I would accept the reasoning of the motions judge that the authority existed in both cases. The real complaint, here and below, was that somehow the Town had improperly preferred the Bank over the appellants by declining to call on the Bank to honour its letters of credit to pay for the cost of removing the topsoil from the school block. In my view, this approach was totally misconceived. Absent any express agreement restricting the manner in which the security holders could realise on their respective securities, they were all entitled to act in their own best interests. If the Town thought that its interests were best served by having the Bank take over the grading responsibilities of the developer rather than engaging contractors to do the work for the Town and claiming against the Bank under its letters of credit, it was entitled to do so. If the Bank was prepared to take on this responsibility in return for upgrading the quality of its security, there is no reason why it should not have done so.

[9] The appellants argued that, on their reading of the subdivision agreement, the Town was obliged to have recourse to the letters of credit provided by the Bank in enforcing its rights against the insolvent developer and that it could only rely upon its first lien rights on exhausting those letters of credit. The agreement certainly does not say that this is the case and it is now conceded that there were no representations by the Bank or any one else to that effect. This brings the appellants to their primary argument that the court as a matter of equity should bring about the same result by invoking the equitable doctrine of marshalling.

[10] As has been stated by this court in *Re Allison* (1998), 38 O.R. (3d) 337 at p.341, citing *Aldrich v. Cooper* (1803), 8 Ves. 382, 32 E.R. 402 (L.C.), the right to marshal securities is an equitable one intended to prevent a creditor who can resort to two funds of a debtor from defeating another creditor who can resort to only one of them. Fundamentally, the doctrine is applied for the purpose of regulating the rights of the two creditors among themselves, although in so regulating their rights the court will never interfere with the paramount claim of the superior creditor (the one which has the choice of the two funds of the debtor from which to collect) to pursue his or her remedy against either fund, but provides that if he or she resorts to the fund which the inferior creditor can alone resort, then the inferior creditor shall not be prejudiced. The doctrine is applicable unless some other equity prevents its application such as in the case where its application would prejudice third parties. There are five criteria: (a) two creditors; (b) one common debtor; (c) two funds of the debtor with the superior creditor having access to both and the inferior creditor to but one; (d) no interference with the choice of remedy of the superior creditor and (e) no prejudice to third parties.

[11] There are a number of reasons why the doctrine of marshalling has no application here. In the first place, marshalling will not permit the court to instruct the Town that it must choose one avenue of relief over another. In the second place, the Town was not attempting to recover a debt from the developer, it was attempting to have remedied a default of the

developer by having someone remove top soil from the school block so that it would be useable for school purposes. The issue of how it would be recompensed would only come up if it chose to do the work itself. As we know, however, it did not make this choice but instead chose to assign its lien to the Bank in return for the Bank's commitment to see that the work was done. In the third place, there was no common debtor for both "funds". Even assuming that the letters of credit and the lien could be treated as sources of funds for the purposes of this doctrine, while the Town had access to the two funds, only one of them was a resource of the debtor. That resource was the school block and the money that its sale would represent. The letters of credit were an obligation of the Bank to the Town. While admittedly access by the Town to the letters of credit could only be triggered by the default of the developer, it was the Bank, not the developer, which would become the debtor on the happening of that event. Accordingly, there was no common debtor to the appellants and the Town with respect to the two funds that the Town had access to such as to permit the invocation of the doctrine of marshalling. Fourthly, the effect of the order sought would prejudice the Bank, which is a third party to the marshalling scheme.

[12] In summary then, there are three parties that are affected by the insolvency of the developer: the Town, the appellants and the Bank. All are creditors. The doctrine of marshalling does not permit the court to prefer the rights of one creditor to another. It cannot dictate to the Town which of a number of options it must exercise in order to protect the appellants at the expense of the Bank because to do so would not only interfere with the paramount claim of the Town as the superior creditor, it would prejudice the rights of the Bank. In this instance, the appellants are asking the Town to do two things: first to do the work itself and second to make a claim against the security it holds from the Bank. The Town apparently thought it would be more advantageous to its interests to arrange to have the Bank remove the topsoil in return for its first lien on the property affected. In this way it had no responsibility to see that the work was properly done and it retained the full value of its security with the Bank against any other defalcations by the developer. What this analysis discloses is that the appellants are asking the court to unscramble this omelette at the behest of one creditor to the detriment of the other two. The sole beneficiary of such an order would be the appellants who would receive the full proceeds of the sale of the school block. The equitable doctrine of marshalling offers no support for this request and I see no basis at all to provide the appellants with the relief that they seek.

[13] Accordingly, for the above reasons, I would dismiss the appeal with costs.

Released: DEC 06 1999
GDF

Signed: "G.D. Finlayson J.A."
"I agree K.M. Weiler J.A."
"I agree. M.J. Moldaver J.A."

TAB 4

Court of King's Bench of Alberta

Citation: Griffon Partners Operation Corporation (Re), 2024 ABKB 277

Date: 20240514
Docket: 2401 01422
Registry: Calgary

2024 ABKB 277 (CanLII)

In the Matter of the *Companies' Creditors Arrangement Act*, RSC 1985,
c C-36 as amended;

And in the Matter of the Compromise or Arrangement of Griffon Partners
Operation Corporation, Griffon Partners Holding Corporation, Griffon Partners
Capital Management Ltd., Stellion Limited., 2437801 Alberta Ltd.,
2437799 Alberta Ltd., 2437815 Alberta Ltd., and Spicelo Limited

**Griffon Partners Operation Corporation, Griffon Partners Holding Corporation,
and Griffon Partners Capital Management Ltd., Stellion Limited, 2437801 Alberta Ltd.,
2437799 Alberta Ltd., 2437815 Alberta Ltd. and Spicelo Limited**

Applicants

**Reasons for Decision
of the
Honourable Justice L.K. Harris**

I. Introduction

[1] Griffon Partners Operation Corporation (“GPOC”), Griffon Partners Holding Corporation (“GPHC”) and Griffon Partners Capital Management Ltd. (GPCM”) (collectively, the “Griffon Entities”) are private corporations registered in Alberta, engaged in the exploration and development of oil and gas in Alberta and Saskatchewan. In August 2023, the Griffon Entities each filed a Notice of Intention to Make a Proposal under the *Bankruptcy and Insolvency Act*, RSC 1985 c B-3 (“NOI”). The NOIs were filed in response to senior secured creditors to GPOC demanding payment under a loan agreement between those creditors and GPOC.

[2] An issue has now arisen as to the order in which the senior secured creditors should realize upon their security. A junior secured creditor argues that the principle of marshalling applies so that some security is preserved for them. The Applicants argue that marshalling is not available in this case. They say that marshalling has never been applied in these factual circumstances, and that even if marshalling were available, it would be pointless because the doctrine of subrogation would then apply to extinguish any ability of the junior secured creditor to recover.

[3] The question I must resolve is whether marshalling is available in this case. If it is, then I must go on to resolve the question of whether there is a right of subrogation available which would effectively extinguish the subordinate creditor's claim in any event.

II. Background

[4] GPHC and GPOC are wholly owned subsidiaries of GPCM. All three entities share primarily the same directors, including Jonathan Klesch ("Klesch") (the exception being GPHC, which has an additional director).

[5] GPCM is, in turn, wholly owned by the four holding companies belonging to the four directors. Klesch's holding company is Stellion Limited ("Stellion"). Stellion is incorporated in the Republic of Cyprus and is extra-provincially registered in Alberta.

[6] Klesch also is the sole beneficial shareholder of a second corporation, Spicelo Limited ("Spicelo"), also incorporated in Cyprus and extra-provincially registered in Alberta. The only significant assets held by Spicelo are approximately 1.125 million shares in Greenfire, a private Alberta Corporation specializing in Western Canadian oil and gas.

[7] GPOC is the operating entity which holds all the Griffon Entities' interests and conducts all of the Griffon Entities' business and operations. GPOC acquired all its holdings from Tamarack Valley Energy Ltd ("Tamarack") in July 2022, for a total purchase price of \$70.0 million.

[8] GPOC's purchase from Tamarack was funded in part by financing pursuant to an Amended Credit Agreement between GPOC as the borrower and Trafigura Canada Limited and Signal Alpha C4 Limited as lenders (the "Lenders"). Pursuant to the Amended Credit Agreement, the Lenders made available a non-revolving, single advance term loan facility in the maximum principal amount of US\$35,869,565.21. The Lenders were granted security over all GPOC's present and after-acquired property.

[9] GPCM and GPHC are guarantors under the Amended Credit Agreement. The Directors' four holding companies are also guarantors under a Limited Recourse Guarantee and Securities Pledge Agreement. Finally, Spicelo is a guarantor pursuant to a Limited Recourse Guarantee and Securities Pledge Agreement (the "Spicelo Guarantee"). The Spicelo Guarantee is generally limited to the securities held by Spicelo in Greenfire.

[10] GPOC's purchase from Tamarack was also funded in part pursuant to a Subordinated Secured Promissory Note for \$20.0 million issued by GPOC to Tamarack (the "Subordinated Tamarack Note"). The Subordinated Tamarack Note is secured against all present and after-acquired property of GPOC. Tamarack agreed to subordinate all security interests granted under the Subordinated Tamarack Note to all senior loan obligations to the Lenders under the Amended Credit Agreement.

[11] Tamarack has no security interest in Spicelo or the Greenfire shares, and Spicelo owes no obligations to Tamarack.

[12] In late 2022, GPOC ran into financial difficulties and defaulted on its payments due under the Amended Credit Agreement. Efforts to refinance or restructure the business were unsuccessful, and on August 16, 2023, the Lenders served Demands for Payment and Notices of Intention to Enforce Security pursuant to s 244 of the *BIA*.

[13] On August 25, 2023, the Griffon Entities responded by each filing an NOI, stating that the Griffon Entities' business was viable and had significant value, and that the Lenders and Tamarack were over-collateralized.

[14] On October 18, 2023, the Court granted an Order approving a Sale and Investment Solicitation Process ("SISP") pursuant to which the assets of GPOC were to be sold. The SISP is nearing completion, but it appears that the proceeds from the sale of the GPOC assets will not be sufficient to satisfy the full amount outstanding to the Lenders, let alone the amount owed to Tamarack. This will necessitate a liquidation of at least some of the Greenfire shares held by Spicelo.

[15] Tamarack objects to the Lenders realizing upon the proceeds from the SISP first because all of those proceeds will be used to satisfy GPOC's obligations to the Lenders, leaving nothing to satisfy GPOC's obligations to Tamarack. Tamarack says that the Lenders should resort to its security against the Spicelo assets first (as a guarantor for the GPOC indebtedness) then the proceeds from the SISP, leaving something to satisfy GPOC's obligations to Tamarack under the Subordinated Tamarack Note.

[16] On March 15, 2024, the Griffon Entities, the Directors' four holding companies and Spicelo filed an Application for a declaration that:

- (a) Tamarack has no claim against the assets of Spicelo;
- (b) The Lenders are not required to exhaust their remedies pursuant to the Spicelo Guarantee prior to realizing on the proceeds from the SISP; and
- (c) Spicelo is subrogated to the Lenders' security against GPOC in priority to Tamarack.

[17] The Application is opposed by Tamarack. The Lenders take no position, saying they simply wish to have the Court's direction as to which security should be realized first.

III. Analysis

a. The General Principles of Marshalling

[18] The equitable doctrine of marshalling is described by Manderscheid, J in *Gerrow v Dorais*, 2010 ABQB 560 at para 21:

In its simplest form the doctrine of marshalling dictates that if a creditor has two funds to draw upon to satisfy the debt, the Court will require him to take satisfaction from that fund upon which another creditor has no security.

[19] Manderscheid J notes that the "seminal" case on marshalling in Alberta is *First Investors Corporation Ltd. v Veeradon Developments Ltd.*, 1988 ABCA 38. There, Belzil JA sets out the "leading formulation of the doctrine of marshalling" as a principle of equity:

The leading formulation of the doctrine of marshalling as a principle of equity is that of Lord Hardwicke in *Lanoy v The Duke and Dutchess of Athol* (1742). 2 Atk. 444. He said at p 669:

“It is not then the constant equity of this court that if a creditor has two funds, he shall take his satisfaction out of that fund upon which another creditor has no lien. (*Vide Clifton v Burt*, 1 Cox’s P.W. 679, note 1. *Gallon v Hancock*, ante, 436, 438. *Martin v Martin*, 1 Ves. 212.)

Suppose a person, who has two real estates, mortgages both to one person, and afterwards only one estate to a second mortgagee, who had no notice of the first; the court, in order to relieve the second mortgagee, have directed the first to take his satisfaction out of the estate only which is not in mortgage to the second mortgagee, if that is sufficient to satisfy the first mortgage, in order to make room for the second mortgage, even though the estates descended to two different persons.”

[20] See also *Condominium Corp No 082 6970 v 1117398 Alberta Ltd*, 2012 ABQB 233 and *Wolfe et al v Taylor et al*, 2020 MBCA 44.

[21] There are criteria which must be met before marshalling becomes available. In *House v Baird*, 2019 ONSC 1712 (CanLII) at para 39 the Court states:

A number of common law rules have developed in the application of marshalling, although its equitable nature enables courts to craft relief appropriate to each case. There are five preconditions for marshalling:

- (a) two creditors;
- (b) one common debtor;
- (c) two funds of the debtor with the superior creditor having access to both and the inferior creditor to but one;
- (d) no interference with the choice of remedy of the superior creditor; and
- (e) no prejudice to third parties.

[22] Considering whether these criteria are met in this case, there certainly is a senior creditor (the Lenders) and a junior creditor (Tamarack), but there is not a single debtor with two funds. Rather, there is one debtor indebted to both creditors (GPOC) and one surety having provided a guarantee only to the Lenders (Spicelo).

[23] Neither *Gerrow, Condo Corp* nor *First Investors* directly address the question of when it might be permissible to apply the doctrine of marshalling in cases where there is more than one debtor. This point was raised in *Strategic Acquisition Corp. v Multus Investment Corporation*, 2013 ABQB 534 at paras 13-14:

The principle of marshalling is straightforward. Where there are two creditors of the same debtor and one of those creditors has the ability to recover from two funds of the debtor and the other creditor only has resort to one, the court will

marshal the funds to pay out both creditors as much as possible. A first mortgagee, however, cannot be prejudiced by marshalling: *Snell's Principles of Equity*, 28th ed, at 416, cited in **First Investors Corp. v Veeradon Developments Ltd**, 1988 ABCA 38 (CanLII), 47 DLR (4th) 446, 84 AR 364 at para 11 (ABCA).

There is nothing in the doctrine that says that both creditors must be secured or mortgagees and there is nothing that says that it only operates where there is one debtor rather than related debtors...

[24] The issue before the Court in **Strategic Acquisition** was a summary judgment application. The statement above is *obiter*. There are other authorities however which do provide guidance on the issue of whether there is an exception to the single-debtor rule, and under what circumstances that exception might be employed.

b. The Exception to the Single-Debtor Rule

[25] In **Ernst Brothers Co. v Canada Permanent Mortgage Corporation** (1920) 47 OLR 362 at pp 367-8, affirmed 57 DLR 500 (CA) the Court affirms the general principles of marshalling, but in a situation where there were multiple debtors. In **Ernst Brothers**, two brothers each owned a lot of land which they each mortgaged to a single mortgagee to secure a single loan. One of the brothers then created a charge on his lot for a second loan before selling his lot to his brother. The Court concluded that the doctrine of marshalling applied.

[26] Another Ontario case considering multiple debtors is **807933 Ontario Inc. v Paddon and Associates**, 1998 CanLII 3766. There, a mortgagee obtained security from two property owners (who were spouses) as security for a single debt. Each property owner also cross-guaranteed each other's mortgage. A second secured creditor for one spouse sought an order directing marshalling, requiring the mortgagee to recover from the security on the property of the other spouse. The Court states:

The key issue in the case on appeal is whether Mr. and Mrs. Allison were common debtors to the appellant. While it is conceded that they were common debtors to Tomas, it would appear to me on the facts of the case that only Mr. Allison was a debtor of the appellant and all the other creditors whose claims arose out of the Meaford Project. Mrs. Allison had nothing to do with those debts. If the court was to apply the doctrine of marshalling to Mrs. Allison's Parcel A so that Mr. Allison's Parcel B will be available to satisfy the appellant, then Mrs. Allison would be forced to pay her husband's debts for which she is not in law obligated. Marshalling was not intended to create such an inequity between two debtors. (emphasis added).

[27] The Court in **Paddon** distinguished **Ernst Brothers** on its facts because in **Ernst Brothers**, both brothers executed the mortgage, and it was registered on both lots. Both covenanted to repay the full amount of the mortgage, and so there was no inequity in compelling one brother to pay the full amount owed.

[28] **Paddon** does note that the trial judge's decision in **Ernst Brothers** explains why marshalling may be used only in some cases where there are multiple debtors. The trial judge in **Ernst Brothers** concluded, at p 371, that "[i]t would be inequitable to permit the securities to be marshalled if in the result one who was not under any obligation to pay both debts should suffer".

[29] In *Paddon*, the Court goes on to state:

Unless the appellant can establish that it is just and equitable that Mrs. Allison should pay in the first instance, it has no equity to compel a person such as Tomas, who has resort to both funds, to go against Mrs. Allison's parcel of land.

[30] The exception to the single debtor rule was employed in *Brown v Canadian Imperial Bank of Commerce* (1985) CanLII 2116 (ONSC) and in *G Ruso Construction Ltd. v Laviola* (1979), 27 Chitty's LJ 136. In *Brown*, Southey J found that marshalling did apply to a situation where there were two debtors that were in effect common since they were in a surety-principal relationship, i.e., the debtor facing the claims of two creditors was in effect a creditor of the second debtor. In *G Ruso Construction Ltd.*, the Court concluded that for marshalling to apply there must be a relationship or equities between the two debtors such that one debtor is entitled to require the other to be primarily liable to either of the creditors.

[31] There clearly is an exception to the general rule that there be one debtor. That exception appears to be that marshalling may be employed in cases involving more than one debtor when one of the debtors can put primary liability upon the other, for example, when the debtors are principal and surety: *Halsbury's Laws of England*, vol. 16, 4th ed (1980) at p 786, para 877. Such a relationship must exist, otherwise it would be inequitable to force one debtor to pay the other's debt when that debtor was not under any obligation to do so: *Paddon*.

c. Should the Exception to the Single Debtor Rule be Employed Here?

[32] The Griffon Entities point out that the facts of this case are distinct from the circumstances in which the exception to the single debtor rule was applied. In each of *Brown*, *G Ruso* and *Ernst Brothers*, the Court held that it was equitable to apply marshalling because the relationship between the debtors was such that primary liability could rest with the principal debtor. The Griffon Entities say that is not the case here. Tamarack does not disagree that the facts in this case are distinct from that scenario but argues that the flexibility of the doctrine of marshalling allows me to consider other circumstances, and that equity demands its application here. The Lenders are doubly secured and thus not prejudiced by marshalling. Tamarack says that there are no authorities that prohibit the position they are taking.

[33] Asserting that it is equitable to employ marshalling in this case simply because the Lenders are doubly secured misses the point. Further, although there are no authorities expressly prohibiting marshalling in these circumstances, this does not tell the entire story: the authorities do explain why there is only a limited exception to the single-debtor rule. The Court must be satisfied that one of the debtors is in a position to put primary liability upon the other – otherwise, it would be inequitable to enforce a debt against an entity who has no obligation to pay it. An example showing that marshalling is not so flexible as Tamarack argues is found in *Green v Bank of Montreal*, 1999 CanLII 821 (ONCA). We must look to whether there is a relationship between GPOC on one hand and Spicelo on the other such that it is equitable to compel the Lenders to enforce their security with Spicelo first, leaving some assets within the SISF for Tamarack.

[34] Tamarack argues that it is equitable to employ marshalling in this case for two reasons.

[35] First, it says that there is a close relationship between the Griffon Entities and Spicelo, pointing to Klesch's ownership role in and control of GPOC, Stellion and Spicelo, arguing that "there is effectively only one debtor."

[36] Second, Tamarack argues that I should consider the fraudulent and inequitable conduct of Klesch. Tamarack argues that Klesch caused GPOC to enter into the Subordinated Tamarack Note with no intention of repaying Tamarack and sought to disregard or discharge Tamarack's security interest in the course of the refinancing negotiations. Tamarack argues that corporate veils ought to be pierced in this circumstance to expose Klesch's involvement and justify marshalling as an exception to the single debtor rule. Tamarack has cited American authorities for this proposition: *Re Field*, 226 B.R. 178, 183 (*Bankr. D.S.C.* 1998) (quoting *Borges*, 184 B.R. at 879, n.3); *Fundex Capital Corp. v Balaber-Strauss* (In *Re Tampa Chain Co.*), 53 B.R. 772, 778-79 (*Bankr. S.D.N.Y.* 1985).

[37] Simply pointing to Klesch's role in the various corporate entities does not automatically create the relationship necessary for marshalling.

[38] Whether GPOC and Spicelo are truly affiliated companies as that term is used in the *Alberta Business Corporations Act*, RSA 2000 ch B-9 ("BCA") is debateable, as none of the criteria identified in s 2 of the BCA appear to be met. They do share a director in Klesch, but while Spicelo is wholly owned by Klesch, GPOC is wholly owned by GPHC, which in turn is wholly owned by GPCM. Stellion (Klesch's holding company) owns 25% of GPCM's Class A shares in addition to 79.5% of GPCM's Class B shares. So, while Stellion and Spicelo are both wholly owned by Klesch the corporate structure of the Griffon Entities does not allow the conclusion that there is an affiliation between GPOC and Spicelo such that one can conclude there is "effectively only one debtor". One cannot say that Spicelo and GPOC are truly "alter egos" of each other.

[39] Further, I am not persuaded that there are circumstances that permit me to lift corporate veils such that I may consider the actions of Klesch apart from those of the corporate entities.

[40] The concept of piercing a corporate veil was explained recently by the Alberta Court of Appeal in *Swanby v Tru-Square Homes Ltd*, 2023 ABCA 224, where the Court states starting at para 32:

The concept of separate legal personality was established in *Salomon v Salomon & Co*, [1897] AC 22, 22-32, 51-54 (HL), in which the court said: "either the limited company [is] a legal entity or it [is] not. If it [is], the business belong[s] to it and not to Mr. Salomon"; and further, "the company is at law a different person altogether from subscribers to the memorandum". That distinction is the "corporate veil" between the company and its owner.

The *Alberta Business Corporations Act*, RSA 2000, c B-9, ss 16(1), 46(1), provides for a corporation establishing a separate corporate personality from its shareholders, with no exception for single shareholder corporations. Additionally, the *Interpretation Act*, RSA 2000, c I-8, s 16, provides that the establishment of a corporation vests in the corporation the right to contract and be contracted with in its corporate name, makes the corporation liable to be sued in its corporate name, and exempts from personal liability individual members of the corporation.

Courts are generally unwilling to lift or pierce the corporate veil unless required to do so by statute or in the face of extraordinary circumstances: Kevin P McGuinness, *Canadian Business Corporations Law*, 3rd ed (Toronto: LexisNexis, 2017), vol 1, 7.47. It requires a court to disregard the fundamental

principle of separate identity and view the corporation as an “agent” or “puppet” of its controlling shareholder.

[41] Only in such extraordinary circumstances is the directing mind of a corporation is held to be responsible for the liabilities and obligations of the corporation.

[42] There are many Canadian decisions which describe circumstances in which it might be appropriate to lift the corporate veil in order to consider the actions of a shareholder. In **Kosmopoulos v Constitution Insurance Co**, 1987 CanLII 75 (SCC), [1987] 1 SCR 2 at p 10:

As a general rule a corporation is a legal entity distinct from its shareholders: **Salomon v Salomon & Co.**, [1897] A.C. 22 (H.L.) The law on when a court may disregard this principle by “lifting the corporate veil” and regarding the company as a mere “agent” or “puppet” of its controlling shareholder or parent corporation follows no consistent principle. The best that can be said is that the “separate entities” principle is not enforced when it would yield a result “too flagrantly opposed to justice, convenience or the interests of the Revenue”: L.C.B. Gower, *Modern Company Law* (4th ed. 1979), at p. 112.

[43] In **Driving Force Inc v I Spy-Eagle Eyes Safety Inc**, 2022 ABCA 25, the Court notes at para 53:

A frequently cited case is **Transamerica Life Insurance Company of Canada v Canada Life Assurance Company (1996)**, 1996 CanLII 7979 (ON SC), 28 OR (3d) 423, aff'd [1997] OJ No 3754 (CA). It concluded at p 431 that **Kosmopoulos** did not signal a departure from the traditional rule set out in **Salomon v Salomon & Co.**, [1897] AC 22:

There are undoubtedly situations where justice requires that the corporate veil be lifted. The cases and authorities already cited indicate that it will be difficult to define precisely when the corporate veil is to be lifted, but that lack of a precise test does not mean that a court is free to act as it pleases on some loosely defined “just and equitable” standard. . . (at p 433)

Transamerica confirms at pp 433-34 that mere control, which in this context means “complete domination”, is not sufficient to lift the corporate veil. There must additionally be some element of fraud, improper purpose, or improper activity which caused the plaintiff’s loss: see **Aubin v Petrone**, 2020 ABCA 13 at paras 23-26, 100 Alta LR (6th) 10; **Yaiguaje v Chevron Corporation**, 2018 ONCA 472 at paras. 67, 70, 141 OR (3d) 1, leave refused April 4, 2019, SCC #38183.

...

It is sometimes said that the corporate veil will be lifted where the corporation is merely a “sham”, or is just the “alter ego” of its controlling shareholders. This equally imprecise test is not often helpful, unless the corporation never, from the beginning, had any legitimate business or assets of its own and was merely being used as a pretext. As noted by Lord Neuberger of Abbotsbury PSC in **VTB Capital plc v Nutritek International Corp.**, [2013] UKSC 5 at para 124, [2013] 2 AC 337:

124. . . . Words such as “façade”, and other expressions found in the cases, such as “the true facts”, “sham”, “mask”, “cloak”, “device”, or “puppet” may be useful metaphors. However, such pejorative expressions are often dangerous, as they risk assisting moral indignation to triumph over legal principle, and, while they may enable the court to arrive at a result which seems fair in the case in question, they can also risk causing confusion and uncertainty in the law. . . .

...

One thing is clear. It is an error of principle to equate “control” of the corporation with the corporation merely being the alter ego of the shareholders. The *Alberta Business Corporations Act*, RSA 2000, c. B-9, permits “one person corporations” and gives them a separate legal personality just like any other corporation. It is an error to conclude that the corporation has no “real” independent existence simply because one person, being the sole shareholder and director, controls the corporation and is the ultimate beneficiary of any economic value within the corporation. *Kosmopoulos* at p 11 cautioned against recognizing an “indefensible distinction” between single person corporations and other corporations.

[44] In the circumstances of this case, there is no basis for me to lift the corporate veil and consider the actions of Klesh separate and apart from GPOC and Spicelo such that they could form the basis for an equitable application of the doctrine of marshalling. The evidence demonstrates that the parties in this case are all sophisticated commercial actors and that there is no reason to believe that they, including Tamarack, were unable to bargain and reach the agreements they felt were in their interests and commercially reasonable. Tamarack did not bargain to have Spicelo pledge its Greenfield shares as security for the debt it was owed. At all times Tamarack understood that it was contracting with GPOC, not Klesch or Spicelo. It was undoubtedly aware of the implications of subordinating its security to that of the Lenders without obtaining further guarantees. While Tamarack might take issue with some of Klesh’s beliefs and actions, I cannot conclude that they amount to fraud or extraordinary circumstances that should be considered in determining whether the equitable principle of marshalling should apply.

[45] The circumstances of this case do not permit marshalling. While it is clear that Spicelo is GPOC’s guarantor with respect to the debt owed to the Lenders, Spicelo is not the guarantor with respect to the debt owed to Tamarack, and has no obligation to Tamarack. There is nothing which would compel Spicelo to pay the debt owed to Tamarack and there is nothing which would compel GPOC to repay Spicelo if Spicelo paid anything to satisfy Tamarack. In short, the relationship between GPOC and Spicelo that is necessary to support marshalling does not exist here.

[46] Further, because there are insufficient assets within the SISP to satisfy even the debt to Tamarack, directing marshalling in this case would be inequitable to Spicelo as it would not be able to recoup as against GPOC, and would cause Spicelo to become liable for GPOC’s debt to Tamarack – a debt that it has no involvement in. Marshalling is not appropriate in these circumstances.

[47] Given my conclusion that marshalling does not apply in this case, I need not determine whether Spicelo would become subrogated to the Lenders' right of recovery as against GPOC and the assets under the SISP.

IV. Conclusion

[48] The Griffon Entities' application is therefore granted. Specifically, Tamarack has no claim against the assets of Spicelo and the Lenders are not required to exhaust their remedies pursuant to the Spicelo Guarantee prior to realizing on the proceeds from the SISP.

[49] If the parties cannot agree on costs, then they may provide written submissions to me on that issue within 60 days.

Heard on the 12th day of April, 2024.

Dated at the City of Calgary, Alberta this 14th day of May, 2024.

L.K. Harris
J.C.K.B.A.

Appearances:

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for the Applicants

Kyle Kashuba
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For the Monitor (Alvarez & Marsal Canada Inc.)

Karen Fellowes, K.C. and Natasha Doelman
Stikeman Elliott LLP
For the Primary Lenders (Trafigura Canada Limited and Signal Alpha C4 Limited)

Matti Lemmens and Jakub Maslowski
Stikeman Elliott LLP
for the 2nd Lien Creditor (Tamarack Valley Energy)

TAB 5

The Marshalling Plan for Junior Creditors

*Matti Lemmens, Jakub Maslowski and Heather Cattell**

I. INTRODUCTION AND OVERVIEW

Debt marshalling is an equitable doctrine designed to safeguard the interests of subordinate creditors by ensuring a fair distribution of a debtor's assets. While its potential to prevent the unfair disadvantage of junior creditors has been recognized, marshalling has been largely overlooked in Canadian jurisprudence despite its flexibility. The doctrine has been infrequently discussed and applied in Canadian courts, limiting its impact on insolvency proceedings despite its possible benefits for balancing creditor claims.

Recent changes to Canadian insolvency legislation, notably the introduction of the good-faith principle into the *Bankruptcy and Insolvency Act*¹ and the *Companies' Creditors Arrangement Act*,² provide a timely opportunity to reassess the role and application of marshalling. In 2019, the requirement that "interested person[s]" must act in good faith was codified in section 4.2 of the *BIA* and section 18.6 of the *CCAA*.³ The codification of good faith requires that all parties involved in insolvency proceedings act honestly and fairly, which aligns with the equitable objectives of marshalling.

This article explores the current state of marshalling in Canadian law, highlighting its underutilization and the potential benefits of its broader application. Equitable remedies, such as marshalling and equitable subordination, have a place in Canadian insolvency law. However, guidance is needed on how to address these remedies in the insolvency framework, whether through the recent adoption of good-faith principles in the legislation or through direction from the courts. By examining the interplay between good-faith principles and the doctrine of

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¹ *Bankruptcy and Insolvency Act*, RSC 1985, c B-3, s 4.2 [*BIA*].

² *Companies' Creditors Arrangement Act*, RSC 1985, c C-36 [*CCAA*].

³ *BIA*, *supra* note 1, s 4.2; *CCAA*, *supra* note 2, s 18.6.

marshalling, this article illustrates how these doctrines could enhance the fairness and further the remedial objectives of insolvency proceedings in Canada. The evolving legal landscape offers a compelling reason to revisit and potentially expand the use of marshalling, ensuring a more equitable approach to resolving creditor disputes and distributing debtor assets.

II. DEBT MARSHALLING

Debt marshalling aims to protect junior creditors when a senior creditor has access to multiple funds to satisfy its debt. The doctrine suggests that courts should enforce the senior creditor's claim against funds inaccessible to the junior creditor first, minimizing harm to the latter's security interest.

In *Gerrow v Dorais*, the Court of King's Bench of Alberta adopted the doctrine as articulated by Snell's Principles of Equity,⁴ which dictates that

[W]here there are two creditors of the same debtor, and one creditor has a right to resort to two funds for payment of his debt, and the other a right to resort to one fund only, the court will "marshal" or arrange the funds so that both creditors are paid as far as possible.⁵

This approach ensures an equitable distribution of assets and prevents the junior creditor from being unfairly disadvantaged or having their security "needlessly" wiped out.⁶ Marshalling as set forth in *Snell's Principles of Equity* is a doctrine whereby equity assumes that the senior creditor "would want to act honourably, and not capriciously, by leaving as much as possible" for the junior creditor.⁷

Marshalling does not have well-defined or clear limits and is to be applied with "flexibility, adaptability, and utility".⁸ Despite its flexibility, the doctrine has not

⁴ *Gerrow v Dorais*, 2010 ABQB 560 at para 22 [*Gerrow*]; Edmund Henry Turner Snell, Paul Vivian Baker & Peter St John Langan, *Snell's Principles of Equity*, 28th ed (London: Sweet and Maxell, 1982) at 416.

⁵ *Gerrow*, *supra* note 4 at para 22.

⁶ *Ibid.* See also *Condominium Corporation No 082 6970 v 1117398 Alberta Ltd*, 2012 ABQB 233 at para 10.

⁷ *First Investors Corporation Ltd v Veeradon Developments Ltd*, 1988 ABCA 38 at para 17.

⁸ *House v Baird*, 2019 ONSC 1712 at para 37 [*Baird*].

received any significant treatment by the Supreme Court of Canada and only limited treatment among appellate courts across the country.⁹

Several conditions must be satisfied for marshalling to apply, including that there must be:

- (a) two creditors;
- (b) one common debtor;
- (c) two funds of the debtor with the superior creditor having access to both and the inferior creditor to but one;
- (d) no interference with the choice of remedy of the superior creditor; and
- (e) no prejudice to third parties.¹⁰

With respect to the last two conditions, marshalling must not undermine the senior secured creditor's rights or disadvantage third parties.¹¹ This means that while marshalling can help balance the interests of multiple creditors, it cannot be used in a way that affects the first creditor's ability to claim their debt or unfairly affects other parties with claims to the same fund.

There is a recognized exception to the one-common-debtor or single-debtor requirement where there are sureties or guarantors of a primary debtor. In *Brown v Canadian Imperial Bank of Commerce et al*, Southey J of the Ontario Superior Court found that marshalling could apply in cases where two debtors are effectively linked through a surety–principal relationship, meaning the debtor

⁹ *Wolfe et al v Taylor et al*, 2020 MBCA 44 at para 34 [Wolfe].

¹⁰ *Baird*, *supra* note **Erreur ! Signet non défini.** at para 39. See also *Re Griffon Partners Operation Corporation*, 2024 ABKB 277 at para 21 [Griffon].

¹¹ *Gerrow*, *supra* note 4 at para 23; *Bear Creek Contracting Ltd v Canadian Western Bank*, 2024 NLSC 92 at para 61, online (pdf): [mcusercontent<https://mcusercontent.com/a3e2039936cbf8a31bda45ab3/files/06698157-1e22-ed9a-fdab-4c640b305b80/202201G0266_Bear_Creek_Contracting_Ltd._v._Canadian_Western_Bank_June_20_2024_SIGNED_FINAL_AM_1_4863_7504_6860_1_1_.pdf?utm_source=insolvencyinsider.ca&utm_medium=referral&utm_campaign=lifting-the-stay-to-pierce-the-corporate-veil>](https://mcusercontent.com/a3e2039936cbf8a31bda45ab3/files/06698157-1e22-ed9a-fdab-4c640b305b80/202201G0266_Bear_Creek_Contracting_Ltd._v._Canadian_Western_Bank_June_20_2024_SIGNED_FINAL_AM_1_4863_7504_6860_1_1_.pdf?utm_source=insolvencyinsider.ca&utm_medium=referral&utm_campaign=lifting-the-stay-to-pierce-the-corporate-veil) [Bear Creek].

facing claims from two creditors is also a creditor of the second debtor.¹² The Court cited the following passage from *Halsbury's Laws of England*:

Generally, three conditions must be satisfied in order that the doctrine of marshalling may be applied as regards claims by creditors. First, the claims must be against a single debtor. If one creditor has a claim against C and D, and another creditor has a claim against D only, the latter creditor cannot require the former to resort to C unless the liability is such that D could throw the primary liability on C, for example where C and D are principal and surety.¹³

Another exception to the single-common-debtor rule involves “piercing the corporate veil,” where the “controlling mind” of a corporation is held accountable for its liabilities.¹⁴ However, as discussed below, this concept lacks consistent application to a corporation and its directors, who will be treated as “separate entities” unless this would yield a result “too flagrantly opposed to justice”.¹⁵

These exceptions have been applied only in limited circumstances. However, recent amendments to the *BIA* and the *CCAA*, which include the duty of good faith, provide a stronger foundation for encouraging a more extensive application of this principle.

III. MARSHALLING IS BEING APPLIED INFLEXIBLY

Canadian courts have recently reconsidered the exception to the single-common-debtor rule in the context of sureties and principals but have mostly felt constrained by prior precedents that apply marshalling inflexibly.

In *Wolfe et al v Taylor et al*, the Manitoba Court of Appeal declined to apply marshalling. Wolfe and Taylor jointly owned two companies, TBF and EPG.¹⁶

¹² *Brown v Canadian Imperial Bank of Commerce et al* (1985), 50 OR (2d) 420, 1985 CanLII 2116 (HC) [*Brown*]. See also *Griffon*, *supra* note 10 at para 30.

¹³ *Brown*, *supra* note 12 at para 4, citing *Halsbury's Laws of England*, vol 16, *Equitable Jurisdiction* at 962–963, para 1427 “Application of Doctrine of Marshalling” 4th ed (London: Butterworths, 1980).

¹⁴ *Griffon*, *supra* note 10 at para 42.

¹⁵ *Ibid.* See also *Kosmopoulos v Constitution Insurance Co*, [1987] 1 SCR 2 at para 12, 1987 CanLII 75 (SCC).

¹⁶ *Wolfe*, *supra* note 9 at para 2.

Disputes led Wolfe to seek their liquidation. During these proceedings, TBF owed debts to Wolfe's company, RLW.¹⁷ The Bank of Montréal ("BMO") was a primary creditor with priority over the assets of RLW.¹⁸ Assets from TBF and EPG were liquidated, fully covering the debt owed to BMO, but leaving insufficient funds to cover the debts owed to RLW.¹⁹ RLW sought to apply marshalling to prioritize repayment to BMO from EPG's sale proceeds, leaving amounts from TBF to repay RLW.²⁰ There were two debtors, which typically precludes the application of marshalling. Citing *Brown*, the Court acknowledged the surety–principal exception to the single-common-debtor rule.²¹ In *Brown*, marshalling applied when a junior creditor of the surety invoked it to have a senior creditor's claim paid by the principal debtor.²² The Court found the exception inappropriate, as there was no obligation for the surety to indemnify the principal debtor.²³ The Court also rejected piercing the corporate veil, finding insufficient evidence that EPG and TBF were interconnected enough to be treated as a single entity.²⁴

In *Re Griffon Partners Operation Corporation*,²⁵ the Court of King's Bench of Alberta also rejected marshalling. Tamarack Valley Energy Ltd ("TVE") sold assets to Griffon Partners Operation Corporation ("GPOC"), which financed the transaction through a loan from Signal Alpha C4 Limited and Trafigura Canada Ltd (the "lenders").²⁶ The lenders had senior secured interests in GPOC's assets.²⁷ Spicelo Limited ("Spicelo"), a related entity, provided a limited-recourse guarantee and pledged shares as collateral.²⁸ Griffon Partners Operation Corporation issued a subordinated secured promissory note to TVE, but

¹⁷ *Ibid* at paras 4–6.

¹⁸ *Ibid* at paras 9–15.

¹⁹ *Ibid* at para 16.

²⁰ *Ibid* at para 17.

²¹ *Ibid* at para 35.

²² *Brown*, *supra* note 12; *Wolfe*, *supra* note 9 at para 60.

²³ *Wolfe*, *supra* note 9 at para 61.

²⁴ *Ibid* at para 53.

²⁵ *Griffon*, *supra* note 10.

²⁶ *Ibid* at paras 7–8.

²⁷ *Ibid* at para 8.

²⁸ *Ibid* at para 9.

defaulted on both the loan and the note, leading to insolvency.²⁹ The Court considered whether marshalling could require the lenders to first enforce their security against Spicelo's shares, potentially allowing TVE to recover from the promissory note. TVE argued for marshalling, despite GPOC and Spicelo being separate debtors, since, in this case, the primary liability to the lenders rested with both Spicelo (the surety) and GPOC (the primary debtor).³⁰ TVE also advanced arguments that Spicelo and GPOC were closely related and engaged in inequitable conduct, thereby allowing for the corporate veil to be pierced and for the doctrine of marshalling to apply.³¹ The Court found that the director's involvement in multiple entities did not, in itself, justify marshalling.³² Further, there was no substantial evidence of fraudulent behaviour or improper conduct by Spicelo.³³ The Court did not address the effect of the waiver of subrogation on marshalling.

TVE successfully applied for leave to appeal this decision to the Alberta Court of Appeal, with the Court finding that the proposed appeal raised "serious and arguable grounds that are of real and significant interest to the parties".³⁴ The Court held that although TVE was advancing a seemingly novel argument, equitable doctrines and remedies are flexible and that:

Just as courts have made exceptions to the "single debtor rule" in the cases set out above, they could reasonably find such an exception to be equitable on other facts or otherwise relax the criteria for marshalling where justified by the equities in a particular case. The circumstances in this case are such that it is reasonable for the applicant to argue that the equities weigh in its favour and that applying

²⁹ *Ibid* at para 12.

³⁰ *Ibid* at paras 22, 32.

³¹ *Ibid* at paras 35–36.

³² *Ibid* at para 44.

³³ *Ibid*.

³⁴ *Re Griffon Partners Operation Corporation*, 2024 ABCA 279 at para 15, citing *BMO Nesbitt Burns Inc v Bellatrix Exploration Ltd*, 2020 ABCA 264 at para 7 and *Re Liberty Oil & Gas Ltd*, 2003 ABCA 158 at para 15.

marshalling would be consistent with the principles that underpin the doctrine.³⁵

Grosse JA held that TVE's appeal had significance to the practice and development of the equitable doctrine of marshalling, as the appellate authority on the general principles of the doctrine were "dated".³⁶ It was further held that:

Regardless of whether the applicant is ultimately successful, a decision by this Court would contribute to the body of law and it will provide some certainty for parties in similar circumstances as to whether marshalling is potentially available.³⁷

In *Bear Creek Contracting Ltd v Canadian Western Bank*, the Supreme Court of Newfoundland and Labrador recently permitted marshalling arguments to proceed to trial, but with no guarantee that they will be accepted.³⁸ Bear Creek Contracting Inc ("Bear Creek") sold Lakelse Air Ltd ("Lakelse") to Universal Helicopter Group ("Universal"), the purchase of which was financed with a \$10 million loan from Canadian Western Bank ("CWB").³⁹ Bear Creek retained a \$2.5 million promissory note from Lakelse, which Universal did not guarantee.⁴⁰ CWB's security was prioritized over Bear Creek's⁴¹ and CWB later advanced an additional \$3 million to Lakelse, guaranteed by Universal, which Bear Creek was unaware of.⁴² Both Universal and Lakelse went bankrupt, and CWB recovered most of its loan but faced a \$790,000 shortfall.⁴³ Canadian Western Bank then sought to recover the shortfall from Universal's assets; however, Universal's money was used to pay all secured creditors of Universal, including the deficiency on Lakelse's loan.⁴⁴ Bear Creek sought to pierce the corporate veil between Lakelse and Universal, aiming to recover from Universal through

³⁵ *Ibid* at para 10.

³⁶ *Ibid* at para 13.

³⁷ *Ibid*.

³⁸ *Bear Creek*, *supra* note 11.

³⁹ *Ibid* at para 3.

⁴⁰ *Ibid* at para 4.

⁴¹ *Ibid* at para 5.

⁴² *Ibid* at paras 7–8.

⁴³ *Ibid* at paras 9–10, 12.

⁴⁴ *Ibid*.

marshalling.⁴⁵ Prior to seeking to recover, Bear Creek was first required to lift a bankruptcy stay of proceedings for Universal.⁴⁶ The Court denied the request to pierce the veil due to insufficient evidence showing any wrongdoing by Universal or Lakelse,⁴⁷ but allowed Bear Creek to pursue marshalling and subrogation. The Court ruled that marshalling could proceed, as equity may allow the inferior creditor to stand as the superior creditor in relation to the property against which the inferior creditor otherwise has no recourse.⁴⁸ The stay was lifted, enabling Bear Creek to seek these equitable remedies.⁴⁹ It is now open for Bear Creek to pursue these remedies at trial.

From the recent case law, it appears that courts may be open to applying the doctrine of marshalling flexibly, although a clear, definitive statement at the appellate level on the application of this doctrine would provide much-needed guidance in modern times.

IV. THE DUTY OF GOOD FAITH AND MARSHALLING

As outlined above, recent decisions regarding the exception to the single-common-debtor rule and the application of marshalling have focused, in part, on the conduct of the principal and the surety. Of note is that none of these decisions consider the relatively recent amendments to the duty of good faith in the *BIA* and *CCAA*, nor the codified obligation of good faith in the *Civil Code of Québec*⁵⁰ that has existed for some time, and which could potentially expand the applicability of the doctrine of marshalling, the origins of which demand flexibility.

⁴⁵ *Ibid* at para 15.

⁴⁶ *Ibid* at para 1.

⁴⁷ *Ibid* at para 45.

⁴⁸ *Ibid* at para 55.

⁴⁹ *Ibid* at para 67.

⁵⁰ *Civil Code of Québec*, CQLR c CCQ-1991, arts 1375, 1434. See also *Ponce v Société d'investissements Rhéaume Itée*, 2023 SCC 25 at para 70 [*Ponce*] (wherein the Supreme Court considered the codification of the principles of good faith in the *Civil Code of Québec* and affirmed that the obligation of good faith must be upheld even if contradicted by the contract's terms).

In 2019, the requirement that “interested person[s]” must act in good faith was codified in section 4.2 of the *BIA* and section 18.6 of the *CCAA*.⁵¹

There has not yet been extensive judicial consideration of the application of these new legislative provisions. In *CWB Maxium Financial Inc v 2026998 Alberta Ltd*,⁵² the Court of King’s Bench of Alberta acknowledged the lack of case law specifically addressing section 4.2 of the *BIA*.⁵³ In light of this void in the law, the Court provided some guidance on its application. The Court observed that the common law interpretation of good faith established in *Bhasin v Hrynew* and further interpreted in *CM Callow Inc v Zollinger*⁵⁴ is relevant to the application of section 4.2 of the *BIA*, particularly when it involves a creditor initiating insolvency proceedings.⁵⁵ However, the Court also emphasized that any application of the common law interpretation of good faith must align with and advance the policy objectives underlying the *BIA*.⁵⁶

In *Bhasin*, the Supreme Court of Canada described the duty of good faith as requiring parties to act honestly and reasonably in the performance of their contractual obligations.⁵⁷ This duty mandates that parties not undermine each other’s interests in bad faith, but it does not require one party to actively serve the interests of the other.⁵⁸

In *Callow*, the Supreme Court of Canada expanded the duty of good faith to include the exercise of discretionary decisions, even when the decision-maker has an absolute contractual right to make those decisions.⁵⁹ The Court also

⁵¹ *BIA*, *supra* note 1, s 4.2; *CCAA*, *supra* note 2, s 18.6.

⁵² *CWB Maxium Financial Inc v 2026998 Alberta Ltd*, 2021 ABQB 137 [CWB].

⁵³ *Ibid* at para 40, cited with approval in *Saskin v City of Toronto*, 2022 ONSC 7378 at para 376; *Malhotra v City of Brampton*, 2023 ONSC 3204 at para 202; *Re Bannikova*, 2023 ONSC 5131 at para 216; *Re Sergio Grillone*, 2023 ONSC 5710 at para 47.

⁵⁴ *Bhasin v Hrynew*, 2014 SCC 71 [Bhasin]; *CM Callow Inc v Zollinger*, 2020 SCC 45 [Callow].

⁵⁵ *CWB*, *supra* note 52 at para 58.

⁵⁶ *Ibid*.

⁵⁷ *Bhasin*, *supra* note 54 at para 33.

⁵⁸ *Ibid* at para 65.

⁵⁹ *Callow*, *supra* note 54 at paras 136–38.

clarified that the duty of good faith extends beyond outright lies to include any form of dishonesty or misleading conduct by a contracting party.⁶⁰

In *Ponce v Société d'investissements Rhéaume Itée*, the Supreme Court of Canada addressed the codification of good faith in the *Civil Code of Québec*. The Court asserted that this inclusion embedded the obligation of good faith to the extent that it is required even if it is contradicted by the terms of the contract.⁶¹

In the insolvency context, in *CWB*, the Court of King's Bench of Alberta emphasized that the lender–debtor relationship is contractual and that remedies such as receiverships are at the lender's discretion.⁶² Therefore, good faith must be exercised in *BIA* proceedings; this encompasses not only conduct during such proceedings, but also the conduct that precipitated the proceedings.⁶³ The Court made several key conclusions regarding section 4.2 of the *BIA*:

- All interested persons involved in *BIA* proceedings must act in good faith. This includes the conduct of a secured creditor seeking a receivership order, if it is factually and temporally connected to the proceedings;
- Good faith in insolvency requires that interested parties not initiate or conduct proceedings for ulterior or improper purposes;
- The common law principles of good faith in contractual performance, as established in cases such as *Bhasin* and *Callow*, can inform the interpretation of good faith under section 4.2 of the *BIA*;
- The duty of good faith does not impose a requirement for loyalty or disclosure, nor does it necessitate the subordination of one's own interests to those of another. It falls short of creating a fiduciary duty;
- Whether dishonesty has occurred is fact specific and can include lies, half-truths, omissions and even silence, depending on the circumstances;

⁶⁰ *Ibid* at para 91.

⁶¹ *Ponce*, *supra* note 50.

⁶² *CWB*, *supra* note 52 at para 56.

⁶³ *Ibid*.

- The conduct of a party alleged to have breached the good-faith requirement should be assessed by considering the intent and policy objectives of the *BIA*.⁶⁴

The content and scope of the good-faith requirement may vary depending on the roles of different *BIA* actors and the specific facts of each case;⁶⁵ nevertheless, these conclusions provide valuable insights for assessing how section 4.2 of the *BIA* may be applied in supporting claims of marshalling.

Other cases provide similar commentary on section 4.2 of the *BIA*. In *Re Chester Basin Seafood Group Inc*, the Nova Scotia Supreme Court addressed section 4.2 of the *BIA*, aligning its interpretation of good faith with the Supreme Court's view in *Bhasin*.⁶⁶ The Court emphasized that good faith under the *BIA* represents a positive obligation requiring “honest performance” and “appropriate regard” for the other party, rather than merely the absence of bad faith.⁶⁷

In *Re Bellatrix Exploration Ltd*, the Court of King's Bench of Alberta explored bad-faith conduct within insolvency proceedings.⁶⁸ The Court cited Janis Sarra's article “La bonne foi est une considération de base – Requiring Nothing Less than Good Faith in Insolvency Law Proceedings”, which defined bad faith as:

[C]onduct where a debtor, creditor or their professionals fail to meet the requirements to act candidly, honestly, forthrightly and reasonably in their dealings with one another and the court; where parties act capriciously and arbitrarily; or where they lie or otherwise knowingly mislead each other about matters relating to the insolvency proceedings.⁶⁹

⁶⁴ *Ibid* at para 59.

⁶⁵ *Ibid* at para 60.

⁶⁶ *Re Chester Basin Seafood Group Inc*, 2023 NSSC 388.

⁶⁷ *Ibid* at para 19. See also *Re Atlantic Sea Cucumber Limited*, 2023 NSSC 238 at para 25.

⁶⁸ *Re Bellatrix Exploration Ltd*, 2020 ABQB 809.

⁶⁹ *Ibid* at para 105, citing Janis Sarra, “La bonne foi est une considération de base – Requiring Nothing Less than Good Faith in Insolvency Law Proceedings” in Janis Sarra & Barbara Romaine, eds, *Annual Review of Insolvency Law 2014* (Toronto: Thomson Reuters, 2015).

Although section 18.6 of the CCAA has not received as extensive consideration as section 4.2 of the BIA, it appears that courts will apply similar principles regarding good faith in CCAA proceedings.⁷⁰

The inclusion of good-faith principles into insolvency legislation supports the equitable goals of marshalling. As outlined above, good faith under the BIA and CCAA represents a positive obligation on creditors requiring honest performance and appropriate regard for the other party. To align with this obligation, parties should not be allowed to needlessly “wipe out” the interests of junior creditors. Marshalling serves to protect these interests and could do so as part of the obligation of good faith.

V. THE ROLE OF EQUITABLE SUBORDINATION

The potential expansion of the doctrine of equitable subordination following the inclusion of good faith in the BIA and the CCAA was recently discussed in detail by Pavle Masic in the *Annual Review of Insolvency Law*;⁷¹ however, it is useful to note its potential role in supporting claims for marshalling.

Originating in the United States, the doctrine of equitable subordination has seen limited and mixed application in Canada, without definitive recent guidance from the Supreme Court or superior provincial courts.⁷² In the recent decision in *Re Alderbridge Way GP Ltd*,⁷³ a proceeding under the CCAA, the British Columbia Supreme Court expressly declined opining on whether the doctrine of equitable

⁷⁰ *US Steel Canada Inc et al v The United Steel Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union et al*, 2022 ONSC 6993 at para 46.

⁷¹ Pavle Masic, “Has the Statutory Duty of Good Faith Opened a Window to Recognition of Equitable Subordination in Canadian Law” in Jill Corraini & the Honourable D Blair Nixon, eds, *Annual Review of Insolvency Law*, 19th ed, 2021 CanLII Docs 13548.

⁷² See eg, *Canadian Deposit Insurance Corp v Canadian Commercial Bank*, [1992] 3 SCR 558, 1992 CanLII 49 (SCC) (wherein Iacobucci J left open the possibility of the application of the doctrine of equitable subordination); *Sun Indalex Finance, LLC v United Steelworkers*, 2013 SCC 6 at para 77 (wherein the Supreme Court did not outright dismiss the application of the doctrine of equitable subordination, but rather stated that there was no need to endorse it based on the facts before the Court).

⁷³ *Re Alderbridge Way GP Ltd*, 2024 BCSC 1433.

subordination is part of Canadian law.⁷⁴ Nevertheless, creditors, debtors, sureties, guarantors and practitioners would benefit from a comprehensive, authoritative decision on the applicability of this doctrine.

With that, and in light of the amendments to the *BIA* and *CCAA* introducing the duty of good faith, it merits reconsidering the reordering of secured parties' interests that could support a broader application of marshalling where the surety exception to the single-common-debtor rule applies.

Equitable subordination allows courts to subordinate a creditor's claim due to the creditor's misconduct, especially if that misconduct harms other creditors or gives the creditor an unfair advantage.⁷⁵ The doctrine is subject to a three-part test:

- (i) The claimant must have engaged in some type of inequitable conduct.
- (ii) The misconduct must have resulted in injury to the creditors ... or conferred an unfair advantage on the claimant.
- (iii) Equitable subordination of the claim must not be inconsistent with the provisions of the Bankruptcy Act.⁷⁶

With marshalling, in the event that the surety exception to the single-common-debtor rule is applied where the senior secured creditor is directed to enforce against a surety prior to realizing upon any assets held by the principal debtor, the surety would generally be subrogated to the senior secured creditor's priority position. This would, in turn, result in the junior creditor remaining in its subordinate position behind the surety with no better prospect of recovery than if the doctrine of marshalling had not been applied. While in this scenario any benefit to creditors derived from applying marshalling appears illusory, the incorporation of the doctrine of equitable subordination under the good-faith provisions would provide the court with the ability to reorder the priority of creditors to ensure a just and fair result and to ensure that sureties or principals

⁷⁴ *Ibid* at para 328.

⁷⁵ *Taylor v Standard Gas & Electric Co*, 306 US 307 (1939); *Pepper v Litton*, 308 US 295 (1939).

⁷⁶ *In re Mobile Steel Co*, 563 F (2d) 692 at 700 (5th Cir 1977) [footnotes omitted].

do not benefit from any fraud or misconduct to the detriment of subordinate secured creditors.

VI. POTENTIAL EXPANDED APPLICATION OF THE DOCTRINE OF MARSHALLING BASED ON GOOD FAITH

Within the context of the exception to the single-common-debtor rule where sureties and principals are involved, there is room for a more expansive application of the doctrine of marshalling. That expansive application aligns with the fundamental principles of marshalling—that it must be applied with “flexibility, adaptability, and utility” with a view to ensuring that a junior or subordinate creditor’s security is not needlessly wiped away.⁷⁷

Where the surety exception to the single-common-debtor rule is engaged, the doctrine of marshalling could be applied more broadly to ensure that all creditors maximize their recovery. Specifically, the narrow interpretation of this exception as stated in *Wolfe* and *Brown* suggests that it will only apply in circumstances where the senior creditor and junior creditor are doubly secured against the surety and not the principal. The authors note that no Canadian courts have held that it cannot be applied in the reverse scenario.

The surety exception should be revisited by courts in Canada, especially because many, if not all, modern guarantees include language whereby the surety agrees to indemnify a creditor in full and to become primarily liable for debts owing by the principal. In this situation, it cannot be said that it would be unfair to marshal a senior creditor to enforce against a guarantor or surety in the first instance when that is what was expressly contemplated in the underlying guarantee. This would, in turn, give subordinate creditors the opportunity to potentially enforce against the principal, ensuring maximum recovery for all secured creditors.

⁷⁷ *Baird*, *supra* note **Erreur ! Signet non défini.** at para 37.

When considering whether a surety has an obligation to indemnify the singly secured subordinate creditor, it is important to note that, under the doctrine of marshalling, the surety would be paying the senior secured creditor and not the junior creditor. The junior creditor would only have recourse against the assets of the principal over which it holds a secured interest. The surety would only be required to indemnify the senior creditor and not the subordinate creditor with which it does not have any contractual relationship.

With respect to the exception to the single-common-debtor rule and the subrogation rights of a surety, courts should have regard to the good-faith requirements under the *CCAA* and *BIA*. These provisions have incorporated concepts from the contractual duty of good faith as set out in *Bhasin* and *Callow*, including requiring parties to act honestly and reasonably in the performance of their contractual obligations, allowing consideration of any form of dishonesty or misleading conduct by a contracting party and requiring that interested parties not initiate or conduct insolvency proceedings for ulterior or improper purposes. These requirements would ensure that parties attempting to resist the application of marshalling have acted in good faith and are coming to court with “clean hands.” Applying this doctrine would ensure that just results are achieved where marshalling is being considered.

Further, a reordering of priorities should be considered under the doctrine of equitable subordination where a surety has a right of subrogation, though this doctrine would benefit from guidance from the courts given the substantive legislative and common law developments in the past several years and the general dearth of substantive case law on the topic.

VII. CONCLUSION

Debt marshalling remains underutilized in Canadian insolvency law despite its potential to foster fairness among multiple creditors. The limited application of marshalling by Canadian courts, coupled with a lack of significant Supreme Court of Canada guidance, has restrained its broader use. However, the recent

amendments to the *BIA* and the *CCAA* that incorporate principles of good faith present an opportunity to reassess and potentially expand the application of marshalling.

The inclusion of good-faith principles into Canadian insolvency legislation aligns with the equitable goals of marshalling, emphasizing fair conduct and addressing inequitable behaviour among creditors. This shift opens the door for a more robust application of equitable remedies, such as marshalling and equitable subordination, particularly in cases involving sureties and principal debtors where a surety may also have a right of subrogation against the principal. By integrating these doctrines, Canadian courts could enhance the equitable distribution of assets and ensure more balanced outcomes in insolvency proceedings.

The evolving legal landscape, including recent case law and legislative changes, suggests a growing receptivity to these equitable doctrines. Although remedies such as marshalling and equitable subordination can play an important role in insolvency law, there is a need for clearer guidance on how these doctrines should be addressed, either through legislation or case law. As Canadian jurisprudence continues to develop, a more comprehensive application of marshalling could significantly improve the fairness and effectiveness of insolvency resolutions. Such advancements would benefit all parties involved—including creditors, debtors and practitioners—by ensuring that equitable principles are more fully realized in insolvency scenarios.

TAB 6

IN THE COURT OF APPEAL OF MANITOBA

Coram: Chief Justice Richard J. Chartier
Mr. Justice Marc M. Monnin
Madam Justice Karen I. Simonsen

B E T W E E N :

	)	<i>F. J. Trippier and</i>
	)	<i>I. Vakurova</i>
	)	<i>for the Appellants</i>
	)	
<i>LINCOLN WOLFE and 5606269</i>	)	<i>R. A. McFadyen</i>
<i>MANITOBA LTD.</i>	)	<i>for the Respondents</i>
	)	<i>Lincoln Wolfe and</i>
<i>(Applicants) Respondents</i>	)	<i>5606269 Manitoba Ltd.</i>
	)	
<i>- and -</i>	)	<i>J. R. N. Boudreau</i>
	)	<i>for the Interveners</i>
	)	
<i>DUANNE TAYLOR and 5608067</i>	)	<i>J. M. Lee, Q.C. and</i>
<i>MANITOBA LTD.</i>	)	<i>J. J. Burnell</i>
	)	<i>for Deloitte Restructuring</i>
<i>(Respondents) Appellants</i>	)	<i>Inc., the Court-Appointed</i>
	)	<i>Liquidator for Taylor</i>
<i>- and -</i>	)	<i>Bros. Farm Ltd. and</i>
	)	<i>Edwin</i>
<i>TAYLOR BROS. FARM LTD. and EDWIN</i>	)	<i>Potato Growers Ltd.</i>
<i>POTATO GROWERS LTD.</i>	)	
	)	<i>T. W. Turner</i>
<i>(Respondents)</i>	)	<i>for Pitblado LLP, a</i>
	)	<i>judgment creditor of</i>
<i>- and -</i>	)	<i>Taylor Bros. Farm Ltd.</i>
	)	<i>and Edwin Potato</i>
<i>GERALD WIEBE and MARTHA WIEBE</i>	)	<i>Growers Ltd.</i>
	)	
<i>Interveners</i>	)	<i>Appeals heard:</i>
	)	<i>August 27, 2019</i>
	)	

) *Judgment delivered:*
) *April 27, 2020*

MONNIN and SIMONSEN JJA

[1] These three appeals arise from liquidation proceedings under the provisions of *The Corporations Act*, CCSM c C225 (the *Act*), with respect to the assets of two corporations, namely, Taylor Bros. Farm Ltd. (TBF) and Edwin Potato Growers Ltd. (EPG). By a liquidation order dated April 28, 2017, the liquidation judge appointed Deloitte Restructuring Inc. (the liquidator) the liquidator of the assets and property of TBF and EPG. Those proceedings followed their course and culminated in the granting of the three orders under appeal in these proceedings:

- a) an order pronounced August 31, 2018, whereby the liquidation judge ordered that certain funds in the hands of the liquidator be reallocated between TBF and EPG, allowing for the claim of a secured creditor, R. L. Wolfe Ltd. (RLW), to be paid in full, and the claims of a judgment creditor, the Pitblado LLP law firm (Pitblado), to be paid to a greater extent (the Marshalling Order);
- b) another order pronounced August 31, 2018, whereby the liquidation judge approved a distribution schedule proposed by the liquidator (the Distribution Order); and
- c) an order pronounced September 25, 2018, whereby the liquidation judge granted priority to the claims of Pitblado, to the extent not otherwise satisfied by the Distribution Order, over any other unsecured creditor of TBF and EPG

notwithstanding a bankruptcy of either (the Supplemental Order).

Background

History and Corporate Structure

[2] In early 2008, Lincoln Wolfe (Wolfe) and Duanne Taylor (Taylor) began farming together using two corporate entities, TBF and EPG. The shares of those two companies were held equally by Wolfe and Taylor through their own personal holding companies, 5606269 Manitoba Ltd. (269) for Wolfe and 5608067 Manitoba Ltd. (067) for Taylor. Those two individuals entered into a unanimous shareholders agreement (USA) to define their relationships with each other and with TBF.

[3] TBF and EPG essentially carried on as one business operation. While EPG owned much of the land, all of the active farming operations were carried on through TBF. All of the obligations of TBF and EPG to the Bank of Montreal (BMO) were secured by a first charge over all of the assets of TBF and EPG.

[4] Disputes with respect to the farming operation arose between Taylor and Wolfe. Wolfe moved for the appointment of a liquidator and dissolution of the companies under the *Act*. The application was stayed by a motion judge to allow the dispute to proceed to arbitration. The arbitration proceedings resulted in an award on April 20, 2016, ordering the liquidation of all of the assets of TBF and EPG in accordance with section 207 of the *Act*. However, prior to the award being implemented, the parties agreed to a postponement of the liquidation until a series of interim steps were

completed, including the determination of issues with respect to the amounts owing to TBF and EPG by either of the shareholders or companies controlled by them.

[5] In a subsequent award made on August 24, 2016, the arbitrator dealt with the amounts owing between the respective corporations and individuals. Those amounts included debts owing by TBF to Farm Credit Canada (FCC) and the Bank of Nova Scotia (BNS) on account of input costs for previous farming years which Wolfe, through RLW (a corporation that he owned and controlled), had paid and received assignments of the securities held by those creditors. The allegation before the arbitrator was that Wolfe should not be entitled to the benefit of the securities he held on those loans and the benefits of the transfer since he had obtained them at a discounted amount, nor should TBF be liable for the increased interest rates charged as a result of the default. Wolfe's position was that he had advanced those funds to the creditors in order to ensure the continued operation of the farming operation.

[6] The arbitrator accepted Wolfe's version of events and confirmed that TBF owed RLW \$1,823,842 for the loans it acquired from secured creditors, including the FCC and BNS loans.

[7] Between May and December 2016, Wolfe and Taylor agreed to liquidate the majority of the equipment owned by TBF and EPG through a third-party auctioneer. By December 2016, the primary assets of TBF and EPG that remained were approximately 2,900 acres of land and physical building structures located upon those lands.

[8] Wolfe and Taylor were unable to reach an agreement on how to deal with those remaining assets and Wolfe proceeded before the Court of Queen's Bench to enforce the April 20, 2016 arbitration decision to have a liquidator appointed. The liquidation judge granted that request on April 28, 2017 with the liquidation order being filed on June 5, 2017. A request was made to stay that liquidation order pending resolution of various matters which remained subject to the arbitration proceedings. The stay request was dismissed and appealed to this Court. By decision dated August 11, 2017, the application to stay the liquidation order was dismissed by a chambers judge in our Court (see 2017 MBCA 74).

The Liquidation Proceedings

[9] In its first report of October 31, 2017, the liquidator outlined the steps it had taken to secure the assets of the corporations and deal with their indebtedness.

[10] The liquidator confirmed that BMO was the principal lender to the companies and held various first-ranking security positions against both companies and their assets. It was owed approximately \$5,200,000. As well, the liquidator confirmed that, during 2015, RLW purchased indebtedness owed by TBF to BNS, FCC and the Royal Bank of Canada (RBC).

[11] Given a lack of cooperation between the parties on how to proceed, the liquidator proposed and received approval from the Court of a liquidation plan which included a sale process with respect to the assets of the companies. As well, it proposed and received approval for a claims process.

[12] By the time of the second report dated March 26, 2018, the liquidator had updated the security claims and they were as follows:

- BMO \$5,182,300
- RLW \$2,407,367
- Gerald and Martha Wiebe (the Wiebes)..... \$788,711
- a small amount to another party

Unsecured debt included amounts owed pursuant to the arbitration award to Taylor and charges to the shareholders' accounts of both corporations reflecting the amounts in the award. However, by that time, the liquidator had formed the view that the proceeds from the sale process could well be insufficient to pay out all the companies' secured and unsecured creditors' claims in full.

[13] In a supplement to the second report, the liquidator confirmed the validity and enforceability of the security held by BMO against the assets of both TBF and EPG, the security held by the Wiebes against the assets of EPG and the security held by RLW against the assets of TBF. It is common ground that the BNS and RBC portions of TBF's debt to RLW were guaranteed by EPG but the FCC portion was not. The liquidator also confirmed the amounts owing to BMO and to RLW but was not able to do so with respect to the Wiebes. Given that the Wiebes' claim ranked in priority to the RLW claim in respect of the lands owned by EPG, the liquidator was not in a position to recommend a distribution to either RLW or the Wiebes. The liquidator recommended a distribution to BMO in the

amount of \$5,518,039 in satisfaction of both companies' obligations. This distribution was premised on the successful sale of the lands and equipment.

[14] On April 13, 2018, the liquidation judge approved the sale and a vesting order. The sale and distribution of proceeds were made subject to certain conditions, namely:

- a) With respect to priorities, the net proceeds from the sale would stand in the place and stead of the assets and any claims and encumbrances would attach to the net proceeds with the same priority as they had immediately prior to the sale.
- b) The distribution could be made to BMO without prejudice to the rights of the parties as to how the distribution amounts would be allocated as between the assets of TBF and EPG and the costs of the liquidation proceedings would be allocated as between the assets of TBF and EPG; the allocations would be deferred to be made by the Court at a later date.

[15] The sale of the assets of TBF and EPG realised the amount of \$9,357,455. The receipts were allocated by the liquidator as follows:

- TBF \$4,238,475
- EPG..... \$5,118,980

[16] On completion of the sale of the lands, the BMO debt was paid in full. BMO's own internal allocation of the debt between TBF and EPG, based on a payment statement summary provided by BMO, was as follows:

- TBF \$3,838,986
- EPG \$1,679,053

This was reflected in the liquidator’s proposed distribution schedule as at May 30, 2018. The result was that considerable funds were left remaining in EPG but limited funds remained in TBF.

Marshalling Application

[17] RLW filed a motion in June 2018, seeking the application of “the equitable doctrine of marshalling” as between the secured creditors of TBF and EPG to have the debt owing to BMO by those two companies paid, or deemed to have been paid, from the proceeds realised from the sale of EPG assets to a greater extent than shown in the proposed distribution schedule of the liquidator.

[18] On the hearing of the marshalling application, RLW had agreed that the Wiebes would have a holdback from EPG funds pending a final determination of the quantum of their claim. The reallocation that RLW proposed would therefore not prejudice them. As well, Pitblado, a judgment creditor by virtue of the registration of two judgments for legal services, was also present seeking to have its priority against the TBF and EPG lands maintained.

[19] In a brief endorsement, the liquidation judge, acknowledging that he was unable to determine exactly the extent of RLW’s secured interest—in particular, as assigned from FCC—was of the opinion that RLW had access

to both funds (presumably the proceeds from the sale of the TBF and EPG lands).

[20] As such, the liquidation judge was incorrectly of the view that RLW was a secured creditor in respect of both corporate debtors and it was irrelevant whether the doctrine of marshalling was applicable. In his conclusion, he held that RLW was entitled to the reallocation sought to the extent that its secured interest in both funds permitted.

[21] The initial order prepared by the successful party, RLW, and provided to the judge for signing, made a reference to the doctrine of marshalling. In a second endorsement dated July 27, 2018, the liquidation judge stipulated that the order should not refer to that doctrine. In the same supplemental endorsement, the liquidation judge recognised that he had not dealt with the claim advanced by Pitblado that it had a priority over other unsecured creditors. That issue was deferred to a later hearing.

[22] Subsequently, in a court appearance on August 31, 2018, scheduled to deal with the liquidator's request for approval of a distribution schedule, the liquidation judge confirmed that it was his intention to allow the reallocation of funds on an equitable basis similar to a marshalling principle.

[23] In the same proceeding, the liquidation judge was asked to grant Pitblado a priority over unsecured creditors as a result of it being a judgment creditor and reallocate funds from EPG to TBF to satisfy its judgment against TBF. Again, this was opposed by Taylor on the grounds that marshalling was not available. The liquidation judge disagreed and allowed Pitblado to rank in priority above the unsecured creditors with respect to the

proceeds from the sale of the lands behind only RLW and the Wiebes and also allowed reallocation in favour of Pitblado.

[24] At that appearance of August 31, 2018, the liquidation judge was also asked to approve the distribution to the Wiebes of their claim on EPG assets. This was opposed by Taylor, arguing that it had not been properly quantified before being accepted by the liquidator. The liquidation judge, finding that the liquidator had followed the claims process in dealing with the matter, confirmed the priority and the amount.

[25] The liquidator accepted, as part of the EPG claims process, a claim by TBF in the amount of \$916,336 as against EPG. The basis for that claim were general ledger details from the books and records of TBF and the December 31, 2015 financial statement for EPG which indicated that EPG was indebted to TBF in that amount.

[26] In the proceedings of August 31, 2018, dealing with the liquidator's further report before the liquidation judge, Taylor sought to contest both the amount and the underlying indebtedness of EPG to TBF. It is unclear from the transcript of the proceedings whether the liquidation judge ever turned his attention to that issue. However, with the liquidation judge having accepted that a reallocation should occur, counsel for the liquidator made it clear that there were no longer funds available to satisfy that indebtedness. The matter was therefore moot.

Issues

[27] These appeals raise the following issues:

- a) as to the Marshalling Order, whether the liquidation judge erred in ordering the reallocation of the BMO debt between TBF and EPG such as to allow RLW to recover fully on its securities acquired from BNS, FCC and RBC and to allow Pitblado to make a more substantial recovery, ahead of unsecured creditors;
- b) as to the Distribution Order, whether the liquidation judge erred in dismissing the challenge to the claims of the Wiebes and TBF in the EPG claims process and, if the Marshalling Order is set aside, whether the intercompany debt claim between TBF and EPG should be reviewed; and
- c) as to the Supplemental Order, whether Pitblado, as a judgment creditor, was entitled to rank in priority to unsecured creditors and benefit from the reallocation notwithstanding the potential bankruptcy of TBF or EPG.

Standard of Review

[28] The liquidation proceedings were conducted pursuant to the provisions of the *Act* (see section 207 and following).

[29] Pursuant to those provisions, a court has the power to make a number of different orders it thinks fit, including:

- a) orders determining the validity of any claims made against a corporation (see section 210(e));

- b) orders approving payment, satisfaction or compromise of claims (see section 210(h)); and
- c) orders giving directions on any matter arising in the liquidation (see section 210(j)).

[30] These orders were made in the course of the Court's supervision of the liquidation. They are, for the most part, discretionary orders for which a liquidation judge is entitled to significant deference. Unless the liquidation judge has misdirected himself or the order is so wrong as to amount to an injustice, appellate interference is not justified (see *Perth Services Ltd v Quinton et al*, 2009 MBCA 81).

Issue #1—The Marshalling Order

The Doctrine of Marshalling

[31] Marshalling is an equitable remedy, intended to protect the recovery of a junior creditor against the arbitrary action of a senior creditor, and to thereby treat all secured creditors equitably.

[32] While its origin may be as early as Roman civil law, it found its way into English law in the mid-17th century (see Bruce MacDougall, "Marshalling and the Personal Property Security Acts: Doing Unto Others. . ." (1994) 28:1 UBC L Rev 91 at 91, online (pdf): *Allard Research Commons* <commons.allard.ubc.ca/fac_pubs/220>. One of the most recognised statements of the doctrine was set out by Lord Eldon in *Aldrich v Cooper* (1803), 8 Ves Jun 382, 32 ER 402 (Ch (Eng)) (at p 407):

... a person having two funds shall not by his election disappoint the party having only one fund; and equity, to satisfy both, will throw him, who has two funds, upon that, which can be affected by him only; to the intent that the only fund, to which the other has access may remain clear to him.

[33] To obtain marshalling, certain specific criteria must be met. These criteria include the requirements that: two or more creditors share a single common debtor; and the senior creditor has a claim against two of the debtor's funds, while the junior creditor, ranking behind the doubly secured senior creditor, has recourse to only one (see *Green v Bank of Montreal*, 1999 CarswellOnt 3954 (CA)).

[34] The Supreme Court of Canada has not discussed marshalling in any detail. The most recent decisions of this Court addressing the doctrine are more than 100 years old (see *In Re Hamilton Trusts*, 1895 CanLII 155; and *Dominion Lumber & Fuel Co v Gelfand*, 1916 CarswellMan 110). In both *Hamilton* and *Dominion Lumber*, this Court declined to grant marshalling because there was no single common debtor.

[35] An exception to the single common debtor rule has developed in situations where a surety and principal relationship exists between the two debtors (see *Brown v Canadian Imperial Bank of Commerce*, 1985 CarswellOnt 729 (SC (H Ct J))).

[36] Furthermore, as stated in his text, Walter M Traub, *Falconbridge on Mortgages*, 5th ed (Toronto: Thomson Reuters, 2003) (loose-leaf updated 2019, release 29) at 14-23, the single common debtor requirement and a general exception can be described as follows based upon the decisions of *Ex parte Kendall* (1811), 17 Ves Jun 514, 34 ER 199; and *Ernst*

Bros Co v Canada Permanent Mortgage Corp, [1920] OJ No 147 (Ont SC (HC Div)):

It is often stated that marshalling does not apply unless the creditors, in the language of Lord Eldon, “both are creditors of the same person” [quoting from *Kendall* at p 201]. . . . While, however, the ordinary case for the application of the doctrine is that of two creditors and a common debtor, it is sufficient that as between the persons interested [in] the two debts ought to be paid by the same person even though that person may not be directly liable to the creditor for the two debts.

[37] In *Ernst*, Orde J formulated the doctrine as follows (at para 24):

. . . It must, of course, be almost universally the case that in the application of the doctrine there will be a single debtor and two creditors, and that in cases where there are two debtors the doctrine is inapplicable, not because there are two debtors but because it would be inequitable as between those debtors to marshal the securities. . . .

Bars to Marshalling

[38] Jurisprudence recognises bars to marshalling. The first one is that marshalling will not be permitted if it would interfere with the superior right of a secured creditor to pursue its remedy against either of the two funds. The other bar, for our purposes, is that the doctrine is applicable unless it causes prejudice to a third party. Potential prejudice to unsecured creditors is irrelevant (see *Williamson v Loonstra* (1973), 34 DLR (3d) 275 (BC SC), cited in *St Gregor Credit Union Ltd v Zimmer*, 2004 SKQB 75; and *Ledco Ltd, Re*, 2008 CarswellOnt 6137 (Sup Ct J)).

Position of Taylor and 067

[39] With respect to the appeal of the Marshalling Order, Taylor and 067 take the position that the liquidation judge committed reversible error by misapprehending the facts upon which he reached his conclusion and by failing to appreciate the law on marshalling. They recognise that the standard of review on the misapprehension is one of palpable and overriding error but argue that the failure to appreciate the requirements of the law on marshalling is to be reviewed on a standard of correctness.

[40] As to the misapprehension, they point to the liquidation judge's comments in his first endorsement, whereby he proceeded on the belief that RLW held security over the assets of EPG such that marshalling was not required, an obvious error.

[41] As to the misapplication of the law, they argue that marshalling was and is not available given that there is no single common debtor and that the exception relating to sureties and principals does not apply to the fact situation, particularly given that there was no guarantee of the FCC debt by EPG.

[42] Taylor and 067 also argue that there was no second fund available as RLW did not have access to both funds (being the proceeds of the sale of the assets of TBF and EPG) for which the senior creditor, BMO, had security. In their submission, the guarantee given by EPG did not constitute a fund at the disposal of RLW.

[43] For these reasons, they argue that there is no basis upon which the liquidation judge could find that RLW is entitled to the funds remaining in EPG for the purposes of satisfying the debts RLW had purchased from the creditors of TBF.

Position of Wolfe and 269

[44] In response, Wolfe argues marshalling is available simply because TBF and EPG should be treated as one entity. It was admitted in cross-examination by Taylor that the farming operation was conducted by both companies as one. The mutual cross-guarantees given to BMO by both entities in like amounts confirm that they were, in essence, being operated jointly. This would satisfy the one-debtor rule for the purposes of applying the doctrine of marshalling and would also address the issue of two funds as the single debtor would be the source of the second fund. Wolfe also argues that there has been recognition that the doctrine can be applied in situations of two or more debtors as long as the matter relates to the same debt (see *Condominium Corporation No 082 6970 v 1117398 Alberta Ltd*, 2012 ABQB 233 (*Condo Corp 6970*)). It is not limited to the precise principal/surety exception articulated in the *Brown* decision.

Position of the Wiebes

[45] The Wiebes acknowledge that the proposal advanced by Wolfe would not affect their interests as he requested that the EPG assets be subject to a holdback to satisfy their claim in priority to the reallocation of the BMO debt repayment. As such, there is no prejudice to a secured third party. The quantification of the Wiebes' claim is another issue and will be dealt with in the discussion of the Distribution Order.

Position of Pitblado

[46] Pitblado agrees with Wolfe and says that it too should benefit from the doctrine of marshalling as its judgments made it akin to a secured

creditor or, at the very least, that it should rank above other unsecured creditors. As mentioned previously, at the hearing of August 31, 2018, Pitblado advanced the argument that it should rank as a junior secured creditor.

Analysis

[47] The effect of the Marshalling Order was to reallocate between TBF and EPG funds in the hands of the liquidator to allow RLW to realise on its securities to a greater extent and provide funds to satisfy Pitblado's judgments.

[48] The liquidation judge reached his first decision on a factually incorrect premise, namely, that RLW had access to the assets of both TBF and EPG. That was an error and led him to the initial finding that marshalling was not required. It was a clear and palpable error. He then proceeded to reach a similar outcome by, in essence, ordering marshalling without calling it so. There was no basis for him to do so in law. This was also reversible error.

[49] In our view, marshalling is not available on the facts of this case as there is not a single common debtor. RLW argues that marshalling in favour of itself and Pitblado should be allowed on the basis that the single common debtor criterion is met because TBF and EPG should be considered as one entity. In our view, EPG and TBF can only be treated as one entity if the corporate veil between them is pierced.

Piercing the Corporate Veil

[50] Piercing the corporate veil in the context of marshalling has been the subject of considerable American authority (see Paul AU Ali, *Marshalling of Securities: Equity and the Priority-Ranking of Secured Debt* (Oxford: Clarendon Press, 1999) at 147-53), and has been mentioned by one Canadian court. In *Montmor Investments Ltd v Montreal Trust Co*, 1984 CarswellBC 130 (SC), McKenzie J discussed the possibility of piercing the corporate veil to allow marshalling but declined to do so. As explained by Professor MacDougall (MacDougall at pp 105-6):

The question of two legal persons being considered a common debtor for the purposes of marshalling will often arise in the context of a corporate debtor. The court in [*Montmor*] . . . alluded to the possibility that a corporate veil could be lifted so as to make a shareholder and the company a common debtor for the purposes of the doctrine of marshalling. However, in that case, the court found that there was not such unity between the various corporate entities to justify lifting the corporate veil. In the U.S., most courts have declined to lift the corporate veil so as to use the doctrine of marshalling because the proponent has not met the high standard of proof (clear and convincing evidence) required to rebut the presumption of separate entities. . . . The decision to lift the corporate veil will be made in accordance with the general rules of when it is appropriate to do so. . . .

[emphasis added]

[51] Canadian courts have been very reluctant to pierce the corporate veil, whether by looking behind the corporation at the shareholder or by treating two or more corporations as one entity. Generally, the separate identity of related or integrated corporations has been disregarded only where there is evidence that one corporation is a subsidiary, which is completely dominated by its parent, such that it does not operate independently—almost invariably with an improper purpose; or there is

clear evidence establishing that one corporation is an express or implied agent of the other corporation. That said, as an exception to the general proposition that the corporate veil should be lifted only in cases of illegality or agency, some courts have recognised a “group enterprise”¹ or “single business entity” concept² where an injustice would otherwise result, but this has been carefully limited (see *Salomon v Salomon & Co*; *Salomon & Co v Salomon*, [1897] (1896) AC 22 (HL (Eng))); *Fairview Donut Inc v The TDL Group Corp*, 2012 ONSC 1252, affirmed 2012 ONCA 867, leave to appeal to SCC refused, 35207 (16 May 2013); and *Teti and ITET Corp v Mueller Water Products*, 2015 ONSC 4434 at paras 17-21).

[52] The reason for the courts’ reluctance to pierce the corporate veil is clear. As stated in CED 4th (online), *Business Corporations* (Ont), “Introduction: Characteristics of Corporation: Limited Liability: Piercing or Lifting Corporate Veil” (I.2.(b).(ii)) (at para 35):

If investment is to be encouraged, it is necessary that stability prevail. The constant recognition of corporate personality promotes stability, for otherwise investors and business people would be unable to predict when the corporate form would be respected and when it would not, and thus no confidence would be placed in it. The need for stability justifies the limited willingness of the courts to pierce the corporate veil.

[53] In this case, the evidence does not establish the domination of either TBF or EPG by the other for improper purposes, or otherwise, nor an agency relationship between them. Furthermore, there is not sufficiently

¹ *Teti and ITET Corp v Mueller Water Products*, 2015 ONSC 4434 at para 19

² *Fairview Donut Inc v The TDL Group Corp*, 2012 ONSC 1252 at para 657, affirmed 2012 ONCA 867, leave to appeal to SCC refused, 35207 (16 May 2013), quoting from *801962 Ontario Inc v MacKenzie Trust Co*, 1994 CarswellOnt 6168 at para 37 (Ct J (Gen Div))

clear and convincing evidence of the unity between the two companies to support a finding that they should be treated as one.

The Operation of TBF and EPG

[54] As previously stated, for many years, starting in 2008, TBF and EPG were engaged in a farming enterprise. The two companies had the same owners and ownership structure. They provided full security and cross-guarantees to their primary secured creditor, BMO. While Taylor acknowledged on cross-examination that the companies were conducting business together, with EPG effectively operating as part of TBF, this arrangement is typical of the manner by which many enterprises structure and conduct their affairs.

[55] Furthermore, there is significant evidence indicating that TBF and EPG were operated as separate entities throughout:

- At the outset of Wolfe's involvement in the business, a decision was made to conduct the farming operation through two corporations as opposed to another business structure, such as a partnership.
- The USA signed by Wolfe and Taylor was in relation to TBF only.
- EPG was solely a landholding company whereas TBF operated the farm (and also owned some farmland). The lands held by the two companies were not owned jointly; each held separate parcels. Agricultural buildings were situated on land owned by

EPG while a farm home, older farm buildings and a vacant residence were on land owned by TBF.

- TBF employed about 40 people during the growing season and had liabilities to these employees. There is no evidence that EPG shared these liabilities.
- Although the evidence includes a Combined Financial Statement for TBF (together with EPG, 067 and 269) as of December 31, 2013, there are also Non-Combined Financial Statements for TBF only.
- The arbitration award dated August 24, 2016 addressed an issue regarding Taylor’s remuneration as an employee of TBF during the years 2013 and 2016. The issue involved interpretation of a contract between TBF and Taylor—that is, whether “profits of the employer” meant only profits from the operation of TBF or also profits from the sale of TBF lands and profits from EPG. Interestingly, contrary to the positions taken on these appeals, Wolfe argued before the arbitrator that profits from EPG should not be included as TBF was the only party named in the employment contract, and Taylor argued that profits from EPG should be included because the parties always treated EPG and TBF as a single entity.
- Land titles registrations indicate that, over many years, the two companies gave individually secured mortgages to BMO and

only the last \$10,000,000 credit advance by BMO was a jointly secured debt on the land owned by each corporation.

- In 2014, BMO's term sheets for its loans set different credit limits for each corporation: \$4,308,475 for TBF and \$1,993,737.64 for EPG.
- BMO kept track of the amounts loaned to each corporation which is how it generated its payout statements. The parties were aware of this as counsel for Wolfe sent an email to counsel for Taylor on May 7, 2016, confirming an agreement between the parties that money received from renting EPG and TBF lands should be forwarded to BMO "with specific instructions that the amounts be applied to the credit of TBF against the outstanding debt owing by TBF to BMO on the line of credit."
- TBF borrowed money from FCC, BNS and RBC, and provided security to those entities. EPG only provided guarantees on those debts and did not provide a guarantee to FCC.
- The Wiebes are secured creditors of EPG but not of TBF.
- Pitblado, lawyers for both companies, sued TBF and EPG separately and obtained default judgment against each, treating them as separate entities.

- The liquidator's instructions to creditors indicated that the creditor should set out its claims against TBF and its claims against EPG separately.
- The liquidator has advanced a claim for an intercompany debt, owed by EPG to TBF, in excess of \$900,000.

[56] In these circumstances, RLW has not established that it is equitable for the corporate veil between TBF and EPG to be pierced such that they should be considered one entity. The single common debtor criterion has not been satisfied.

Principal/Surety Exception

[57] An exception to the single common debtor rule has developed related to sureties and principals. We are of the view that the facts of this case do not bring it within that exception. The first factual problem is that a major component of the RLW debt, the FCC loan, is not the subject of any guarantee by EPG to TBF. As conceded by RLW in argument on appeal, the principal/surety exception has no application in the facts of this case, even where guarantees were provided.

[58] In *Brown* at para 12, the Court explained the exception, adopting the following passage from the decision of Bell J in the Supreme Court of Pennsylvania case of *Neff v Miller*, 8 PA 347 (1848):

Here is a surety, whose money has been applied in payment of the debt of his principal, to the exclusion of his own proper creditors. That he would be entitled to come in, by way of substitution, upon the estate of the principal, is every-day equity; and I think it equally clear, that his creditor, who has suffered by

the appropriation of a fund which otherwise would have been available for the discharge of his claim, may well ask to stand upon this equity, to the extent of the deprivation to which he has been subjected.

[59] Similarly, according to Halsbury's Laws of Canada (online), *Guarantee and Indemnity*, "The Rights of a Surety: As Against the Creditor: Securities in Favour of the Creditor" (V.1.(5)) at HGI-234 "Surety Entitled to Securities Received by Creditor from Principal" (Cum Supp – 1 June 2019):

. . . **It is an ancient** principle, . . . founded upon the equitable doctrine of marshalling, . . . that unless otherwise agreed . . . on payment or performance by the surety of the guaranteed obligation, . . . the surety has the right to the benefit of all securities that the creditor has received from the principal debtor in respect of the debt in order to enable the surety to obtain satisfaction for what the surety has paid. . . .

Similar equitable principle governs marshalling of funds and securities. The surety's rights with respect to securities existing in respect of the guaranteed obligation are derived from the equitable doctrine imposed upon the principal debtor to indemnify the surety. . . . In addition, it is felt to be inequitable for a creditor to fail to realize against a security which is available to the creditor in respect of the guaranteed debt, and instead to throw the whole liability upon the surety. (underlining added) . . . To compensate the surety for the payment that the surety has made on the principal's behalf in respect of the guaranteed debt, the surety is given a right to look to the security held by the creditor in respect of that debt. . . . As mentioned above, this right is based upon general principles of equity that are similar to those which govern the marshalling of funds and securities. . . .

[60] These passages confirm that marshalling may be allowed based on the principal/surety exception in circumstances where the senior creditor of both the principal debtor and surety seeks payment from the surety—to the

detriment of the junior creditor of the surety which has access only to the property of the surety. That junior creditor can invoke marshalling in order to have the senior creditor's claim paid by the principal debtor. This arises because of a principal debtor's obligations to the surety.

[61] By contrast, in the present case, it is the junior creditor (RLW) of the principal debtor (TBF) rather than the junior creditor of the surety (EPG) that seeks marshalling. It asks to have funds of the surety marshalled. However, marshalling is not fair in this situation because a surety has no obligation to indemnify a principal debtor (see MacDougall at p 108).

[62] Finally, the principal/surety exception has no application with respect to Pitblado as the debts owed to it by each of TBF and EPG are not the subject of guarantees.

Other Circumstances Where Marshalling May be Just and Equitable

[63] With respect to *Condo Corp 6970*, which was the authority relied upon by Wolfe on this issue and in which the Court found that marshalling was available where the "funds belong[ed] to the same debtor, or to two or more debtors with respect to the same debt" (at para 43), it is not clear how the Court arrived at that language. The decision, which seems to extend marshalling beyond the scope allowed in other cases, was not appealed, nor has it been judicially considered by any other court.

[64] In this case, we are of the view that it is not just and equitable to order marshalling. RLW assumed the loans of FCC, RBC and BNS to TBF on the basis that it would have security against the assets of TBF and partial

guarantees from EPG. Had RLW insisted on more security before assuming those loans, it could have sought it from EPG but it did not do so.

[65] Nonetheless, the effect of allowing marshalling is that RLW would be paid, before the unsecured creditors of EPG, from the funds of EPG that resulted from the sale of its land. RLW would effectively become a secured creditor of EPG despite it holding no security against the assets of EPG—and, with respect to the debt RLW assumed from FCC, not even having a guarantee from EPG.

Conclusion on the Issue of the Marshalling Order

[66] For the reasons outlined above, we would not order marshalling in favour of RLW or Pitblado on the facts of this case. That is not to say that an order of marshalling may not be allowed in a case of related companies which do not fall strictly within the criteria that have traditionally been followed in the granting of the remedy to date. In an appropriate case, a court retains the power to pierce the corporate veil in a situation where equity would demand such an outcome (in the context of the enforcement of a judgment, see the concurring reasons of Nordheimer JA in *Yaiguaje v Chevron Corporation*, 2018 ONCA 472, leave to appeal to SCC refused, 38183 (4 April 2019)). However, on the evidentiary matrix before us, our view is that it would not be just and equitable to pierce the corporate veil to allow marshalling.

Issue #2—The Distribution Order

[67] Taylor and 067 appeal from the Distribution Order made by the liquidation judge whereby he approved a distribution schedule. Two areas of contention by Taylor with respect to that schedule are:

- a) recognition of an “inter-company debt” owing to TBF from EPG in the amount of \$916,336; and
- b) payment to the Wiebes with respect to security held by them over the assets of EPG.

Intercompany Debt

[68] As a consequence of our conclusion regarding marshalling, the intercompany debt claim of TBF against EPG is not moot.

[69] Taylor was only notified of the liquidator’s approval of the intercompany debt in the EPG claims process on August 9, 2018 when it was included on a proposed distribution schedule for the first time.

[70] In correspondence with the liquidator and in submissions before the liquidation judge, Taylor/067 sought to challenge this intercompany debt. In a letter to the liquidator dated August 24, 2018, they argued that a thorough accounting between EPG and TBF would show that TBF owed funds to EPG for a number of reasons as set out in that letter. They also advised the liquidator that they would be taking that position at the next appearance before the liquidation judge on August 31, 2018.

[71] While no further affidavit evidence was provided to the liquidation judge at that hearing providing substantive details regarding this issue, it was raised before him at that time. However, the liquidation judge did not turn

his mind to the issue as it had been rendered moot once he ordered the reallocation sought by RLW. On appeal, Taylor/067 take the position that, if marshalling is not allowed, the issue of the intercompany debt should be remitted to the liquidation judge for adjudication.

[72] The liquidator argues that, even if marshalling is not allowed and no reallocation is made, there is no basis for this Court to interfere with its approval of the intercompany debt and the matter should not be returned to the liquidation judge. The liquidator notes that it conducted a claims process in respect of EPG in accordance with the order approving a claims process for both companies (the Claims Process Order), which provided for a final and conclusive determination of a claimant's claim by an independent court officer—the liquidator. The liquidator further argues that the Claims Process Order gives Taylor/067 no standing to challenge the claim; the relevant records to challenge the claim were in the possession of Taylor/067 and not presented to the Court; and the doctrines of collateral attack and issue estoppel protect the Claims Process Order.

[73] We are of the view that the liquidation judge has meaningful supervisory jurisdiction to review a determination made by the liquidator during the claims process. That jurisdiction has not yet been exercised in connection with the intercompany debt. Therefore, the matter should be remitted to the liquidation judge for that purpose.

[74] While it will be the liquidation judge's decision as to how to conduct that review, given the extensive litigation which has already taken place over these issues and the need to respect the proportionality principle, a summary proceeding in keeping with the liquidation process would appear

to be the desired approach. A quick resolution also takes into consideration the fact that no further information substantiating their position has been provided by Taylor/067 either by affidavit or other form notwithstanding a promise to do so in the August 24, 2018 letter.

The Wiebes' Claim

[75] The exact nature of the Wiebes' relationship with EPG and the nature of its security are unclear. However, as early as the liquidator's second report in March 2018, the fact that they were secured creditors was known. In its supplement to the second report, the liquidator advised that it had received a legal opinion to the effect that the Wiebes' security was valid and enforceable, that the lands owned by EPG were charged with a second fixed and specific charge in favour of the Wiebes ranking behind the BMO registration, and that their security ranked in priority to the claims of the unsecured creditors of the company. At that time, the exact amount of the indebtedness was not known given that the claims process, while approved by the Court, had not yet been instituted by the liquidator.

[76] As stated previously, the sale and vesting order preserved priorities in the sold lands as if the lands had not been sold and attached that priority to the net proceeds of the sale, in essence preserving whatever security interest the Wiebes had in the EPG lands.

[77] At the hearing of the marshalling argument on June 21, 2018, the liquidation judge was advised that, under the allocation proposed by RLW, the Wiebes would have a holdback from the EPG funds pending a final determination of the quantum of their claim.

[78] In the meantime, the Wiebes had submitted their proof of claim to the authorised claims officer on June 10, 2018. On August 21, 2018, the liquidator issued a notice of revision of proof of claim for the Wiebes, informing them that, after deduction of an offsetting claim by EPG, the amount was \$813,928, which amount was disclosed in the liquidator's fourth report of August 27, 2018 and to which the Wiebes agreed.

[79] At the August 31, 2018 hearing before the liquidation judge, the liquidator sought the approval of its proposed distribution, including the payment of the Wiebes' claim.

[80] In an affidavit filed on August 30, 2018, Taylor disputed the Wiebes' claim on the grounds that "the claim may be extinct or significantly less than the amount stated by the [l]iquidator". In Taylor's affidavit, he suggests that the Wiebes removed equipment with an estimated value of approximately \$400,000 and that the Wiebes had already received sale proceeds from the sale of the EPG lands.

[81] At the hearing of August 31, 2018, the liquidation judge determined that the claims process had resolved the matter and that he was not going to revisit it.

[82] On appeal, Taylor took the position that the liquidation judge failed to hear his argument on the Wiebes' claim, thereby failing to observe the rules of natural justice and procedural fairness.

[83] The liquidator's position before us was that Taylor had no standing to challenge the liquidator's decision approving the claim and its quantum. As well, the liquidator's actions were in accordance with the claims process,

which had been approved by the Court, and there was no appeal available from those determinations.

Analysis

[84] While we would not agree with the position taken by the liquidator's counsel on the hearing of the appeal that a court has such a limited supervisory role in reviewing a determination by the liquidator made during the claims process, we are satisfied that, on the facts of this case, the liquidation judge properly exercised his discretion not to interfere in the determination of liability and the quantum with respect to the Wiebes' claim. Taylor knew as early as the supplement to the second report that the liquidator had viewed the Wiebes' security as valid and enforceable and that only quantum was left to be determined. While, admittedly, the determination of the correct quantum came late in the day, the evidence which could have changed that determination could have been placed before the liquidator by Taylor much sooner than August 30, 2018 and in a more complete fashion. That the liquidation judge chose not to become involved in reviewing the correctness of the liquidator's decision based upon the limited information in Taylor's affidavit is understandable. While it would have been preferable for the liquidation judge to provide Taylor's counsel with a greater opportunity to explain the reasons for his challenge to the Wiebes' claim, a failure to do so does not amount to a breach of natural justice in the circumstances of this case.

Conclusion

[85] For these reasons, we would allow the appeal from the Distribution Order only to enable a review of the intercompany debt claim.

Issue #3—The Pitblado Claims

[86] Pitblado provided legal services to TBF and EPG. In 2016, it commenced proceedings against TBF and EPG and obtained default judgments in the sums of \$51,889.33 and \$23,296.14 respectively. It registered its judgments against the lands of both corporations. When those lands were sold pursuant to the sale and vesting order, their judgment registrations were erased. Noteworthy, however, as discussed previously, is that the sale and vesting order provided that all claims and encumbrances against the lands existing prior to the sale would attach in the same priority to the net proceeds of the sale as if the lands had not been sold.

[87] In his first endorsement, the liquidation judge failed to address Pitblado's argument but, upon being requested to do so, he held in a second endorsement that he was not convinced of the availability of the remedy to Pitblado but would consider further argument.

[88] At a further hearing on September 25, 2018, the liquidation judge granted relief to Pitblado, directing that they stood behind RLW but ahead of all other general unsecured creditors with respect to the net proceeds of the sale of the lands such that marshalling was available to it. He also directed that such a priority would exist notwithstanding a bankruptcy proceeding; the liquidation judge's order to that effect was made in the Supplemental Order.

[89] Taylor appeals the liquidation judge's decision to recognise Pitblado's judgment claims ahead of unsecured creditors on the basis that Pitblado is simply a judgment creditor and not a secured one. As well, the

issue of whether the order should survive a bankruptcy was sprung at the last minute and not properly dealt with.

[90] Pitblado argues that the registration of its certificates of judgment as against the TBF and EPG lands makes it a “junior secured creditor”. Thus, the liquidation judge rightly found (in the context of considering the availability of marshalling) that it should hold a position as something less than a fully secured creditor but greater than an unsecured or general creditor.

[91] For the reasons we have given discussing the issue of marshalling, we are of the view that Pitblado’s arguments fail on whether marshalling applies to its claims. However, we have come to the conclusion that Pitblado should be entitled to receive the funds owing to it under its judgments from each of TBF and EPG in advance of the other unsecured creditors in the liquidation. We reach this conclusion not on the basis of marshalling but because, in our view, the sale and vesting order granted in this case, which is not the subject of appeal, recognised the priority of the judgments of Pitblado as a registered judgment creditor, preserving its priority with respect to the proceeds of the sale of the lands as if the lands were still held by the respective owners. For that reason, we would grant the relief requested and authorise payment by the liquidator to satisfy the judgments.

[92] However, as to the provision in the Supplemental Order that such a priority would survive a bankruptcy, we hold a different view. The granting of that order in its current form raises concerns. In the first place, we agree with Taylor/067 that they were not provided with sufficient opportunity to

challenge the appropriateness of granting that order. It was raised at the last minute on the hearing to determine the form of the order.

[93] Of greater concern is that it was presented to the liquidation judge as a standard form of order in order to ensure that determinations made by the liquidation judge are not reviewed in a bankruptcy proceeding as a fraudulent preference. However, the Supplemental Order goes further. By its terms, it validates Pitblado's claims, to the extent they are not otherwise satisfied, over any other "unsecured creditor or creditors of TBF or EPG". This presumptively seeks to grant Pitblado a priority in not only the liquidation proceedings, but also on any further bankruptcy proceedings. No law or jurisprudence has been provided to warrant such a conclusion. It may well be that, in a bankruptcy proceeding, notwithstanding the terms of the sale and vesting order, Pitblado would rank solely as an unsecured creditor on the basis of its judgments. Unless there was some reason, equitable or otherwise, to justify a priority in a yet-to-occur bankruptcy, a presumptive order made in anticipation is not warranted in the circumstances. If a bankruptcy does occur, the matter of a priority should be determined by a bankruptcy court according to the appropriate legal principles governing that eventuality.

[94] Therefore, while Pitblado's claims should be recognised in advance of other unsecured creditors in accordance with the priorities set out in the sale and vesting order, the Supplemental Order should be limited to claims of fraudulent preferences or advances under the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3.

Disposition

[95] For the foregoing reasons, we would:

- (1) allow the appeal from the Marshalling Order and from the Distribution Order to the extent that they provide for reallocation based on marshalling;
- (2) refer the intercompany debt claim to the liquidation judge;
- (3) subject to the results of the review of the intercompany debt claim by the liquidation judge, order distribution as set out in Scenario 1 (no residual fund reallocation) of the liquidator's fourth report;
- (4) allow the Pitblado claims to rank in priority to other unsecured creditors in the liquidation proceedings but leave any priority to be claimed in a bankruptcy proceeding to the bankruptcy court if it arises; and
- (5) allow distribution to the Wiebes according to their claim.

Costs

[96] We would allow costs as follows:

- (1) costs in the Court below in connection with the Marshalling Order in accordance with the applicable tariff and one set of costs in this Court in accordance with Tariff C, both in favour of Taylor/067, to be paid by RLW;
- (2) one set of costs in this Court in accordance with Tariff C in favour of each of the Wiebes and the liquidator to be paid by

Taylor/067 in respect of the Distribution Order appeal—we order no costs on the intercompany debt issue to any party but direct that the costs be dealt with by the liquidation judge upon the hearing of the matter; and

(3) as to the Pitblado claims, given the relative success of both parties, we order no costs in this Court and, as no costs were provided in the Court below, we make no disposition with respect to those costs.

_____ JA

_____ JA

I agree: _____ CJM

TAB 7

KeyCite treatment

Most Negative Treatment: Distinguished

Most Recent Distinguished: [Williams v. Oulahan](#) | 2001 CarswellOnt 4456, 30 C.B.R. (4th) 240, 110 A.C.W.S. (3d) 564 | (Ont. S.C.J., Dec 19, 2001)

1995 CarswellOnt 46

Ontario Court of Justice (General Division)

807933 Ontario Inc. v. Allison (Trustee of)

1995 CarswellOnt 46, [1995] O.J. No. 324, 22 O.R. (3d) 102, 30 C.B.R.
(4th) 144, 30 C.B.R. (3d) 144, 44 R.P.R. (2d) 237, 53 A.C.W.S. (3d) 428

Re bankruptcy of ROSSWELL MYLES ALLISON

807933 ONTARIO INC. (c.o.b. 1516 ENGINEERING) and HENDERSON, PADDON &
ASSOCIATES LIMITED v. PADDON & ASSOCIATES (trustee in bankruptcy for R. MYLES
ALLISON, bankrupt), SAM WARNOCK, DAVID DAWSON & ASSOCIATES LIMITED,
CHERYL RUMBLE, DAWN THOMPSON, MARY TEETER ALLISON and REVENUE CANADA

Ground J.

Heard: December 22, 1994

Judgment: February 15, 1995

Docket: Doc. 31-285350

Counsel: *Ross H. Thomson* and *Peter C. Card*, for applicants.
William J. Leslie, Q.C., for respondent Mary Teeter Allison.

Subject: Corporate and Commercial; Insolvency; Property

Related Abridgment Classifications

Bankruptcy and insolvency

[X](#) Priorities of claims

[X.1](#) Secured claims

[X.1.e](#) Miscellaneous

Real property

[VIII](#) Mortgages

[VIII.14](#) Priorities

[VIII.14.a](#) Doctrines

[VIII.14.a.ii](#) Marshalling

Real property

[VIII](#) Mortgages

[VIII.14](#) Priorities

[VIII.14.c](#) Determining priorities between types of creditors

[VIII.14.c.xiii](#) Miscellaneous

Headnote

Bankruptcy --- Priorities of claims — Secured claims — Marshalling of secured claims

Mortgages --- Priorities — Between types of creditors — Registered mortgagees — Marshalling

Mortgages --- Priorities — Between types of creditors

Secured creditors — Marshalling — Subconsultants asserting right to marshall their claims against bankrupt architect — Subconsultants having obtained judgment against bankrupt and filed writs of execution — Subconsultants being unsecured creditors until writ executed — Unsecured creditors being unable to invoke doctrine of marshalling.

In 1994, an architect filed an assignment in bankruptcy, leaving various subconsultants unpaid for their work. The bankrupt's only asset at the time of the assignment was a parcel of land, which his wife had severed from a parcel she held and conveyed to him for \$1 many years before. The two parcels of land had been mortgaged jointly under the same instrument seven times and collaterally once. In each mortgage, the bankrupt and his wife covenanted to be liable for the money due under each mortgage. In 1992, both parcels had been mortgaged in trust for \$185,000 to the same mortgagee. The mortgages were cross-guaranteed. The bankrupt's parcel of land was sold and the cross-guaranteed mortgages were substantially paid off out of the net proceeds of the sale.

The subconsultants applied for an order declaring that they, as creditors, were entitled to marshall their claims against the parcel of land formerly owned by the bankrupt and that the mortgagee should have recourse to the wife's parcel of land before having recourse to the bankrupt's. They sought an order declaring that they were entitled to an assignment of the mortgage to the mortgagee on the wife's parcel, and an order declaring the an amount equal to the net proceeds received from the sale of the bankrupt's parcel should be available to them from the wife's parcel to satisfy the debts owed to them. In the alternative, they sought an order declaring that the wife had been unjustly enriched by the sale of the bankrupt's parcel and that her parcel should be subject to a constructive trust.

Held:

The application was dismissed.

The first criterion for the application of the doctrine of marshalling requires that the mortgagee have access to two properties from which the payment due under the mortgages could be satisfied, and have resorted to only one property. That criterion was satisfied in the case at bar. The second criterion requires that there be a common debtor. In the case at bar, where there were cross-guarantees given on both mortgages and where the mortgages provided that the mortgagee could proceed directly against the guarantor without first exhausting the mortgagee's rights against the mortgagor, both the bankrupt and his wife were common debtors. The doctrine can apply in situations where there is a joint debt to one creditor and a second debt due to another creditor, which is given directly by one of the joint debtors and assigned by the other joint debtor.

In the case at bar, the subconsultants were initially unsecured creditors. They later obtained judgment against the bankrupt and his wife and filed writs of execution. However, a writ filed, but not yet executed under the [Execution Act \(Ont.\)](#), does not create a secured interest in any asset of the judgment debtor. An unsecured creditor may not invoke the doctrine of marshalling.

The claim for apportionment could not succeed. The remedy cannot be granted where the two mortgages in question were given by different owners on two parcels of property, even if that was done to secure a single debt. Further, the subconsultants, as unsecured creditors, were not entitled to assert the right of apportionment.

With respect to the unjust enrichment claim, the evidence did not suggest that the enrichment of the bankrupt's wife was truly unjust in the circumstances. There was no reason to subject the wife's parcel of land to a constructive trust.

Annotation

This case is a fascinating read for real estate lawyers, particularly those in the bar practicing mortgage remedy work.

Firstly, and most notably, the case reminds practitioners of the doctrine of marshalling, a chapter in *Falconbridge on Mortgages* all too often ignored or glossed over. Although the analysis of marshalling in *Allison* is not extensive, the case does at least confirm that the doctrine of marshalling *cannot* be invoked by unsecured creditors.

Secondly, the case confirms that execution creditors do not become secured merely by filing a writ of execution, and, in fact, are not embellished with secured creditor attributes unless and until the sheriff actually executes the writ. Therefore, while real estate practitioners have been conditioned, for the purposes of a title search, to treat an execution creditor as if it were another mortgage on title, for other purposes (including, of course, ascertaining the availability of the doctrine of marshalling, but also, for instance, the death of a joint tenant subject to a writ of execution), no secured status is conferred upon judgment creditors unless and until the sheriff has taken possession of the property or published a notice of sale.

Thirdly, the court neatly disposed of the argument that the guarantor wife had been "unjustly enriched" as a result of the mortgagee's decision to sell the execution debtor husband's property in preference to the guarantor wife's property (even though both were available for sale by the mortgagee). While the enrichment and corresponding deprivation were obvious (as is usually the case), Ground J. rightly pointed out that the juristic reason negating unjust enrichment "need not be tied to the applicant creditors," but, instead, could arise as between the execution debtor and his guarantor wife.

Finally, in *Allison*, the court was asked by the execution creditors to, first, apportion all of the mortgage debt onto the unsold parcel, failing which, to at least apportion the indebtedness pro rata against each parcel based upon their respective values. With some considerable relief to all counsel of mortgagees generally, Ground J. refused apportionment of the mortgage debt, finding instead that the apportionment remedy, like the doctrine of marshalling, is not available where the mortgagors are different (even though the indebtedness is all and singular), and, in any event, is not available to execution creditors.

Jeffrey W. Lem

Table of Authorities

Cases considered:

Bank of Nova Scotia v. Adriatic Development Ltd. (1984), [1985] 2 W.W.R. 627, 60 B.C.L.R. 294 (S.C.) — *distinguished*
Becker v. Pettkus, [1980] 2 S.C.R. 834, 19 R.F.L. (2d) 165, 8 E.T.R. 143, 119 D.L.R. 257, 34 N.R. 384 — *followed*
Brown v. Canadian Imperial Bank of Commerce (1985), 50 O.R. (2d) 420, 37 R.P.R. 128 (H.C.) — *considered*
Canada (Attorney General) v. French (June 15, 1988), Doc. County of Grey 1746/84, Austin J. (Ont. H.C.), [1988] O.J. No. 736 — *applied*
Canada Trustco Mortgage Co. v. Wenngatz Construction & Holdings Ltd. (1986), 60 C.B.R. (N.S.) 270, 1 B.C.L.R. (2d) 302 — *referred to*
Ernst Brothers Co. v. Canada Permanent Mortgage Corp. (1920), 47 O.L.R. 362 (H.C.) [affirmed (1920), 48 O.L.R. 407, 57 D.L.R. 500 (C.A.)] — *considered*
Peter v. Beblow, [1993] 1 S.C.R. 980, [1993] 3 W.W.R. 337, 77 B.C.L.R. (2d) 1, 44 R.F.L. (3d) 329, 48 E.T.R. 1, 150 N.R. 1, 23 B.C.A.C. 81, 39 W.A.C. 81, 101 D.L.R. (4th) 621 — *referred to*
Petrie v. Petrie, [1944] S.C.R. 246, [1944] 2 D.L.R. 609 — *referred to*
Power v. Grace, [1932] O.R. 357, [1932] 2 D.L.R. 793 (C.A.) — *considered*
Rathwell v. Rathwell, [1978] 2 S.C.R. 436, [1978] 2 W.W.R. 101, 1 E.T.R. 307, 1 R.F.L. (2d) 1, 83 D.L.R. (3d) 289 — *referred to*
Royal Bank of Canada v. Harowitz (1994), 17 O.R. (3d) 671 (Gen. Div.) — *applied*
Victor Investment Corp. v. Fidelity Trust Co. (1974), [1975] 1 S.C.R. 251, 41 D.L.R. (3d) 65 — *referred to*
Williamson v. Loonstra (1973), 34 D.L.R. (3d) 275 (B.C. S.C.) *considered*

Statutes considered:

Court Order Enforcement Act, R.S.B.C. 1979, c. 75 —

s. 79(2)

Execution Act, R.S.O. 1990, c. E.24 —

s. 10

Application by creditors of bankrupt for orders declaring that creditors entitled to marshal certain of their claims, that creditors entitled to assignment of certain mortgage, that certain money would be available to them to satisfy debts owed to them or, in the alternative, that certain property subject to constructive trust.

Ground J.:

1 This is an application by certain creditors of Rosswell Myles Allison ("Allison"), a bankrupt, for:

1. An order declaring that the creditors of Allison are entitled to marshal their claims against part of Lot 16, Concession 2, Township of Vespra, County of Simcoe, being the lands and premises formerly owned by Allison ("Parcel A2") and that the first mortgagee, Diane Tomas, in Trust, who held a first mortgage on Parcel A2 and a first mortgage, securing the same indebtedness, on the balance of Lot 16, Concession 2, Township of Vespra, County of Simcoe, ("Parcel A1"), being lands and premises registered in the name of Mary Teeter Allison, the wife of Allison ("Mrs. Allison"), shall have recourse first to Parcel A1 before recourse to Parcel A2.

2. An order declaring that, as Parcel A2 has been sold, the applicants shall be entitled to an assignment of the mortgage to Diane Tomas, in Trust, on Parcel A1 subject to the payment to Diane Tomas, in Trust, of the sum of \$1,632.97, being the balance remaining payable, following the application of the proceeds of the sale of Parcel A2, on the mortgages to Diane Tomas, in Trust, together with accrued interest.

3. An order declaring that an amount equal to the net proceeds received from the sale of Parcel A2 shall be available to the creditors of Allison, from Parcel A1, to satisfy the debts owed by Allison to them.

4. In the alternative, an order declaring that Mrs. Allison has been unjustly enriched by the sale of Parcel A2 to the detriment of Allison's creditors and that Parcel A1 is subject to a constructive trust to the extent that the net proceeds received on the sale of Parcel A2 were applied toward the repayment of the Tomas mortgages.

2 The motion is responded to only by Mrs. Allison who seeks to have the motion dismissed.

Factual Background

3 Allison is an architect and was awarded by Delcan Corporation ("Delcan") the design contract for the messes and dining hall to be constructed at the Meaford Tank Range of the Department of National Defence (the "Meaford Project").

4 To undertake the Meaford Project, Allison engaged sub-consultants. In particular, Allison engaged 807933 Ontario Inc., carrying on business as 1516 Engineering ("1516 Engineering") to provide electrical and mechanical engineering services and Henderson, Paddon & Associates Limited ("HPA") to provide structural engineering work and assistance with the preparation of architectural specifications.

5 Allison defaulted in the payment of the invoices of HPA and 1516 Engineering as well as those of other sub-consultants.

6 The default in payment of invoices submitted by the applicants occurred in respect of the eighth invoice submitted by Allison to Delcan. The invoice was dated April 16, 1992, and was for a total amount of \$106,477.55. Delcan paid \$104,784.56 on account of this invoice to Allison on June 23, 1992. There was a shortfall of \$1,692.99. Allison did not pay the sub-consultants the money due them for their work done up to and including the date of the eighth invoice.

7 Allison maintained one blended personal and professional bank account at the Royal Bank of Canada in Barrie. Allison paid numerous personal and household expenses from this account.

8 Allison made an assignment in bankruptcy on April 5, 1994. Effectively, Allison's only asset at the time of his bankruptcy was Parcel A2.

9 Mrs. Allison had acquired all of Lot 16, Concession 2, Township of Vespra, County of Simcoe, by Instrument No. 214596 on December 15, 1965. Mrs. Allison obtained a severance of her property and conveyed Parcel A2 which consisted of 19.7 hectares (48.6 acres) of vacant land to Allison for \$1 on March 8, 1978. The lands retained by Mrs. Allison, Parcel A1, contain approximately 23.3 hectares (57.5 acres) and the residence occupied by Allison and Mrs. Allison.

10 Between March 1, 1978 and April, 1994, the two parcels were charged or mortgaged jointly under the same instrument seven times and collaterally once. In each of such mortgages, both Allison and Mrs. Allison jointly covenanted to be liable for

the monies due under each mortgage; Mrs. Allison as principal debtor on Parcel A1 and guarantor on Parcel A2, and Allison as principal debtor on Parcel A2 and guarantor on Parcel A1.

11 By Instrument No. 01194698 registered on July 30, 1992, Allison mortgaged Parcel A2 to Diane Tomas, in trust for \$185,000. By Instrument No. 01194699 registered on July 30, 1992, Mrs. Allison mortgaged Parcel A1 to Diane Tomas, in trust for \$185,000. These mortgages were cross-guaranteed.

12 Mortgage Instrument No. 0119468 provides inter alia as follows:

This mortgage ("Prime Mortgage") is secured by a collateral mortgage dated the 21st day of July, 1992 affecting premises being Parts 1, 2 and 3, Plan 51R-6781, Township of Vespra, County of Simcoe, ("Collateral Mortgage"). The parties acknowledge that a payment on account of this mortgage shall be a payment on account of the Collateral Mortgage and a payment on account of the Collateral Mortgage shall be considered as a payment on account of this mortgage.

13 Allison entered into an agreement of purchase and sale respecting the sale of Parcel A2 to Bryn Styles for an amount of \$200,000. This agreement of purchase and sale was confirmed by Paddon & Associates Inc., Trustee in Bankruptcy for Allison and the transaction was ultimately completed on July 22, 1994.

14 The mortgages to Diane Tomas, in trust, were substantially paid off (the outstanding balance as of July 22, 1994 being \$1,632.97) from the net proceeds from the sale of Parcel A2 in the amount of \$182,500.

Issues

15 The following issues would appear to be raised by this motion.

1. Can the creditors of Allison invoke the doctrine of marshalling?
2. In the event that marshalling may be invoked by the creditors of Allison, as the assets of Allison have been sold, may the creditors look to the mortgage on Parcel A1, which has been assigned by Diane Tomas in trust to the Trustee, and to Parcel A1 as security for the monies owed them by Allison?
3. Has Mrs. Allison been unjustly enriched and should a constructive trust be imposed on Mrs. Allison with respect to Parcel A1?
4. In the event the doctrine of marshalling is not applicable, should the mortgage indebtedness be apportioned between Parcel A1 and Parcel A2?

Submissions

16 Counsel for the applicants submit that the doctrine of marshalling ought to apply in this case. Counsel states that the doctrine requires that, if creditor X has two funds to which he or she can look to to satisfy his or her claim, i.e. fund A and fund B, while creditor Y can only resort to one of them, i.e. fund A, the doctrine of marshalling will require that creditor X will not first resort to fund A, but satisfy the debt first out of fund B and only resort to fund A if there is a deficiency. In addition, if creditor X has already been paid out of fund A the doctrine allows creditor Y to be subrogated to creditor X's position. They submit that, accordingly, the applicants ought to be subrogated to the position of Diane Tomas against Parcel A1 in that when, as here, a secured creditor with a first charge has satisfied its claim out of one of two funds, being the only fund against which unsecured creditors had a claim, the unsecured creditors are entitled to be subrogated to the position of the secured creditor against the second fund. Counsel contends that, in this situation, unsecured creditors can avail themselves of the doctrine of marshalling, and that the doctrine will be applied if it does not prejudice subsequent secured creditors or third parties.

17 In this situation there are no subsequent secured creditors and the only party to be prejudiced by the subrogation would be Mrs. Allison who, it is submitted, is not a third party in that she was a debtor, either directly or by guarantee, on both mortgages,

and accordingly, Allison and Mrs. Allison are each joint debtors in respect of each mortgage as required for the principle of marshalling to apply.

18 With respect to unjust enrichment, counsel for the applicants submit that Mrs. Allison has been unjustly enriched from the proceeds of Delcan cheques deposited to Allison's bank account to the extent of \$17,900 paid out to Mrs. Allison, and to the extent of \$25,000 paid to settle litigation regarding both properties, in addition to the \$182,500 applied toward repayment of the mortgages to Diane Tomas in trust which were secured by Mrs. Allison's lands as well as Allison's lands. Counsel take the position that all elements of unjust enrichment are present in this case. Mrs. Allison has been enriched to such extent, there has been a corresponding deprivation to the applicants, and there is no juristic reason for the enrichment in that the relationship between spouses does not constitute a juristic reason for conferring a benefit to the deprivation of another party.

19 Finally, counsel for the applicants submit that, if the doctrine of marshalling does not apply, the burden of the mortgage debt should be apportioned between the two properties. They submit that, as the mortgage on Mrs. Allison's property was described as the primary mortgage, it is arguable that the mortgage debt ought to be apportioned entirely to Mrs. Allison's property or, in the alternative, that the mortgage debt ought to be apportioned between the two properties based on value. In this regard they submit that the value of Allison's property has been established at \$200,000 on the basis of the sale to the third party, and that Mrs. Allison's property has a value of at least \$275,000, and probably more, because of the existence of a substantial house on the property.

20 Counsel for Mrs. Allison submits that the principle of marshalling is not applicable in this situation in that unsecured creditors cannot take advantage of the principle, and the signing of judgment and filing of a writ of execution does not change the status of a creditor from unsecured to secured. He further submits that the principle does not apply when dealing with land, and particularly when the unsecured creditors were not looking to the land as, in any sense, "security" for the payment of their claims. He further submits that the doctrine of marshalling will not be applied if it prejudices a third party, and that Mrs. Allison is a third party vis-à-vis the relationship between the applicants and Allison which arises out of Allison's professional practice and Mrs. Allison would clearly be prejudiced if the mortgage on her property is assigned for the benefit of Allison's creditors.

21 With respect to unjust enrichment, counsel for Mrs. Allison submits that the monies paid out to Mrs. Allison may well have been applied toward household or common expenses, and there is no evidence that such monies were used for the exclusive benefit of Mrs. Allison. Similarly, the \$25,000 paid to settle the litigation expenses was for their joint benefit in that the litigation involved both Allison's property and Mrs. Allison's property. In addition, the mortgages to Tomas were put in place to consolidate earlier mortgage loans which were secured on both properties, and would have been repaid out of the proceeds of sale of either property and that there is therefore nothing unjust in the payment of the mortgage on Mrs. Allison's property out of the proceeds of sale of Allison's property.

22 With respect to apportionment, counsel for Mrs. Allison submits that it would not be equitable to apportion the total mortgage debt to Mrs. Allison's property, in that the mortgage on her property was undoubtedly described as the primary mortgage only because her property was of greater value and the matrimonial home was located on her property.

Reasons

23 I shall deal first with the application of the principle of marshalling. The first criteria for the application of the principle would appear to be satisfied in the case at bar; the mortgagee, Tomas, clearly had access to two properties from which the payment due under the mortgages could be satisfied, and has resorted only to Parcel A2, Allison's property, for the payment of the amount owing under the two mortgages.

24 In *Brown v. Canadian Imperial Bank of Commerce* (1985), 50 O.R. (2d) 420 (H.C.) [at p. 422], Southey J. quoted the description of the doctrine of marshalling in 16 Hals., 4th ed., as follows:

Where one claimant, A, has two funds, X and Y, to which he can resort for satisfaction of his claim, whether legal or equitable, and another claimant, B, can resort to only one of these funds, Y, equity interposes so as to secure that A shall not by resorting to Y disappoint B. Consequently, if the matter is under the court's control, A will be required in the first

place to satisfy himself out of X, and only to resort to Y in case of deficiency; and if A has already been paid out of Y, it will allow B to stand in his place as against X. This is known as the doctrine of marshalling, and is adopted in order to prevent one claimant depriving another claimant of his security. ...

25 The second criteria is that there must be a common debtor for the doctrine to be applicable. I am satisfied that in this situation, where there were cross-guarantees given on both mortgages and where the mortgages provided that the mortgagee could proceed directly against the guarantor without first exhausting the mortgagee's rights as against the mortgagor, both Allison and Mrs. Allison are common debtors with respect to both mortgages in that the mortgagee could have proceeded against either of them with respect to the claims under both mortgages.

26 It is clear from the decision in *Ernst Brothers Co. v. Canada Permanent Mortgage Corp.* (1920), 47 O.L.R. 362 (H.C.), that the doctrine of marshalling can apply in situations where there is a joint debt to one creditor and a second debt to another creditor which is given directly by one of the joint debtors and assigned by the other joint debtor. In that case Orde J. stated at pp. 368 and 369:

There are two estates mortgaged to the Canada Permanent for the one debt, for which Jeremiah McAsey is liable, not only directly by virtue of his covenant, but also as between himself and Frank by virtue of his agreement to assume Frank's share of the debt, and there is the second charge or mortgage in favour of the plaintiffs, upon only one of the estates — given, it is true, by Frank, but which Jeremiah has agreed to pay.

Does the fact that Jeremiah is not directly liable to the plaintiffs exclude the application of the doctrine? I am of the opinion that it does not. It must, of course, be almost universally the case that in the application of the doctrine there will be a single debtor and two creditors, and that in cases where there are two debtors the doctrine is inapplicable, not because there are two debtors but because it would be inequitable as between those debtors to marshal the securities. The illustration given in Story's Equity, sec. 632, makes this clear: "Supposing the case of a joint debt due to one creditor by two persons, and a second debt due by one of them to another creditor. In such a case if the joint creditor obtains a judgment against the joint debtors, and the second creditor obtains a subsequent judgment against his own several debtor, a Court of Equity will not compel the joint creditor to resort to the funds of one of the joint debtors so as to leave the second judgment in full force against the funds of the other several debtor." But the underlying principle involved is brought out in the next sentence of the same direction: "At least it will not do so unless it should appear that the debt, though joint in form, ought to be paid by one of the debtors only, or there should be some other supervening equity."

In other words, the real test is not whether or not the debts to the first and second mortgagees are owed to them by the same person, but whether or not, in working out the equities among the persons interested, the two debts ought to be paid by the same person. It is clear from the illustration given by Story that if as between the two joint debtors the debt owing by them jointly to the first creditor should in fact be paid by the one who is indebted to the second creditor, then the doctrine of marshalling would apply.

27 The question then becomes whether the doctrine of marshalling can be asserted by an unsecured creditor. It is clear that the applicants were initially unsecured creditors. Both applicants have, however, obtained judgment against Allison and have filed writs of execution. It is the position of counsel for the applicants that the effect of s. 10 of the *Execution Act*, R.S.O. 1990, c. E.24 (the "*Execution Act*") is that the filing of writs of execution gives the execution creditors the status of secured creditors.

28 The extent to which goods are bound by a writ of execution is set out in 17 Hals., 4th ed. at para.468 [footnotes omitted]:

The writ is said to "bind" the property in the goods of the judgment debtor in the bailiwick. When it is said that the goods, or the property in them, are "bound", what is meant is that the sheriff acquires a legal right to seize the goods. Notwithstanding the binding effect of the writ, the ownership continues in the judgment debtor until the sale, and he can legally, until seizure, deal with the goods himself or, until sale, pass the property to others. Any transfer or assignment of the goods after the date at which the binding power of the writ operates will (except in the cases of a purchaser in market overt or of a purchaser in good faith for value without notice) be subject to the sheriff's right to follow up and seize the goods under the writ.

29 In *Power v. Grace*, [1932] O.R. 357 (C.A.), it was held that the delivery of a writ of execution to the sheriff is not part of the execution and that, accordingly, the death of one joint tenant after delivery to, but before execution by, the sheriff of a writ of execution vests the property in the survivor free from the claim of the execution creditor. Grant J.A. stated at p. 362:

The effect of the authorities ... is ... that, until execution against the lands is actually commenced by advertisement ... or probably by an actual seizure upon the lands themselves ... there is no such effect wrought upon the title or interest of the joint-tenant (the judgment debtor) as will operate to sever the joint-tenancy.

30 Counsel for the applicants referred to *Bank of Nova Scotia v. Adriatic Development Ltd.* (1984), [1985] 2 W.W.R. 627 (B.C. S.C.). Unfortunately the case is of little assistance in interpreting the *Ontario Execution Act* as it is dealing with a very different piece of legislation: the then new sections of the British Columbia *Court Order Enforcement Act*, 1979. Section 79(2) of that Act states:

From the time of its registration the judgment forms a lien and charge on the land of the judgment debtor specified in the application ... in the same manner as if charged in writing by the judgment debtor under his hand and seal,

(a) to the extent of his beneficial interest in the land;

In interpreting that section, Murphy L.J.S.C. stated at p. 632 [emphasis in original]:

The effect of the above was to enlarge a judgment creditor's rights by giving him a charge against specific property. In the words of the statute, registration of the judgment "... forms a lien and charge on the *land* of the judgment debtor *specified* in the application ... to the extent of his beneficial interest in the *land* ..." In other words, registration of the judgment no longer attaches only to whatever beneficial interest a mortgagor may have after deducting all mortgages from the value of all of the lands in the name of the mortgagor. It attaches to the specific land against which it is registered and as such constitutes a charge against that particular land.

31 This decision has, in my view, little bearing on the *Ontario Execution Act* as our Act does not provide that the writ attaches to specific property until the writ is executed by the sheriff, thus leaving the creditor unsecured until actual execution. As our law stands, a writ filed, but not yet executed under the *Execution Act*, does not create a secured interest in any particular asset of the judgment debtor.

32 It then remains to consider whether unsecured creditors may assert the principle of marshalling. Counsel for the applicants have been unable to cite any clear authority for the proposition that an unsecured creditor or judgment creditor is entitled to invoke the doctrine of marshalling. By contrast, the decision of the British Columbia Supreme Court in *Williamson v. Loonstra* (1973), 34 D.L.R. (3d) 275, would appear to support the proposition that an unsecured creditor or judgment creditor may not invoke the doctrine. Ruttan J. stated at pp. 278-279:

The doctrine of marshalling has been succinctly and simply stated in the judgment of Mr. Justice Orde in these words (*Ernst Bros. Co. v. Canada Permanent Mortgage Corp.* (1920), 47 O.L.R. 362 at pp. 367-8):

The doctrine of marshalling, in its application to mortgages or charges upon two estates or funds, may be stated as follows: If the owner of two estates mortgages them both to one person, and then one of them to another, either with or without notice, the second mortgagee may insist that the debt of the first mortgagee shall be satisfied out of the estate not mortgaged to the second, so far as that will extend. This right is always subject to two important qualifications: first, that nothing will be done to interfere with the paramount right of the first mortgagee to pursue his remedy against either of the two estates; and, second, that the doctrine will not be applied to the prejudice of third parties ...

This dicta was repeated with approval by Mr. Justice Donohue in the case of *Victoria & Grey Trust Co. v. Brewer et al.* (1970), 14 D.L.R. (3d) 28 at p. 30, [1970] 3 O.R. 704.

Mr. Justice Orde underlined the end of his judgment to the effect that the doctrine will not be applied to the prejudice of third parties. However, the third party in that case was a mortgagee, thus a secured creditor of equal degree. The doctrine does not extend to all creditors of every degree, it does not apply in favour of an unsecured creditor and it does not apply in favour of a judgment creditor unless he has obtained a charge on the estate that he seeks to have marshalled in his favour. The judgment creditors in the present case claim only as against the remaining interest of the mortgagor. But the second mortgagee has a higher interest than that of the mortgagor. He claims against the property itself, while the mortgagor's claim is only to any residue that is left. The execution creditors take only the same right that remains to the mortgagor or prime debtor. In *Fisher and Lightwood's Law of Mortgages*, 7th ed. (1931), at p. 574, the learned authors, in discussing against whom the doctrine of marshalling is applied, has [sic] this to say:

... it does not apply in favour of unsecured creditors, or in favour of a judgment creditor; unless he has obtained a charge on the estate.

In the case of *Gray v. Stone and Funnell* (1894), 69 L.T.R. (N.S.) 282, it was stated that a judgment creditor cannot by his charging order get any more than the debtor could honestly give him. In his judgment at p. 285 Mr. Justice Romer said:

... an execution creditor is shown by the cases cited not to be in the same position as a purchaser or a mortgagee who has actually advanced money on the property, but he can only take the beneficial interest of the debtor in the property.

33 See also *Canada Trustco Mortgage v. Wenngatz Construction & Holdings Ltd.* (1986), 60 C.B.R. (N.S.) 270 (B.C. S.C.), where McEachern C.J.S.C., in dealing with the submission that the bankruptcy of the debtor precludes the operation of the marshalling principle, stated at p. 272:

This question was carefully considered in *Re Bread Man Inc.* (1978), 21 O.R. (2d) 59, (sub nom. *Re Bread Man Inc.; Re Maple Leaf Mills Ltd.*) 29 C.B.R. (N.S.) 58, 89 D.L.R. (3d) 599 (S.C.), where Saunders J. explained that the marshalling doctrine cannot interfere with the right of a first mortgagee to realize upon its security as it may be advised, but in such case equity resorts to the principle of subrogation to place the second mortgagee in the shoes of the first in order to do equity. But Saunders J. goes on to hold that the third parties who may not be prejudiced by the principle of marshalling do not include unsecured creditors of the debtor and this is supported by reference to the judgment of Ruttan J. in *Williamson v. Loonstra* (1973), 34 D.L.R. (3d) 275 (B.C. S.C.). ...

34 Accordingly, in the case at bar, I conclude that the applicants are not entitled to invoke the doctrine of marshalling to require that the mortgagee shall have recourse first to Mrs. Allison's lands or to obtain an entitlement of an assignment to them of the mortgage to Diane Tomas in trust on Mrs. Allison's lands, or a declaration that an amount equal to the net proceeds received from the sale of Allison's lands shall be available to the creditors of Allison from Mrs. Allison's lands.

35 Counsel for the applicants have taken the position that Mrs. Allison has been unjustly enriched by the sale of Parcel A2 and the application of the proceeds of such sale to the mortgages held by Tomas, and that accordingly Parcel A1 ought to be subject to a constructive trust to the extent of the net proceeds received on the sale of Parcel A2 which were applied toward the repayment of the mortgages held by Tomas. The elements of unjust enrichment are stated by Dickson J. in *Becker v. Pettkus* (198), 117 D.L.R. 257 (S.C.C.), at pp. 273 and 274, in reference to his earlier decision in *Rathwell v. Rathwell* (1978), 83 D.L.R. (3d) 289 (S.C.C.), as follows:

In *Rathwell* I ventured to suggest that there are three requirements to be satisfied before an unjust enrichment can be said to exist: an enrichment, a corresponding deprivation and absence of any juristic reason for the enrichment. This approach, it seems to me, is supported by general principles of equity that have been fashioned by the Courts for centuries, though, admittedly, not in the context of matrimonial property controversies.

36 In the case at bar, there is clearly an enrichment to Mrs. Allison by virtue of the fact that the mortgages were substantially paid off out of the proceeds of the sale of Allison's property, and there is a corresponding deprivation to the creditors of Allison

in that no proceeds of sale of Allison's property were available to the creditors after payment of the Tomas mortgage. The question then becomes whether there is an absence of any juristic reason for the enrichment.

37 This issue is considered by Killeen J. in the recent decision in *Royal Bank of Canada v. Harowitz* (1994), 17 O.R. (3d) 671 (Gen. Div.). In that case, the defendant lent money to Melnitzer, who was not a party to that action, the payment of which was secured by a promissory note. Upon the note's maturity, the defendant asked for full repayment of the note. Melnitzer complied by supplying a personal cheque from his account at the plaintiff bank for the entire amount. The cheque was dated July 2, 1991, and was debited to this account on July 10, 1991. Unbeknownst to the defendant, Melnitzer was having financial difficulties. Within a few weeks Melnitzer's assets were ordered frozen, a receiver was appointed, and Melnitzer was petitioned into bankruptcy.

38 The bank claimed that the defendant held the sum paid to her by Melnitzer shortly before his bankruptcy as its constructive trustee under the principle of unjust enrichment. Counsel for the bank attempted to raise an argument not unlike that raised in the case before this court: that the juristic reason justifying the receipt of the money must arise out of an obligation between the bank and the defendant. In this case, the contract was with Melnitzer and not the bank. Killeen J. held at p. 682:

It is ... absurd to suggest that, in other kinds of cases where an unjust enrichment is claimed, the juristic reason must always be tied irrevocably to the person who asserts the unjust enrichment.

39 Accordingly, in our case, the juristic reason need not be tied to the applicant creditors but it is sufficient if it arises out of a relationship between Allison and Mrs. Allison.

40 In *Peter v. Beblow*, [1993] 1 S.C.R. 980, McLachlin J., in dealing with the absence of juristic reason, stated as follows [at p. 990]:

It is at this stage that the court must consider whether the enrichment and detriment, morally neutral in themselves, are "unjust".

What matters should be considered in determining whether there is an absence of juristic reason for the enrichment? The test is flexible, and the factors to be considered may vary with the situation before the court. For example, different factors may be more relevant in a case like *Peel*, *supra*, at p. 803, a claim for unjust enrichment between different levels of government, than in a family case.

In every case, the fundamental concern is the legitimate expectation of the parties ...

41 In *Royal Bank of Canada v. Harowitz*, *supra*, Killeen J. stated at p. 684:

At the end of the day, the hallmark of a legitimate unjust enrichment claim is a clear showing that the enrichment of the defendant was truly "unjust" in the circumstances.

42 In our case the payments made to Mrs. Allison from Allison's bank account into which the Delcan cheques were deposited were a payment of \$25,000 to settle litigation relating to both Allison's property and Mrs. Allison's property, and payments totalling \$17,900 during the period May 19, 1992 to September 9, 1992. It is not clear for what purpose these latter payments were made although there is some suggestion that they may have been made for joint household and other expenses. It should also be kept in mind that these payments were made in 1992, whereas Allison's assignment in bankruptcy did not occur until April 5, 1994, and that the \$30,000 bequest received by Allison in April, 1992 was deposited into this account.

43 In addition, as submitted by counsel for Mrs. Allison, the mortgages to Tomas were put in place to consolidate earlier mortgage loans which had always been secured on both properties and would have been repaid out of the proceeds of sale of either property.

44 Considering all of these factors I am not satisfied that the enrichment of Mrs. Allison was truly unjust in the circumstances, or to find that Mrs. Allison has been unjustly enriched so as to subject Parcel A1 to a constructive trust for the benefit of the applicant creditors.

45 With regard to the submissions on apportionment, the authorities cited by counsel would all appear to deal with situations where two or more properties are held separately but are subject to one mortgage to secure a joint debt. In *Falconbridge on Mortgages*, 4th ed. at pp. 309-310, it is stated:

If two parcels of land belonging to the same person are mortgaged to secure payment of a single debt and the two parcels subsequently become severed in title, there arises the question whether the burden of the mortgage should be apportioned between the respective owners, or whether the owner of one of the parcels has the right, as between himself and the owner of the other parcel, to insist that the burden of the mortgage shall be thrown wholly upon the other parcel. The simplest situation is where the owner of two parcels, which are in fact subject to a common mortgage, conveys away one of the parcels and retains the other.

.....

As between the owner of two parcels subject to a mortgage and the person to whom he conveys one of the two parcels, the question whether the mortgage debt should be apportioned or not depends on the intention of the parties as manifested by the terms express or implied of the transaction between them.

46 In *Victor Investment Corp. v. Fidelity Trust Co.*, 41 D.L.R. (3d) 65 (S.C.C.), Laskin J. stated at p. 69:

Apportionment arises in relation to the first mortgage debt, and as between Fidelity and Victor, because, at the time of its maturity and enforcement, the two properties were in separate hands but subject to the one mortgage debt covering both of them. Proration of the debt according to the respective values of the two properties must follow in the absence of any stipulation that one of the properties would bear the burden or bear it primarily as between the two holders of the equities of redemption. ...

47 In *Petrie v. Petrie*, [1944] 2 D.L.R. 609, Kerwin J. stated at p. 612:

In the present case, if nothing appeared beyond the fact that Thomas, James and Kenneth executed a mortgage on their respective farms, in which mortgage they jointly and severally covenanted to pay the mortgage moneys, each of the mortgagors should pay one-third. ...

48 The case at bar is not one where a single mortgage instrument was executed by Allison and Mrs. Allison covering their two properties. The evidence would seem to support the conclusion that the mortgage debt was incurred for the benefit of both Allison and Mrs. Allison, and in fact was incurred in part to repay existing mortgages on the properties which were mortgaged jointly under the same instrument. Further, it appears to have been the intention of the parties that the two separate mortgages ultimately given to Diane Tomas in trust were, for all intents and purposes, to be treated as a single obligation.

49 I have not been cited, nor have I been able to find any authority for granting the remedy of apportionment where mortgages were placed on properties with separate titles and owners. The courts would appear to have taken a narrow view of the application of the remedies of apportionment and marshalling in keeping such remedies distinct. The initial ownership of the properties is important. In both cases a single debtor must have two pools of properties, and have given a single mortgage over both properties to a single creditor. For apportionment to arise, the debtor must convey away one of the properties, thus severing title, and creating a problem of how to apportion the mortgage between the two properties. For marshalling to arise, the issue is not one of conveyance: the key is that a second creditor, B, with security in only one property be protected from a first creditor, A, who has security in both properties, to the extent that A not be allowed to enforce its security against the property secured to B, when to do so would deny B its security and when A could readily satisfy its claim out of the property in which B has no interest.

50 Austin J. noted in *Canada (Attorney General) v. French*, [1988] O.J. No. 736 (Ont. H.C.) that counsel had failed to produce any cases where apportionment was awarded where the mortgages were placed on properties with separate titles and owners. *Canada (Attorney General) v. French*, supra, deals with similar issues to the case which is before the court. The facts in that case were as follows: The defendants, Mr. and Mrs. French, lived on a farm in Derby County owned by Mrs. French (the "Derby Property"). Mr. French and his father owed as joint tenants another farm in Sydenham County (the "Sydenham Property"). All three of the Frenches gave a single mortgage over both properties to Mr. Horton, a solicitor. Mrs. French subsequently borrowed money from a Mr. Rosenberg which she secured with a first mortgage on the Derby Property. To do this, she paid Mr. Horton a sum to discharge his mortgage on the Derby Property, taking an assignment of his mortgage at the same time.

51 During the same time period Revenue Canada had several executions filed with the local sheriff against Mr. French. The executions existed prior to the registration of the new mortgage, the assignment, and the discharge. Mr. French's father later died, and Mr. French commenced power of sale proceedings against the Sydenham Property. Revenue Canada brought an action to attack the validity of the mortgage. Counsel for Revenue Canada took the position that marshalling was not relevant, but that Revenue Canada could invoke the principle of apportionment or contribution, if the husband failed to assert his right to apportionment.

52 Austin J. notes that counsel did not provide any authority for the proposition that an execution creditor of a mortgagor has the right to assert the right to apportionment on behalf of a mortgagor. He stated at pp. 5-7:

Assuming, for the purposes of discussion only, that the plaintiff as an execution creditor is entitled to step into the shoes of the husband and to assert his rights, what are those rights? Presumably the husband would have to establish what the arrangement was when the Horton mortgage was entered into, in the sense of who was to pay for what. In addition, he would have to prove what arrangement, if any, was made when Horton was paid off and the mortgage to Rosenberg was put on the Derby title. It is conceivable that such evidence would lead to the conclusion that, as amongst the Frenchs, the burden of the Horton mortgage should have been placed entirely on one property or the other, or divided between the two in some manner. In the absence of such evidence, however, I do not see how I can reach any such conclusion.

The plaintiff argued that the onus was on Mrs. French to come forward and to adduce evidence as to the arrangement made when the Horton mortgage was put on and when it was taken off. It was argued that in the absence of evidence as to the intentions of the parties, the court was entitled to assume that the two properties were to bear the burden of the Horton mortgage either equally or in proportion to the respective values. *Petrie v. Petrie*, [1944] 2 D.L.R. 609, was cited as support for an equal division and *Vancouver Investment Corp. Ltd. v. Fidelity Trust Company* (1973), 41 D.L.R. (3d) 65, as authority for a division on the basis of relative values.

But here the plaintiff is in theory standing in the shoes of the husband. The husband should know the facts and should be in a position to establish the equities. There should be no need for him to rely on presumptions. But no such evidence was tendered.

There is no point in speculating whether the presumptions and conclusions suggested by the plaintiff could have been made and drawn if there had been no mortgage to Rosenberg. That is not the evidence in this case.

I am not satisfied that the plaintiff as a judgment creditor has the right to stand in the shoes of the husband and to exercise the husband's rights with respect to the Horton mortgage. Even if the plaintiff has such a right, he has not, on the evidence presented, made out any case for the intervention of the court by way of apportionment.

53 Applying these authorities to the case at bar, I must hold that the remedy of apportionment cannot be granted where the two mortgages were given by different owners on two pieces of property albeit to secure a single debt. Moreover, it would appear that the applicants as execution creditors of Allison are not entitled to assert the right of apportionment.

54 The application is dismissed. Counsel may speak to me or write to me regarding costs.

Application dismissed.

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TAB 8

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COURT OF APPEAL FOR ONTARIO

McMURTRY C.J.O., FINLAYSON and MOLDAVER J.J.A.

B E T W E E N :)
)
807933 ONTARIO INC. carrying on business)
as 1516 ENGINEERING and HENDERSON,)
PADDON & ASSOCIATES LIMITED)
)
(Appellant))
)
and)
)
PADDON AND ASSOCIATES, Trustee in)
Bankruptcy for Rosswell Myles Allison, a)
Bankrupt, SAM WARNOCK, DAVID)
DAWSON & ASSOCIATES LIMITED,)
CHERYL RUMBLE, DAWN THOMPSON,)
REVENUE CANADA and MARY TEETER)
ALLISON)
)
(Respondent))
)
)

Peter C. Card
for the appellant

William J. Leslie Q.C.
for the respondent Mary
Teeter Allison

Heard: February 12, 1998

FINLAYSON J.A.:

[1] 807933. Ontario Inc., carrying on business as 1516 Engineering, appeals the judgment of the Honourable Mr. Justice Ground of the Ontario Court (General Division) dismissing its action for certain relief directed towards the land of the respondent Mary Teeter Allison (“Mrs. Allison”).

[2] The appellant claims as a judgment creditor of the respondent R. Myles Allison, a Bankrupt (hereinafter "Mr. Allison"). In fact, since its default judgment was signed after the bankruptcy of Mr. Allison on April 5, 1994, the appellant has the status only of a creditor with a claim proven in the bankruptcy.

[3] The appellant brings the action that is the subject of this appeal pursuant to the order of Ground J. dated October 21, 1994 granting it leave under s. 38 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended, to:

- (a) pursue a claim of marshalling in respect of a mortgage granted by Rosswell Myles Allison, the Bankrupt, to Diane Tomas, in Trust;
- (b) pursue a claim in the alternative of unjust enrichment against Mary Teeter Allison.

[4] The bankruptcy of Mr. Allison arose out of the practice of his profession as an architect. He was the architectural sub-consultant to Delcan Corporation, the prime consultant for a dining hall and mess building at the Meaford Tank Range of the Department of National Defence (the "Meaford Project"). He received certain funds for this project from Delcan that he was to disburse to sub-consultants. He failed to do so. One of those sub-consultants was the appellant, which had been engaged to provide electrical and mechanical engineering services. The appellant maintains that Mr. Allison took some of these funds which he was to pay out for the benefit of the subcontractors on

the Meaford Project and co-mingled them with personal funds in a joint bank account for the benefit of himself and Mrs. Allison.

[5] In the judgment under appeal, Ground J. declined to give effect to the claim for marshalling of certain properties owned by Mr. and Mrs. Allison on the basis that the appellant was not a secured creditor. He dismissed the action against Mrs. Allison for unjust enrichment with respect to the above noted funds. In this court, the appellant attempted for the first time to advance a claim that the moneys in the joint bank account were held in trust for the benefit of sub-contractors on the Meaford Project under the provisions of Part II of the *Construction Lien Act*, R.S.O. 1990, c. C.30.

[6] The court did not call upon the respondent with respect to the dismissal of the claim for unjust enrichment. We were satisfied that the disposition of Ground J. was the correct one on the evidence before him. The court declined to consider the new claim under the *Construction Lien Act* because it was not raised in the court below.

Accordingly, the trial judge was not in a position to make the findings of fact that would be crucial to a determination of this issue. Further, the claim is beyond the scope of the order for leave to proceed of Ground J. dated October 21, 1994.

Issue

[7] The only remaining issue that need be addressed is then:

Does the doctrine of marshalling have application to the subject lands of Mr. and Mrs. Allison for the benefit of the appellant creditor and other creditors in its class?

Facts as they relate to marshalling

[8] In December of 1965, Mrs. Allison purchased a farm property and registered it in her own name. On March 8, 1978, she applied for and received the right to sever the said property into two parcels, Parcels A and B. She then conveyed Parcel B to her husband, Mr. Allison.

[9] Between March 1, 1978 and April 1994, Mr. and Mrs. Allison financed the severed parcels through a succession of seven mortgages. These were joint mortgages whereby in one instrument Mr. and Mrs. Allison charged or mortgaged both Parcels A and B and covenanted to pay to the mortgagee the full amount of the indebtedness with respect to both parcels. In July of 1992, the two Allisons decided to re-finance the two parcels by borrowing \$185,000 from Diane Tomas to discharge the existing mortgages on both parcels. In return for the loan, two separate instruments of charge or mortgage were entered into: one by Mrs. Allison with respect to Parcel A for \$185,000 in favor of Tomas and the other by Mr. Allison in the same amount to Tomas with respect to Parcel B. The proceeds of the loan of \$185,000, along with some other money, were used to pay off all prior encumbrancers on both parcels. The two instruments evidencing the first mortgages to Tomas were dated July 21, 1992 and registered simultaneously on July 30, 1992. The

instrument charging Parcel A was signed by Mrs. Allison as the primary debtor for the sum of \$185,000 with Mr. Allison as the guarantor thereof and the instrument charging Parcel B was signed by Mr. Allison as the primary debtor for the same \$185,000 with Mrs. Allison as the guarantor thereof.

[10] For the sake of completeness, the mortgage by Mrs. Allison on Parcel A alone contained the following clause:

Prime Mortgage

THIS MORTGAGE ("Prime Mortgage") is secured by a collateral mortgage dated the 21st day of July, 1992 effecting premises [Parcel B] ("Collateral Mortgage"). The parties acknowledge that a payment on account of this mortgage shall be a payment on account of the collateral mortgage and a payment on account of the Collateral Mortgage shall be considered as a payment on account of this mortgage.

[11] In March of 1994, Mr. Allison entered into an agreement of purchase and sale with one Bryn Styles to sell Parcel B for \$200,000. The amount realized on this sale would be sufficient to discharge the \$185,000 Tomas mortgage on both Parcels A and B, save for a shortfall of \$1,632.97. Prior to the date of closing, Mr. Allison made his assignment in bankruptcy. In order to complete the sale, an agreement was entered into among Paddon & Associates (Trustee in Bankruptcy), Mr. and Mrs. Allison, and Diane Tomas in Trust dated April 29, 1994. Following this agreement, the sale to Styles was closed. The mortgage, given by Mr. Allison on Parcel B in favour of Tomas and cross-

guaranteed by Mrs. Allison, was discharged to allow the sale of the property by the Trustee in Bankruptcy to Styles. The mortgage registered against Mrs. Allison's Parcel A was to remain in place but would be assigned to the Trustee in Bankruptcy until the issue of the applicability of marshalling was settled and, upon the resolution of that issue, any benefit from that mortgage would be subject to the claim for the shortfall of \$1,632.97 owed to Tomas.

Analysis

[12] In *Aldrich v. Cooper* (1803), 8 Ves. 381, Lord Eldon defined the principles upon which a court of equity will apply the doctrine of marshalling. The right to marshal securities is an equitable one intended to prevent a creditor who can resort to two funds from defeating another creditor who can resort to only one of them. Fundamentally, the doctrine is applied for the purpose of regulating the rights of the two creditors among themselves, though in so regulating their rights the court will never interfere with the paramount claim of the superior creditor (or one which has the choice of two funds upon which to collect) to pursue his or her remedy against either fund, but provides that if he or she resorts to the fund which the other creditor can alone resort, then the other creditor shall not be prejudiced. The doctrine is applicable unless some other equity prevents its application such as in the case where its application would prejudice third parties.

[13] As it applies to this case, there are two criteria that must be met before the doctrine of marshalling can be applied. The first criterion is that there must be a creditor or mortgagee who has access to two properties of a debtor to which he or she can resort for the payment of the amount owing. There is no issue that this criterion has been satisfied in this case. The second criterion is that there must be a creditor ranking behind or inferior to another creditor or mortgagee of a common debtor with a claim against only one of the properties available to the superior creditor or mortgagee. Such an inferior creditor can invoke the assistance of equity to cause or marshal the superior creditor or mortgagee to satisfy the mortgage debt from the property against which the inferior creditor has no recourse so that property will be available to the inferior creditor, or if this is impossible, or unfair to the superior creditor, equity may allow the inferior creditor to stand as the superior creditor in relation to the property against which the inferior creditor otherwise has no recourse.

[14] The key issue in the case on appeal is whether Mr. and Mrs. Allison were common debtors to the appellant. While it is conceded that they were common debtors to Tomas, it would appear to me on the facts of the case that only Mr. Allison was a debtor of the appellant and all the other creditors whose claims arose out of the Meaford Project. Mrs. Allison had nothing to do with those debts. If the court was to apply the doctrine of marshalling to Mrs. Allison's Parcel A so that Mr. Allison's Parcel B will be available to satisfy the appellant, then Mrs. Allison would be forced to pay her husband's debts for

which she is not in law obligated. Marshalling was not intended to create such an inequity between two debtors.

[15] Ground J. found that Mrs. and Mr. Allison were common debtors and therefore the second criterion for the applicability of the equitable doctrine of marshalling was satisfied. He stated:

The second criteria is that there must be a common debtor for the doctrine to be applicable. I am satisfied that in this situation, where there were cross-guarantees given on both mortgages and where the mortgages provided that the mortgagee could proceed directly against the guarantor without first exhausting the mortgagee's rights as against the mortgagor, both Allison and Mrs. Allison are common debtors with respect to both mortgages in that the mortgagee could have proceeded against either of them with respect to the claims under both mortgages.

[16] Ground J. then quoted at length the decision of Orde J. in *Ernst Bros. Co. v. Canada Permanent Mortgage Corporation* (1920), 47 O.L.R. 362, affirmed (1920), 48 O.L.R. 407 (C.A.), for the proposition that the "doctrine of marshalling can apply in situations where there is a joint debt to one creditor and a second debt to another creditor which is given directly by one of the joint debtors and assigned by the other joint debtor".

[17] However, *Ernst* is readily distinguishable from the facts of the present appeal. In *Ernst* the joint debtor of the first mortgage was assigned the second debt owed to the other creditor, and thereby created, in the equities among the persons interested, a reason for the two debts to be paid by the same person. In *Ernst*, Frank McAsey wished to buy

a lot of land from his mother's estate, but required his brother Jeremiah to pledge part of an adjoining lot he owned as security for a mortgage large enough to purchase the land. The brothers both executed a mortgage in favour of Canada Permanent Mortgage Corporation, and it was registered upon both lots. Both brothers also covenanted to repay the full amount of the mortgage. Frank later become indebted for the purchase of agricultural implements to the plaintiff, Ernst Bros. Co., and the debt was secured by a charge upon his lot. Orde J. found as a fact (which was not disturbed on appeal), at pp. 366-367, that Frank some years later had conveyed his lot to Jeremiah, and thereby Jeremiah had assumed both the Canada Permanent Mortgage Corporation first mortgage and the plaintiff's second charge.

[18] Orde J., at p. 366, made clear in his reasons, which were upheld on appeal, that the plaintiff's right to have the securities marshalled, if it existed at all, depended upon the plaintiff establishing that Jeremiah purchased the lot from Frank with the obligation to assume and pay off the Canada Permanent mortgage *and* the plaintiff's charge.

Furthermore, as quoted by Ground J. below, Orde J. stated at pp. 368-69:

There are two estates mortgaged to the Canada Permanent for the one debt, for which Jeremiah McAsey is liable, not only directly by virtue of his covenant, but also as between himself and Frank by virtue of his agreement to assume Frank's share of the debt, and there is the second charge or mortgage in favour of the plaintiffs, upon only one of the estates -- given, it is true, by Frank, *but which Jeremiah has agreed to pay.*

Does the fact that Jeremiah is not directly liable to the plaintiffs exclude the application of the doctrine? I am of the opinion that it does not. It must, of course, be almost universally the case that in the application of the doctrine there will be a single debtor and two creditors, and that in cases where there are two debtors the doctrine is inapplicable, *not because there are two debtors but because it would be inequitable as between those debtors to marshal the securities*. The illustration given in Story's Equity, sec. 642, makes this clear: "Supposing the case of a joint debt due to one creditor by two persons, and a second debt due by one of them to another creditor. In such a case if the joint creditor obtains a judgment against the joint debtors, and the second creditor obtains a subsequent judgment against his own several debtor, a Court of Equity will not compel the joint creditor to resort to the funds of one of the joint debtors so as to leave the second judgment in full force against the funds of the other several debtor." But the underlying principle involved is brought out in the next sentence of the same section: "At least it will not do so unless it should appear that the debt, though joint in form, ought to be paid by one of the debtors only, or there should be some other supervening equity."

In other words, the real test is not whether or not the debts to the first and second mortgagees are owed to them by the same person, but whether or not, in working out the equities among the persons interested, the two debts ought to be paid by the same person. It is clear from the illustrations given by Story that if as between the two joint debtors the debt owing by them jointly to the first creditor should in fact be paid by the one who is indebted to the second creditor, then the doctrine of marshalling would apply. [Emphasis added.]

[19] Orde J. cited the reasons of Lord Eldon in *Ex parte Kendall* (1811), 17 Ves. 514 in support of the proposition that there must be a common debtor for the equitable doctrine of marshalling to apply. In that case, five men had been in a partnership and had incurred

debts, one of the partners died, and the remaining four continued in partnership and also incurred debts, and then became bankrupt. In the bankruptcy proceedings, certain creditors, with claims against the four surviving partners only, sought to stay the payment of the dividend to those creditors who were creditors not only of the four surviving partners but also of the deceased partner, until payment had been recovered from the estate of the deceased partner. Lord Eldon, at p. 520, stated (and quoted by Orde J. at p. 369):

Another question is, whether, if this was a bill, filed by creditors of the four, they would have a right to insist upon the benefit, sought by this petition. We have gone to this length: if A. has a right to go upon two funds, and B. upon one, having both the same debtor, A. shall take payment from that fund, to which he can resort exclusively; that by those means of distribution both may be paid. That course takes place, where both are creditors of the same person; and have demands against funds, the property of the same person; and have demands against funds, the property of the same person. Here, it is true, there may be creditors, who have demands against the four, and others who have demands against the one: but it was never said, that, if I have a demand against A., and B., a creditor of A., shall compel me to go against A.; *without more*; as, if B. himself could insist, that A. ought to pay in the first instance; as in the ordinary case of drawer and acceptor, or principal and surety; to the intent, that all obligations arising out of these complicated relations, may be satisfied: but if I have a demand against both, the creditors of B. have no right to compel me to seek payment from A.; *if not founded on some equity, giving B. the right for his own sake to compel me to seek payment from A.* If therefore I had before me a case, in which it was clear, that the creditors of the five could go against the estate of Devaynes and the four, yet, if it was not also clear, that the latter could have turned those creditors against the other fund, it does not advance the

claim, that without such an arrangement they will get less. *Unless they can establish, that it is just and equitable, that Devaynes's estate should pay in the first instance, they have no equity to compel a man to go against that estate, who has resort to both funds.* [Emphasis added.]

[20] Orde J., at p. 370, concluded from the above quoted passage that:

It is clear from the qualification contained in the concluding sentence of the foregoing quotation from Lord Eldon's judgment that the sweeping statement which he made earlier, "where both are creditors of the same person," could not be intended to mean that in every case the debtor must in fact be personally liable to both creditors, but rather that, in working out the equities among those entitled, there must be but one person ultimately liable for the two debts, that is there must be one debtor and two creditors.

[21] Orde J. then cited the leading decision on marshalling by Lord Eldon in *Aldrich v. Cooper*, *supra*, and concluded, at p. 371, that "[i]t would be inequitable to permit the securities to be marshalled if in the result one who was not under any obligation to pay both debts should suffer."

[22] In the present appeal, Mrs. and Mr. Allison held a joint debt in the form of two mortgages on their respective parcels of land that were cross-guaranteed much like the mortgage to Canada Permanent the McAsey brothers held in *Ernst*. Unlike in *Ernst*, however, where Jeremiah McAsey was assigned the debt of Frank McAsey to Ernst Bros. Co. because Jeremiah bought Frank's lot, in the present appeal, Mrs. Allison never was assigned or otherwise obligated towards the debt owed by Mr. Allison to the appellant. Mrs. and Mr. Allison were common debtors to Tomas (as Ground J. found), but they were

not common debtors with respect to the debt owed by Mr. Allison to the appellant. Mrs. Allison was not under any obligation to pay both debts, and therefore should not suffer, especially at the hands of an equitable doctrine. Unless the appellant can establish, that it is just and equitable that Mrs. Allison should pay in the first instance, it has no equity to compel a person such as Tomas, who has resort to both funds, to go against Mrs. Allison's parcel of land.

[23] Counsel for the appellant referred the court to a number of decisions at the trial level where, as in *Ernst*, the court did find that in special circumstances, equity would prevail to apply the doctrine of marshalling where there was not but a single debtor. These cases are distinguishable from the present appeal for the same reasons *Ernst* was distinguished above. The trial decisions rely upon an exception to the general rule that there must be a single debtor for marshalling to apply that was applied in *Ernst* and is explained in *Halsbury's Laws of England*, vol. 16, 4th ed., (1980) at 786, para. 877:

Generally, three conditions must be satisfied in order that the doctrine of marshalling may be applied as regards claims by creditors:

- (1) The claim must be against a single debtor; if one creditor has a claim against C and D, and another creditor has a claim against D only, the latter creditor may not require the former to resort to C unless the liability is such that D could throw the primary liability on C, for example where C and D are principal and surety;

[24] Thus in *Brown v. Canadian Imperial Bank of Commerce* (1985), 50 O.R. (2d) 420 (H.C.J.), Southey J. found that marshalling did apply to a situation where there was no single common debtor but there were two debtors that were in effect common since they were in a surety-principal relationship, i.e. the debtor facing the claims of two creditors was in effect a creditor of the second debtor. Again in *G. Ruso Construction Ltd. v. Laviola et al.*, a decision of Haines J. of the Supreme Court of Ontario, released May 6, 1976, and reported at (1979) 27 Chitty's L.J. 136, the fact situation is very similar to the present appeal: a joint mortgage was held on two parcels of land owned by different people and there was a subsequent charge by an inferior creditor to one of the parcels. Haines J., in considering much of the case law discussed here, concluded, at p. 139, that for marshalling to apply there must be a relationship or equities between the two debtors such that one debtor is entitled to require the other to be primarily liable to either of the creditors.

[25] As indicated above, in this case Ground J. found that there was but one debtor in the circumstances of the cross-guarantees. But this merely made the two Allisons liable for the same debt to Tomas. There is nothing in the two guarantees that permits Mr. Allison to claim over against Mrs. Allison with respect to debts he incurred on the Meaford Project. In fact, he cannot claim over against Mrs. Allison on the Tomas mortgage because both are principals of the same debt as well as being guarantors.

[26] With respect, I am unable to agree with the trial judge on his preliminary finding.

In my opinion, he should have found that the doctrine of marshalling had no application

to the facts of this case because the appellant's claim was against a single creditor,

namely Mr. Allison. As noted, he did find that the doctrine did not apply because the

appellant was not a secured creditor. In view of my finding on the primary point, I do not

propose to deal with this issue.

[27] For the reasons outlined above, I would dismiss the appeal with costs.

*I agree with the trial judge.
I agree with the majority of the
I agree with the majority of the*

Released: *ABN*

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TAB 9

WILLIAMSON v. LOONSTRA et al.

*British Columbia Supreme Court, Ruttan, J., in Chambers.
February 26, 1973.*

C. M. Jeffery, for defendant, applicant, Herbert William Lavallee.

O. P. L. Staplin, for defendant, Mid-Valley Lumber Ltd.

Gaynor Smith, for defendant, Shillinglaw.

A. McEwen, for defendant, Hendry.

RUTTAN, J.:—The defendants other than R. and L. Loonstra, come before me again pursuant to the order already made herein on September 13, 1972, for directions on the priority of distribution of the funds left in Court after payment and discharge of the first mortgage to the plaintiff Williamson.

At the time of the original order *nisi* there was a direction for sale of the lots registered in the names of the defendants, R. and L. Loonstra, the conduct of that sale to be in the hands of the defendant Lavallee, second mortgagee of that part of the lands covered by Lot 159. The proceeds from the sale of those lots were as follows:

PROCEEDS FROM SALE OF LOTS	
155 & 156	9,869.61
154 & 157	9,975.09
158	4,984.47
*159	9,065.85
163	4,432.95
168	4,987.96
170	4,984.47
151, 152, 160, 171 & 172	24,565.73
TOTAL	\$72,866.13
LESS AMOUNT PAID TO PLAINTIFF	55,948.42
	\$16,917.71
*THE PROCEEDS FROM LOT 159 ARE	
12.44% OF THE TOTAL	
THE BALANCE IN COURT IS \$16,917.71	
AND 12.44% OF THIS TOTAL IS \$2,104.56	

From the state of the title it is apparent there were a substantial number of mechanics' liens filed against Lots 159 and 160.

One judgment in the name of Hendry for \$4,188.60 was registered against all the interest of both Loonstras on June 9, 1971. The Lavallee second mortgage in the amount of \$15,000 taken out against both Loonstras on Lot 159, was filed on June 11, 1971. In addition, a number of judgments were all filed after the first mortgagee as plaintiff had filed his *lis pendens* on July 12, 1971, and after the granting of the order *nisi* to him on August 24, 1971.

One of the original mechanics' lien claimants was Mid-Valley Lumber Ltd., which filed a lien for \$2,178.31 against Ruby Loonstra on Lot 159 on June 9, 1971. Another early lien claimant was the firm of Isaaks and Duperron who filed separate liens, one against Ruby Loonstra on Lot 159 and the other against Ruby Loonstra on Lot 160, both on June 25, 1971.

Appearing on behalf of mechanics' lien claimants, Mr. Staplin admitted that none of the claimants had processed their claims by proceeding to Court action within one year as required by ss. 26 and 27 of the *Mechanics' Lien Act*, R.S.B.C. 1960, c. 238. Mr. Staplin's submission was that these liens were wiped out in any event because of the foreclosure and sale by the first mortgagee before the year expired. He submitted they did not have to commence action because it would have certainly failed with the disappearance of the land which was the subject-matter of their actions.

It does not necessarily follow their right to lien would expire since they could possibly have transferred the right to any fund that might represent the residue from the sale of such lots. However, the lien itself creates no right as a credit unless it is proceeded with to action. The lienholder must pursue his remedy under the statute outside the foreclosure action to establish his right and priority. This principle is established and the requisite authorities examined in the 3rd edition (1972) of Macklem and Bristow, *Mechanics' Liens in Canada*, at p. 211 *et seq.* Not having commenced actions on their liens, the lien claimants are not now entitled to any priority in this present distribution, and can claim only as general creditors against the Loonstras.

The judgment creditor Hendry, secured his claim on all the properties before the second mortgage for Lavallee was registered against Lot 159. It is not disputed Hendry is entitled to priority over all other creditors, including Lavallee, and to have his claim paid out of the funds in Court.

However, Lavellee submits that the doctrine of marshalling applies so that the payments made both to Williamson, the

first mortgagee, and Hendry, the first judgment creditor, be deemed taken from those funds representing the lots other than Lot 159, *i.e.*, the lot available for payment of Lavallee's claim.

The remaining judgment creditors dispute this right of marshalling on behalf of Lavallee, submitting they are entitled to claim at least equally with him after payment of the first encumbrance. They submit that from the net proceeds of the sale of all the lots after payment of the first mortgage, the remainder is available first to pay the Hendry claim and the balance remaining as a total fund for distribution rateably between all judgment creditors. With respect to Lot 159 they refer to the statement (above) which indicates that the portion of the fund that can be assigned to Lot 159 is only 12.44% or \$2,104.56. If Lavallee is entitled to any priority they submit it does not exceed this sum.

The judgment creditors further submit that Lavallee did not proceed to judgment in the original foreclosure action, and is therefore to be classed only as the general creditor who has not proved his claim and so is not entitled even to share with the other judgment creditors in this distribution.

The doctrine of marshalling has been succinctly and simply stated in the judgment of Mr. Justice Orde in these words (*Ernst Bros. Co. v. Canada Permanent Mortgage Corp.* (1920), 47 O.L.R. 362 at pp. 367-8) :

The doctrine of marshalling, in its application to mortgages or charges upon two estates or funds, may be stated as follows: If the owner of two estates mortgages them both to one person, and then one of them to another, either with or without notice, the second mortgagee may insist that the debt of the first mortgagee shall be satisfied out of the estate not mortgaged to the second, so far as that will extend. This right is always subject to two important qualifications: first, that nothing will be done to interfere with the paramount right of the first mortgagee to pursue his remedy against either of the two estates; and, second, that the doctrine will not be applied to the prejudice of third parties...

This dicta was repeated with approval by Mr. Justice Donohue in the case of *Victoria & Grey Trust Co. v. Brewer et al.* (1970), 14 D.L.R. (3d) 28 at p. 30, [1970] 3 O.R. 704.

Mr. Justice Orde underlined the end of his judgment to the effect that the doctrine will not be applied to the prejudice of third parties. However, the third party in that case was a mortgagee, thus a secured creditor of equal degree. The doctrine does not extend to all creditors of every degree, it does not apply in favour of an unsecured creditor and it does not apply in favour of a judgment creditor unless he has obtained

a charge on the estate that he seeks to have marshalled in his favour. The judgment creditors in the present case claim only as against the remaining interest of the mortgagor. But the second mortgagee has a higher interest than that of the mortgagor. He claims against the property itself, while the mortgagor's claim is only to any residue that is left. The execution creditors take only the same right that remains to the mortgagor or prime debtor. In *Fisher and Lightwood's Law of Mortgages*, 7th ed. (1931), at p. 574, the learned authors, in discussing against whom the doctrine of marshalling is applied, has this to say:

... it does not apply in favour of unsecured creditors, or in favour of a judgment creditor; unless he has obtained a charge on the estate.

In the case of *Gray v. Stone and Funnell* (1894), 69 L.T.R. (N.S.) 282, it was stated that a judgment creditor cannot by his charging order get any more than the debtor could honestly give him. In his judgment at p. 285 Mr. Justice Romer said:

... an execution creditor is shown by the cases cited not to be in the same position as a purchaser or a mortgagee who has actually advanced money on the property, but he can only take the beneficial interest of the debtor in the property.

See also the decision of Mr. Justice Beck in *Edmonton Mortgage Co. v. Gross* (1911), 3 Alta. L.R. 500 at p. 501, 18 W.L.R. 385:

A mortgage is a specific charge against specific property, which, under certain circumstances, may give rights to the mortgagee in excess of the beneficial rights of the mortgagor. An execution attaches only to the beneficial interest of the execution debtor . . . "nor did the Court ever presume to enlarge a judgment creditor's rights" . . .

In applying the doctrine of marshalling here I direct that the Hendry claim be paid out of those moneys, totalling \$7,851.56 representing the residue of proceeds from the sale of all lots save and except Lot 159 after discharge of the mortgage interest of Williamson. The residue of approximately \$3,000 will be available for distribution among the judgment creditors.

The second mortgage claim of Lavallee is to be charged against the sum of \$9,065.55 representing the sale proceeds of Lot 159. For the balance of his claim, Lavallee will rank as a personal judgment creditor of the defendants Loonstra and will share *pari passu* with the other judgment creditors in the residue.

With respect to the submission that Lavallee is not entitled to rank since he did not proceed to judgment on his mortgage at the time of the first foreclosure, I agree with Mr. Jeffery that his claim has been sufficiently proved when he came in as a defendant in the original action and undertook on behalf of all parties the conduct of the sale of the properties for the purpose of liquidating and distributing the claims.

Lavallee as mortgagee has both a charge against the property and a personal claim against the defendants Loonstra. In the circumstances of the foreclosure and sale he was not required to elect whether to sue them on the personal covenant or to proceed to judgment on his mortgage. His position was preserved so that if the proceeds from Lot 159 are sufficient to pay out his mortgage, he was entitled to confine his claim to that property. If the proceeds are not sufficient, he is entitled to share with the other judgment creditors for the deficiency. His claim was established and crystallized by the accounting which took place before the registrar. Having undertaken the conduct of the proceedings on behalf of all creditors with the consent of them all, his claim was crystallized and preserved and it cannot now be argued he did not establish his right to judgment.

The matter of costs was not spoken to on this application, but since all parties came before me to ask for directions as to the priority of distribution, I feel that they all should be entitled to have their costs on a party-and-party basis paid out of the fund in Court. I will however, hear counsel on this issue if they wish to come before me.

Order accordingly.

TAB 10

T-2416-97

The Governor and Company of the Bank of Scotland (Plaintiff)

v.

The Owners and All Others Interested in the Ship *Nel* and Ocean Profile Maritime Limited (Defendants)**INDEXED AS: GOVERNOR AND COMPANY OF THE BANK OF SCOTLAND v. NEL (THE) (T.D.)**

Trial Division, Hargrave P.—Vancouver and Montréal (teleconference), May 27 and June 25; Vancouver, July 2, 1998.

Maritime law — Creditors and debtors — Motion by necessities supplier to compel production of documents showing any collateral benefits obtained by mortgagee for which should account, making more funds available to lien claimants — Procedure preliminary to determination of priorities to proceeds of judicial sale of ship — Bank's claim as mortgagee will substantially exhaust sale proceeds — Documents relevant if necessities claimants, holding only statutory rights in rem, able to require Bank to marshal — Marshalling equitable right whereby Court ordering creditor, having secured right on more than one res or fund belonging to debtor, or security from two or more debtors for same debt, to exercise right on security in manner in best interests of all creditors — Formerly, unsecured creditors had right to benefit of marshalling — Overlooked in recent Canadian cases concerned with in personam right of creditors — Those cases limited to facts, not to be followed as contrary to equitable doctrine of marshalling — Production of commitment letter ordered.

Equity — Doctrine of marshalling — As between mortgagee, creditor — Priorities to proceeds of judicial sale of ship — Authoritative definitions of marshalling referred to — Whether unsecured creditors have benefit of marshalling — Equity engineered redress of marshalling so that no man made rich by another's injury — Canadian case law limiting availability of marshalling to be departed from to uphold obvious legal principles.

T-2416-97

The Governor and Company of the Bank of Scotland (demanderesse)

c.

Les propriétaires et toutes les autres personnes ayant un droit sur le navire *Nel* et Ocean Profile Maritime Limited (défendeurs)**RÉPERTORIÉ: GOVERNOR AND COMPANY OF THE BANK OF SCOTLAND c. NEL (LE) (1^{re} INST.)**

Section de première instance, protonotaire Hargrave—Vancouver et Montréal (téléconférence), 27 mai et 25 juin; Vancouver, 2 juillet 1998.

Droit maritime — Créanciers et débiteurs — Requête présentée par un fournisseur d'approvisionnements nécessaires sollicitant la production de documents démontrant que la créancière hypothécaire a reçu des avantages accessoires dont elle doit rendre compte, ce qui dégagerait plus de fonds pour les titulaires de privilèges — Procédure préliminaire à l'établissement de l'ordre de priorité pour la répartition du produit de la vente judiciaire du navire — La réclamation de la Banque, créancière hypothécaire, épuiserait en grande partie le produit de la vente — Les documents sont pertinents si les fournisseurs d'approvisionnements nécessaires, titulaires uniquement de droits réels, peuvent obliger la Banque à procéder à une collocation en equity — La collocation est un mécanisme reconnu en equity par lequel le tribunal ordonne au créancier qui possède un droit garanti sur plusieurs choses ou sur plusieurs fonds appartenant au débiteur, ou la garantie de deux ou de plusieurs débiteurs pour la même créance, d'exercer son droit sur la garantie de la manière qui favorise le mieux les intérêts de la masse des créanciers — À l'origine, les créanciers chirographaires avaient droit à la collocation en equity — Les causes canadiennes récentes portant sur les droits personnels des créanciers n'en ont pas tenu compte — Cette jurisprudence se limite aux faits en cause dans chaque cas et ne doit pas être suivie parce qu'elle est contraire à la doctrine de la collocation en equity — La production de la lettre d'engagement a été ordonnée.

Equity — Doctrine de la collocation en equity — Entre la créancière hypothécaire et l'autre créancière — Ordre de priorité pour la répartition du produit de la vente judiciaire — Mention des définitions de la collocation en equity qui font autorité — Les créanciers chirographaires peuvent-ils se prévaloir de la collocation en equity? — L'equity a conçu la collocation en equity comme réparation afin d'empêcher qu'une personne s'enrichisse en lésant autrui — Il faut déroger à la jurisprudence canadienne, qui a limité l'accès

This was a motion by a necessities supplier for production of documents on which the plaintiff's nominee might be cross-examined during the procedure leading up to a determination of priorities to the proceeds of the judicial sale of the *Nel*. The plaintiff mortgagee will be looking to the sale proceeds to satisfy its claim. If it holds a priority coming after the marshal's sale costs, its claims will substantially exhaust the sale proceeds. Alpha Bunkering wishes to cross-examine the Bank's nominee to determine whether the Bank obtained any collateral benefit as lender to the new owners of the *Nel*, for which it should account thus making more funds available to the lien claimants. Such information is relevant only if the necessities claimants do not have maritime liens ranking ahead of the Bank, but are able to require the Bank to marshal. Marshalling is an equitable process whereby the Marshall or the court orders a creditor who has a secured right on more than one *res* or fund belonging to the debtor, or security from two or more debtors for the same debt, to exercise his right on the security in a manner which will be in the best interests of all creditors.

The issue was whether an unsecured creditor is able to rely on the doctrine of marshalling.

Held, the motion should be allowed.

Equity engineered the redress of marshalling as an application of the maxim that no man ought to be made rich out of another's injury. Under Canadian law, necessities suppliers with mere rights *in rem* are in the same position as unsecured creditors. The plaintiff referred to various cases for the proposition that unsecured creditors cannot avail themselves of the doctrine of marshalling. In England, marshalling applies to cases of double security generally to afford equitable redress. While English cases and authorities which treat marshalling as a broad equitable concept to give relief where needed, including to mere holders of oral and written contracts, are not binding on the Federal Court, they are persuasive. The early cases setting out the scope of the doctrine of marshalling do not suggest that it is not available to ordinary contractual creditors. Indeed, the opposite is true. In the past, unsecured creditors always had a right to the benefit of marshalling. Yet some Canadian courts, in certain circumstances, seem to have limited the availability of this remedy, departing from equitable concepts by specifically denying it to ordinary creditors, but without any real reason. The doctrine of *stare decisis* notwithstanding, current

sibilité à la collocation en equity, pour donner effet à des principes de droit évidents.

Il s'agit d'une requête présentée par un fournisseur d'approvisionnements nécessaires en vue de la production de documents à l'égard desquels le représentant de la demanderesse pourrait être contre-interrogé au cours de la procédure à l'issue de laquelle sera établi l'ordre de priorité pour la répartition du produit de la vente judiciaire du *Nel*. La créancière hypothécaire demanderesse s'intéresse au produit de la vente pour obtenir le remboursement de sa créance. Si sa créance prend rang immédiatement après celle du prévôt relativement aux frais de la vente, elle épuiserait en grande partie le produit de la vente. Alpha Bunkering veut contre-interroger le représentant de la Banque afin de vérifier si la Banque a pu obtenir un avantage accessoire en consentant un prêt à la nouvelle propriétaire du *Nel*, dont elle devrait rendre compte, ce qui dégagerait plus de fonds pour les titulaires de privilèges. Ces renseignements ne sont pertinents que si les fournisseurs d'approvisionnements nécessaires ne sont pas titulaires de privilèges maritimes prenant rang avant la Banque, mais peuvent obliger la Banque à procéder à une collocation en *equity*. La collocation est un mécanisme reconnu en *equity* par lequel le prévôt ou le tribunal ordonne au créancier qui possède un droit garanti sur plusieurs choses ou sur plusieurs fonds appartenant au débiteur ou la garantie de deux ou de plusieurs débiteurs pour la même créance d'exercer son droit sur la garantie de la manière qui favorise le mieux les intérêts de la masse des créanciers.

La question à trancher était celle de savoir si un créancier chirographaire peut se prévaloir de la doctrine de la collocation en *equity*.

Jugement: la requête est accueillie.

L'*equity* a conçu la collocation, comme réparation, en application de la maxime selon laquelle personne ne doit s'enrichir en lésant autrui. En vertu du droit canadien, les fournisseurs d'approvisionnements nécessaires qui ne jouissent que de droits réels se trouvent dans la même situation que les créanciers chirographaires. La demanderesse a invoqué différentes décisions à l'appui de sa prétention portant que les créanciers chirographaires ne peuvent pas se prévaloir de la doctrine de la collocation en *equity*. En Angleterre, la collocation s'applique à toutes les sûretés doubles afin d'offrir une réparation équitable. La jurisprudence et la doctrine émanant d'Angleterre qui considèrent la collocation comme un concept d'*equity* de portée étendue visant à permettre une réparation lorsque c'est nécessaire, notamment en faveur des parties à un contrat oral ou écrit, ne lient pas la Cour fédérale, mais elles sont convaincantes. Rien n'indique dans la jurisprudence antérieure établissant la portée de la doctrine de la collocation en *equity* que ce recours ne peut être exercé par les créanciers ordinaires en vertu d'un contrat. En fait, l'inverse est vrai. Les créanciers chirographaires ont toujours eu, par le passé, le droit de

precedent on the right to marshal should not be followed blindly. Given the law surrounding the equitable roots of marshalling, a departure from recent case law was necessary to uphold what are plain and obvious principles of law. Furthermore, the cases cited by the Bank could be limited to their facts. They dealt with the rights of *in personam* creditors, not with those of *in rem* creditors. Production of the commitment letter to the *in rem* claimants would not be denied on the dubious proposition that mere *in rem* creditors may not benefit from marshalling.

profiter de la collocation en *equity*. Pourtant, certains tribunaux canadiens ont semblé limiter l'accessibilité à cette réparation, dans certaines circonstances, dérogeant ainsi aux concepts d'*equity* et niant expressément aux créanciers ordinaires le droit à la collocation en *equity*, mais sans véritable motif. Malgré la doctrine du *stare decisis*, il ne faut pas suivre aveuglément les précédents existants en ce qui concerne le droit à la collocation en *equity*. Compte tenu des règles de droit entourant les racines en *equity* de la collocation, il était nécessaire de déroger à la jurisprudence récente pour donner effet à des principes de droit clairs et évidents. De plus, la jurisprudence citée par la Banque peut être limitée aux faits en cause dans chaque cas. Elle traitait simplement des droits des titulaires d'une créance personnelle, et non des droits des titulaires d'une créance réelle. La production de la lettre d'engagement ne doit pas être refusée aux titulaires d'une créance réelle pour la raison quelque peu douteuse que la collocation en *equity* ne s'applique peut-être pas en leur faveur.

STATUTES AND REGULATIONS JUDICIALLY CONSIDERED

Administration of Estates Act, 1925 (U.K.), 15 Geo. 5, c. 23.
Federal Court Act, R.S.C., 1985, c. F-7, s. 22(2)(m).

CASES JUDICIALLY CONSIDERED

APPLIED:

Aldrich v. Cooper (1803), 8 Ves. Jun. 382; 32 E.R. 402 (Ch.); *Coastal Equipment Agencies Ltd. v. The Comer*, [1970] Ex. C.R. 13; affd [1971] S.C.R. v.

DISTINGUISHED:

Williamson v. Loonstra et al. (1973), 34 D.L.R. (3d) 275 (B.C.S.C.); *Bread Man Inc. (Re)* (1979), 21 O.R. (2d) 59; 89 D.L.R. (3d) 599; 29 C.B.R. (N.S.) 58 (S.C.); *Allison (Re)* (1995), 22 O.R. (3d) 102; 30 C.B.R. (3d) 144; 44 R.P.R. (2d) 237 (Gen. Div.).

CONSIDERED:

Benson Bros. Shipbuilding Co. (1960) Ltd. v. The Miss Donna, [1978] 1 F.C. 379 (T.D.); *National Provincial Bank Ltd. v. Katz*, [1960] Ch. 179; *Allison (Re)* (1998), 38 O.R. (3d) 337 (C.A.).

REFERRED TO:

Trimmer v. Bayne (1803), 9 Ves. Jun. 209; 32 E.R. 582 (Ch.).

LOIS ET RÈGLEMENTS

Administration of Estates Act, 1925 (R.-U.), 15 Geo. 5, ch. 23.
Loi sur la Cour fédérale, L.R.C. (1985), ch. F-7, art. 22(2)m).

JURISPRUDENCE

DÉCISIONS APPLIQUÉES:

Aldrich v. Cooper (1803), 8 Ves. Jun. 382; 32 E.R. 402 (Ch.); *Coastal Equipment Agencies Ltd. c. Le Comer*, [1970] R.C.É. 13; conf. par [1971] R.C.S. v.

DISTINCTION FAITE AVEC:

Williamson v. Loonstra et al. (1973), 34 D.L.R. (3d) 275 (C.S.C.-B.); *Bread Man Inc. (Re)* (1979), 21 O.R. (2d) 59; 89 D.L.R. (3d) 599; 29 C.B.R. (N.S.) 58 (C.S.); *Allison (Re)* (1995), 22 O.R. (3d) 102; 30 C.B.R. (3d) 144; 44 R.P.R. (2d) 237 (Div. gén.).

DÉCISIONS EXAMINÉES:

Benson Bros. Shipbuilding Co. (1960) Ltd. c. (Le) Miss Donna, [1978] 1 C.F. 379 (1^{re} inst.); *National Provincial Bank Ltd. v. Katz*, [1960] Ch. 179; *Allison (Re)* (1998), 38 O.R. (3d) 337 (C.A.).

DÉCISION CITÉE:

Trimmer v. Bayne (1803), 9 Ves. Jun. 209; 32 E.R. 582 (Ch.).

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- Halsbury's Laws of England*, vol. 16, 4th ed. reissue. London: Butterworths, 1992.
- Story, Joseph. *Commentaries on Equity Jurisprudence*, 3rd English ed. by A. E. Randall. London: Sweet and Maxwell, 1920.
- Tetley, William. *Maritime Liens and Claims*, 2nd ed. Montréal: International Shipping Publications, 1998.

MOTION for production of documents showing any collateral benefit received by the mortgagee for which it should account thus making more of the proceeds of the judicial sale of the *Nel* available to unsecured creditors. Motion allowed.

APPEARANCE:

- Peter Bernard* for plaintiff.
- John Bromley* for claimant Campotex Shipping Services Ltd.
- Christopher Giaschi* for claimant Legend Marine Singapore Pte. Ltd.
- Jonathan S. McLean* for claimants Aktina SA, Bureau Veritas and Mariners Medical Clinic.
- David F. McEwen* for claimants Petro Marine Products, Ashland Chemical Inc. and Empire International Steavadores Ltd.
- Doug G. Morrison* for claimant Shell Canada Limited.
- Michael J. Bird* for claimant Sait Communications SA.
- Louis Buteau* for claimant Alfa Bunkering Co. Ltd.
- Marc de Man* and *Andrea J. Sterling* for claimant HBI International.
- A. Barry Oland* for claimant Pacific Pilotage Authority.

SOLICITORS OF RECORD:

- Campney & Murphy*, Vancouver, for plaintiff.
- Bromley, Chapelski*, Vancouver, for claimant Campotex Shipping Services Ltd.
- Giaschi, Margolis*, Vancouver, for claimant Legend Marine Singapore Pte. Ltd.
- Edwards, Kenny & Bray*, Vancouver, for claimants Aktina SA, Bureau Veritas and Mariners Medical Clinic.

DOCTRINE

- Halsbury's Laws of England*, vol. 16, 4th ed. reissue. London: Butterworths, 1992.
- Story, Joseph. *Commentaries on Equity Jurisprudence*, 3rd English ed. par A. E. Randall. London: Sweet and Maxwell, 1920.
- Tetley, William. *Maritime Liens and Claims*, 2nd ed. Montréal: International Shipping Publications, 1998.

REQUÊTE en vue de la production de documents révélant tout avantage accessoire que la créancière hypothécaire aurait reçu et dont elle devrait rendre compte, ce qui rendrait une plus grande part du produit de la vente judiciaire du *Nel* accessible aux créanciers chirographaires. Requête accueillie.

ONT COMPARU:

- Peter Bernard* pour la demanderesse.
- John Bromley* pour la réclamante Campotex Shipping Services Ltd.
- Christopher Giaschi* pour la réclamante Legend Marine Singapore Pte. Ltd.
- Jonathan S. McLean* pour les réclamantes Aktina SA, Bureau Veritas et Mariners Medical Clinic.
- David F. McEwen* pour les réclamantes Petro Marine Products, Ashland Chemical Inc. et Empire International Steavadores Ltd.
- Doug G. Morrison* pour la réclamante Shell Canada Limitée.
- Michael J. Bird* pour la réclamante Sait Communications SA.
- Louis Buteau* pour la réclamante Alfa Bunkering Co. Ltd.
- Marc de Man* et *Andrea J. Sterling* pour la réclamante HBI International.
- A. Barry Oland* pour la réclamante Pacific Pilotage Authority.

AVOCATS INSCRITS AU DOSSIER:

- Campney & Murphy*, Vancouver, pour la demanderesse.
- Bromley, Chapelski*, Vancouver, pour la réclamante Campotex Shipping Services Ltd.
- Giaschi, Margolis*, Vancouver, pour la réclamante Legend Marine Singapore Pte. Ltd.
- Edwards, Kenny & Bray*, Vancouver, pour les réclamantes Aktina SA, Bureau Veritas et Mariners Medical Clinic.

McEwen, Schmitt & Co., Vancouver, for claimants Petro Marine Products, Ashland Chemical Inc. and Empire International Steavadores Ltd.

Bull, Housser & Tupper, Vancouver, for claimant Shell Canada Limited.

Owen, Bird, Vancouver, for claimant Sait Communications SA.

Sproule, Castonguay, Montréal, for claimant Alfa Bunkering Co. Ltd.

Gottlieb & Pearson, Montréal, for claimant HBI International.

A. B. Oland, Vancouver, for claimant Pacific Pilotage Authority.

The following are the reasons for order rendered in English by

[1] HARGRAVE P.: These reasons which touch on the doctrine of marshalling as between mortgagee and creditor, arise out of the motion of Alfa Bunkering Co. Ltd. (Alfa Bunkering), a necessities supplier and claimant to the proceeds of the judicial sale of the *Nel*. Alfa Bunkering wishes to have the plaintiff, The Governor and Company of the Bank of Scotland (the Bank of Scotland) produce various documents on which its nominee might be cross-examined during the procedure leading up to a determination of priorities to the sale proceeds.

BACKGROUND

[2] The judicial sale and the purchase of the *Nel* were organized by the Bank of Scotland. The Bank of Scotland also financed both the purchase of the *Nel* and of the *Blue L*, the latter vessel a sister ship sold by a South African court.¹

[3] The Bank of Scotland, both in this Canadian proceeding and in the South African proceeding, looks to the sale proceeds to satisfy claims for money lent and secured by mortgages on the *Nel* and the *Blue L* and on several other vessels in the same ownership; in effect the Bank of Scotland held, at material times, a fleet mortgage. If the Bank of Scotland, as a mort-

McEwen, Schmitt & Co., Vancouver, pour les réclamantes Petro Marine Products, Ashland Chemical Inc. et Empire International Steavadores Ltd.

Bull, Housser & Tupper, Vancouver, pour la réclamante Shell Canada Limitée.

Owen, Bird, Vancouver, pour la réclamante Sait Communications SA.

Sproule, Castonguay, Montréal, pour la réclamante Alfa Bunkering Co. Ltd.

Gottlieb & Pearson, Montréal, pour la réclamante HBI International.

A. B. Oland, Vancouver, pour la réclamante Pacific Pilotage Authority.

Ce qui suit est la version française des motifs de l'ordonnance rendus par

[1] LE PROTONOTAIRE HARGRAVE: Les présents motifs, qui portent sur la doctrine de la collocation en *equity* (*marshalling*) entre la créancière hypothécaire et l'autre créancière, font suite à la présentation d'une requête par la société Alfa Bunkering Co. Ltd. (Alfa Bunkering), qui est un fournisseur d'approvisionnements nécessaires et qui revendique une participation au produit de la vente judiciaire du *Nel*. Alfa Bunkering désire que la demanderesse, The Governor and Company of the Bank of Scotland (la Banque d'Écosse) produise différents documents à l'égard desquels son représentant pourrait être contre-interrogé au cours de la procédure à l'issue de laquelle sera établi l'ordre de priorité pour la répartition du produit de la vente.

CONTEXTE

[2] La vente judiciaire du *Nel* a été organisée par la Banque d'Écosse. La Banque d'Écosse a également financé l'achat du *Nel* et du *Blue L*, ce dernier bateau étant un navire jumeau vendu par un tribunal d'Afrique du Sud¹.

[3] La Banque d'Écosse, dans les instances intentées au Canada et en Afrique du Sud, s'intéresse au produit de la vente dans le but d'obtenir le remboursement d'un prêt garanti par une hypothèque grevant le *Nel* et le *Blue L* ainsi que plusieurs autres bateaux appartenant à la même propriétaire; en fait, la Banque d'Écosse était titulaire d'une hypothèque grevant la

gagee, holds a priority coming after the marshal's sale costs, its claims will substantially exhaust the sale proceeds of at least the *Nel*.

[4] Counsel for Alfa Bunkering, which looks to the *Nel* proceeds to satisfy its claim, submits it has a maritime lien, but is concerned that if Alfa Bunkering is found to be the holder of a mere statutory right *in rem*, coming behind a mortgage in priority, there will be no funds left from the sale of the *Nel* once the claim of the Bank of Scotland is satisfied. Alfa Bunkering wishes to make certain that the Bank of Scotland, through its nominee, be thoroughly cross-examined, an examination going beyond the usual proof of security and accounting, to test for any collateral benefit the Bank of Scotland might have obtained as lenders to the new owners of the *Nel*. Counsel for various other claimants are in a similar position to that of Alfa Bunkering.

[5] When the motion initially came on for hearing various counsel for the lien claimants, who brought and who supported the motion, could not produce evidence of the Bank of Scotland receiving a collateral benefit and to that extent any exploration would be an improper fishing expedition. However, counsel submitted that the financing of the purchase of the *Nel* and of the *Blue L* is a special circumstance and thus the Bank of Scotland ought to produce various documents bearing on its post-sale involvement with the two vessels, including the commitment letter and the loan agreement between the Bank of Scotland and the present owner of the *Nel* who is also the buyer and owner of the *Blue L*. Counsel for Alfa Bunkering submits that there might be a close connection between the former owner and the new owner of the *Nel* and *Blue L* and that perhaps the new owner remains responsible to the Bank of Scotland for some portion of the original debt. Again, this was an unsupported submission.

flotte à toutes les époques pertinentes. Si, dans l'ordre des priorités, la créance hypothécaire de la Banque d'Écosse prend rang immédiatement après la créance du prévôt relativement aux frais de la vente, sa réclamation épuisera en grande partie le produit de la vente, à tout le moins du *Nel*.

[4] L'avocat d'Alfa Bunkering, qui s'intéresse au produit de la vente du *Nel* aux fins du paiement de sa créance, prétend que cette société est titulaire d'un privilège maritime, mais craint, si elle est considérée comme titulaire d'un simple droit réel d'origine législative, qui prendrait rang après l'hypothèque, qu'il ne reste pas de fonds tirés de la vente du *Nel* après le paiement de la créance de la Banque d'Écosse. Alfa Bunkering veut s'assurer que la Banque d'Écosse soit contre-interrogée de façon approfondie, par l'entremise de son représentant, la portée de l'interrogatoire s'étendant au-delà de la preuve habituelle de la sûreté et de la reddition de compte, afin de vérifier si la Banque d'Écosse a pu obtenir un avantage accessoire en consentant un prêt à la nouvelle propriétaire du *Nel*. Les avocats des différents autres créanciers défendent une position semblable à celle de l'avocat d'Alfa Bunkering.

[5] Lors de l'audition initiale de la requête, les différents avocats représentant les titulaires de privilèges, qui ont présenté et appuyé la requête, n'ont pas pu produire d'éléments de preuve établissant que la Banque d'Écosse aurait reçu un avantage accessoire et, dans cette mesure, la recherche de renseignements constituerait un interrogatoire à l'aveuglette inopportun. Toutefois, les avocats ont soutenu que le financement de l'achat du *Nel* et du *Blue L* constitue une circonstance particulière et que la Banque d'Écosse doit donc produire différents documents portant sur ses opérations postérieures à la vente touchant ces deux bateaux, et notamment sa lettre d'engagement et la convention de prêt conclue entre la Banque d'Écosse et la propriétaire actuelle du *Nel* qui a également acheté le *Blue L*. L'avocat d'Alfa Bunkering soutient qu'il se peut qu'il existe un lien étroit entre l'ancienne et la nouvelle propriétaire du *Nel* et du *Blue L* et que la nouvelle propriétaire pourrait demeurer responsable d'une partie de la dette initiale envers la Banque d'Écosse. Aucun élément de preuve n'a été produit à l'appui de cette prétention non plus.

[6] Counsel for the Bank of Scotland had not seen any of the requested material, but submitted that production was not only irrelevant, but also an uncalled for intrusion into the affairs of the new owner.

[7] I ordered the documents produced to the Court for examination, adjourning the motion pending that examination, with the parties to reattend in due course. To assist the parties I provided each counsel with a copy of a memorandum, being my assessment of the documents, before the motion resumed, the disputed documents being again placed in a sealed envelope, this time in the possession of the Court.

[8] Essentially I found the documents irrelevant, except to the extent that the commitment letter indicated the loan secured by the mortgage of the *Blue L* was substantially in excess of both the appraised value and the purchase price of that ship. Now there may be a perfectly good reason for the apparent advance in excess of the purchase price, for example funds earmarked for dry docking or repairing the ship, to the benefit of both owner and mortgage holder, but that is not the present issue.

[9] Counsel for Alfa Bunkering, with support from counsel for other claimants, submits this excessive loan figure could, if the loan proceeds were not entirely advanced, result in a bonus to the Bank of Scotland on repayment. Further there is an indication that if the venture went well and the *Nel*, a twenty-four-year old vessel in a presently declining market, were to increase in value, during the modest term of the mortgage and be sold for more than her purchase price, a price which was consistent with the then appraised value, the Bank of Scotland would participate in that profit. All of this, submit counsel, is a collateral benefit for which the Bank of Scotland should account, for it could make more funds available to the lien claimants. The latter so-called collateral benefit, a possible participation in a very speculative profit, is too far removed and too uncertain

[6] L'avocat de la Banque d'Écosse n'a examiné aucun des documents demandés, mais il a fait valoir non seulement que leur production serait non pertinente, mais encore qu'elle constituerait une intrusion injustifiée dans les affaires de la nouvelle propriétaire.

[7] J'ai ordonné que les documents soient produits devant la Cour pour examen et j'ai ajourné la requête jusqu'à l'issue de cet examen, les parties devant comparaître à nouveau en temps opportun. Pour aider les parties, j'ai remis à chaque avocat une copie d'un mémoire, faisant état de mon évaluation des documents, avant la reprise de l'audition de la requête, les documents contestés étant à nouveau placés dans une enveloppe scellée, cette fois en possession de la Cour.

[8] J'ai conclu pour l'essentiel que ces documents n'étaient pas pertinents, sauf dans la mesure où la lettre d'engagement indiquait que le montant du prêt garanti par l'hypothèque grevant le *Blue L* était de beaucoup supérieur à la valeur estimative et au prix d'achat de ce navire. Toutefois, il existe peut-être une très bonne raison pour laquelle le montant prêté dépassait apparemment le prix d'achat; il peut par exemple s'agir de fonds destinés au paiement de la mise en cale sèche et des réparations du navire, au profit à la fois de la propriétaire et de la titulaire de l'hypothèque, mais ce n'est pas cette question que la Cour doit trancher en l'espèce.

[9] L'avocat d'Alfa Bunkering soutient, avec l'appui des avocats des autres créanciers, que le montant excédentaire du prêt pourrait permettre à la Banque d'Écosse de toucher une prime lors du remboursement du prêt, si les fonds du prêt ne sont pas versés en totalité. Il y a en outre lieu de croire que la Banque d'Écosse participerait au profit, si l'aventure s'avérait fructueuse et si le *Nel*, un navire vieux de vingt-quatre ans dans un marché en déclin, prenait de la valeur pendant la courte durée du prêt et était vendu à un prix supérieur à son prix d'achat, qui correspondait à sa valeur estimative au moment de l'achat. L'avocat prétend que ces possibilités constituent un avantage accessoire dont la Banque d'Écosse doit rendre compte, car elles pourraient dégager plus de fonds pour les créanciers privilégiés. La dernière possibilité qualifiée d'avantage accessoire, savoir la participation

to be relevant. The former, a possible bonus to the Bank of Scotland on the financing of the *Blue L*, is only relevant if the necessary claimants do not have maritime liens, ranking ahead of the Bank of Scotland, but only hold statutory rights *in rem* and are able to require the Bank of Scotland to marshal.

[10] The concept of marshalling was brought up by counsel and therefore I touched upon it in my memorandum to counsel indicating that if counsel “wished to broach the matter of marshalling and the *Blue L*, or other vessels involved, that ought to be done, to the extent that it may be proper, on cross-examination”: at the time I had doubts as to whether the doctrine of marshalling applied and thus the reservation, “to the extent that it may be proper” for there is some authority that creditors of all types are not necessarily entitled to the benefit of marshalling. I now turn to a consideration of the motion, beginning with the concept of marshalling.

CONSIDERATION

[11] There are some very involved formulations of the concept of marshalling and here I have in mind traditional definitions such as that set out in the 4th edition (reissue) of *Halsbury's Laws of England*, Volume 16, paragraph 876 at page 785. However the basic concept of marshalling is very simple:

... a person having resort to two funds shall not by his choice disappoint another, having only one. [*Trimmer v. Bayne* (1803), 32 E.R. 582, at p. 583, a Chancery decision of Sir William Grant, Master of the Rolls.]

One of the authorities to which the Master of the Rolls was referred in *Trimmer v. Bayne* was an earlier case, *Aldrich v. Cooper* (1803), 32 E.R. 402 (Ch.), in which Lord Chancellor Eldon wrote, at page 407:

éventuelle à un profit hautement spéculatif, est beaucoup trop éloignée et incertaine pour être pertinente. La première, soit la prime que la Banque d'Écosse pourrait tirer du financement du *Blue L*, n'est pertinente que si les créanciers fournisseurs d'approvisionnements nécessaires ne sont pas titulaires de privilèges maritimes prenant rang avant la Banque d'Écosse, mais uniquement de droits réels d'origine législative et peuvent obliger la Banque d'Écosse à procéder à une collocation en *equity*.

[10] Le concept de la collocation en *equity* a été soulevé par les avocats. J'en ai donc traité dans mon mémoire adressé aux avocats indiquant que s'ils [TRADUCTION] «désiraient aborder la question de la collocation en *equity* et du *Blue L*, ou d'autres bateaux concernés, ils devaient le faire, dans la mesure où cela convient, lors du contre-interrogatoire»: à ce moment, j'entretenais des doutes sur la question de savoir si la doctrine de la collocation en *equity* s'appliquait, d'où les termes «dans la mesure où cela convient» exprimant une réserve car, selon certaines sources, tous les types de créanciers n'ont pas nécessairement le droit de se prévaloir d'une collocation en *equity*. J'examinerai maintenant la requête, en commençant par la question de la collocation en *equity*.

ANALYSE

[11] Il existe des formulations très complexes de la notion de collocation en *equity*. Je songe en l'occurrence aux définitions traditionnelles telle celle énoncée dans la 4^e édition (réédition) de l'ouvrage intitulé *Halsbury's Laws of England*, volume 16, paragraphe 876, à la page 785. Toutefois, le concept fondamental de la collocation en *equity* est très simple:

[TRADUCTION] ... la personne qui peut recourir à deux fonds ne doit pas faire un choix qui lèse une autre personne, qui ne peut recourir qu'à un seul. [*Trimmer v. Bayne* (1803), 32 E.R. 582, à la page 583, décision de la Chancellerie rendue par Sir William Grant, président de la Cour d'appel.]

L'une des sources portées à l'attention du président de la Cour d'appel, dans l'affaire *Trimmer v. Bayne*, était la décision antérieure *Aldrich v. Cooper* (1803), 32 E.R. 402 (Ch.), dans laquelle le lord chancelier Eldon a écrit à la page 407:

... a person having two funds shall not by his election disappoint the party having only one fund; and equity, to satisfy both, will throw him, who has two funds, upon that which can be affected by him only; to the intent that the only fund, to which the other has access, may remain clear to him. [See also *Halsbury's*, *supra*, footnote 3, at page 785.]

[12] Tetley on *Maritime Liens and Claims*, 2nd edition, International Shipping Publications, 1998, describes marshalling in the following straight forward terms (at page 857):

Marshalling is the equitable process, whereby the Marshall or the court orders a creditor who has a secured right on more than one *res* or more than one fund belonging to the debtor, or security from two or more debtors for the same debt, to exercise his right on the security in a manner which will be in the best interests of all creditors. The Marshall or court must also take into consideration the best interests of third parties and even of the debtor. Marshalling was often used in respect to bottomry bonds.

[13] Counsel for the Bank of Scotland submits there is a limitation on marshalling, that in Canada and in British Columbia an unsecured creditor is not able to rely upon the doctrine of marshalling to cause a mortgagee to proceed against security in any particular way. In order to consider this concept I must first establish the position of a necessary supplier with a mere statutory right *in rem*. Certainly in England the necessary supplier becomes a secured creditor on the issuance of a writ *in rem*: see a discussion of this in Tetley on *Maritime Liens and Claims* (*supra*), at pages 556-557. But such is not the case in Canada.

[14] The position of a necessities claimant, with a right *in rem*, is set out in *Coastal Equipment Agencies Ltd. v. The Comer*, [1970] Ex. C.R. 13, in which Mr. Justice Noël dealt particularly with the position of necessities suppliers when the owner of various defendant ships had made a proposal in bankruptcy, but also generally with the position of a necessities supplier under what is now paragraph 22(2)(m) of the *Federal Court Act* [R.S.C., 1985, c. F-7]. He pointed

[TRADUCTION] ... la personne qui possède deux fonds ne doit pas faire un choix qui lèse la partie qui n'en possède qu'un; et, pour qu'elles soient payées toutes les deux, l'*equity* dirigera celle qui possède deux fonds vers celui qu'elle est seule à pouvoir utiliser; de façon que l'unique fonds auquel l'autre a accès puisse demeurer intact pour elle. [Voir aussi *Halsbury's*, précité, note 3, à la page 785.]

[12] Tetley, dans l'ouvrage intitulé *Maritime Liens and Claims*, 2^e édition, International Shipping Publications, 1998, décrit la collocation en *equity* en termes simples (à la page 857):

[TRADUCTION] La collocation est un mécanisme reconnu en *equity* par lequel le prévôt ou le tribunal ordonne au créancier qui possède un droit garanti sur plusieurs choses ou sur plusieurs fonds appartenant au débiteur ou la garantie de deux ou de plusieurs débiteurs pour la même créance d'exercer son droit sur la garantie de la manière qui favorise le mieux les intérêts de la masse des créanciers. Le prévôt ou le tribunal doit également tenir compte des meilleurs intérêts des tiers et même de ceux du débiteur. La collocation a souvent été utilisée dans le contexte des contrats de prêt à la grosse.

[13] L'avocat de la Banque d'Écosse soutient que la collocation en *equity* est assujettie à des limites, qu'un créancier chirographaire ne peut pas, au Canada et en Colombie-Britannique, s'appuyer sur la doctrine de la collocation en *equity* pour obliger un créancier hypothécaire à réaliser sa garantie d'une façon particulière. Pour examiner cette notion, je dois d'abord déterminer quelle est la situation du fournisseur d'approvisionnements nécessaires titulaire d'un simple droit réel d'origine législative. Certes, en Angleterre, le fournisseur d'approvisionnements nécessaires devient un créancier garanti au moment de la délivrance d'un bref *in rem*: voir l'analyse faite dans Tetley: *Maritime Liens and Claims* (précité), aux pages 556 et 557. Ce n'est toutefois pas le cas au Canada.

[14] La situation du fournisseur d'approvisionnements nécessaires titulaire d'un droit réel est précisée dans l'arrêt *Coastal Equipment Agencies Ltd. c. Le Comer*, [1970] R.C.É. 13, dans lequel le juge Noël a traité en particulier de la situation du fournisseur d'approvisionnements nécessaires dans le cas où le propriétaire de différents navires défendeurs avait fait une proposition en vertu du droit de la faillite, mais également de la situation d'un fournisseur d'approvi-

out that none of the legislation or decisions permitted him to say that the *in rem* right conferred any privilege or lien whatsoever, although an *in rem* action against a ship, an extraordinary right, could be advantageous (page 31). He went on at pages 31 and 33 to say:

This action *in rem*, however, does not give any privilege or lien or preference whatsoever, and the claimant for necessities seems to me to be in the same position as an ordinary unsecured creditor. If he is an execution creditor, he will be entitled to his costs of action but his claim will be ranked only in accordance with the order of priorities set by law. In fact, to give him, through the mere fact that he has a simple right of action *in rem*, a right and specific privilege which would deprive the same debtor's other creditors of exercising their claims against the property seized, especially after the corporation owning such property has made a proposal under the *Bankruptcy Act*, seems to me unacceptable and based on no legal text or judgment. In fact, this would be a serious blow to the principle whereby the property of a debtor is the security of his creditors.

[15] Mr. Justice Addy, in *Benson Bros. Shipbuilding Co. (1960) Ltd. v. The Miss Donna*, [1978] 1 F.C. 379 (T.D.), at page 383, notes that Mr. Justice Noël's decision in *The Comer* that "the right of action *in rem* gives no privilege, lien or preference of any kind and that the supplier of necessities is still in the same position as an ordinary creditor", was upheld by the Supreme Court of Canada in an unreported decision 25 March 1971 [[1971] S.C.R. v]. Clearly, in the present instance, if those who supplied necessities to the *Nel* cannot, by various means, for example through the application of substantive foreign law, bring themselves within the ambit of maritime lien holders, they must be, under Canadian law, necessities suppliers with mere rights *in rem* which leave them in the position of unsecured creditors.

[16] Counsel for the Bank of Scotland, as I have said, refers in written argument to various cases for

sionnements nécessaires sous le régime de la disposition qui constitue maintenant l'alinéa 22(2)m) de la *Loi sur la Cour fédérale* [L.R.C. (1985), ch. F-7]. Il a noté qu'aucune disposition législative ni décision ne lui permettait d'affirmer que le droit réel confère un privilège ni un lien quelconque, bien qu'une action réelle intentée contre un navire constitue un droit extraordinaire qui peut être avantageux (page 30). Il a enchaîné, aux pages 30 et 32:

Cette action *in rem*, cependant, ne donne aucun privilège ou lien ou préférence quelconque et le réclamant d'approvisionnement nécessaires me paraît être dans la même situation qu'un créancier chirographaire ordinaire. S'il est créancier exécutant, il aura droit à ses frais d'action mais sa créance ne prendra rang que suivant l'ordre des priorités fixées par la loi. Lui donner, en effet par suite du simple fait qu'il possède un simple droit d'action *in rem* un droit et privilège particulier qui priverait les autres créanciers du même débiteur d'exercer leurs créances contre les biens saisis surtout après que la corporation propriétaire de ces biens ait fait une proposition de vertu de la *Loi sur la faillite*, me paraît inacceptable et fondé sur aucun texte légal ni décision judiciaire. Il y aurait là, en effet, un accroc sérieux au principe qui veut que les biens d'un débiteur soient le gage commun de ses créanciers.

[15] Le juge Addy, dans *Benson Bros. Shipbuilding Co. (1960) Ltd. c. Le Miss Donna*, [1978] 1 C.F. 379 (1^{re} inst.), aux pages 383 et 384, souligne que la décision du juge Noël dans l'affaire *Le Comer* selon laquelle «le droit d'action *in rem* ne donne aucun privilège, ni aucune préférence de quelque sorte que ce soit, le fournisseur de choses indispensables au navire demeurant dans la même situation qu'un créancier chirographaire», a été confirmée par la Cour suprême du Canada dans un arrêt non publié du 25 mars 1971 [[1971] R.C.S. v]. En l'occurrence, si les personnes qui ont fourni les approvisionnements nécessaires au *Nel* ne peuvent, par différents moyens, et notamment par l'application du droit substantiel étranger, être reconnues comme titulaires d'un privilège maritime, il est clair qu'en vertu du droit canadien elles constituent des fournisseurs d'approvisionnements nécessaires qui ne jouissent que de droits réels et qui se trouvent donc dans la même situation que les créanciers chirographaires.

[16] L'avocat de la Banque d'Écosse, comme je l'ai dit, invoque, dans sa plaidoirie écrite, différentes

the concept that unsecured creditors are not able to avail themselves of the doctrine of marshalling. Counsel opposing did not meet this last minute written argument with any case law, perhaps by reason of a clear lack of time to prepare. However there is case law to the contrary. I turn first to three representative cases from among those referred to by counsel for the Bank of Scotland.

[17] In *Williamson v. Loonstra et al.* (1973), 34 D.L.R. (3d) 275, at pages 278-279, Mr. Justice Ruttan, of the B.C. Supreme Court, noted that marshalling did not apply in favour of an unsecured creditor:

The doctrine does not extend to all creditors of every degree, it does not apply in favour of an unsecured creditor and it does not apply in favour of a judgment creditor unless he has obtained a charge on the estate that he seeks to have marshalled in his favour.

In support of this proposition Mr. Justice Ruttan refers to several authorities, but does not look at any of the earlier cases which set out and considered the concept of marshalling.

[18] Mr. Justice Saunders, of the Supreme Court of Ontario, referred to the passage from the *Williamson* case in *Re Bread Man Inc.* (1979), 21 O.R. (2d) 59, at page 63, and noted that:

It is also logical that unsecured credits [*sic*] of debtors should not be protected for in the absence of a statutory provision, they should have no better right to the fund than the debtor himself.

This might seem to offend against a number of equitable maxims and doctrines. The Ontario Court General Division also referred to *Loonstra* in *Allison (Re)* (1995), 22 O.R. (3d) 102, applying it against unsecured creditors, however the Ontario Court of Appeal took a somewhat different tack when it considered *Re Allison*, a point I will touch on in due course.

[19] The line of Canadian cases referred to by counsel for the Bank of Scotland bothers me in that

décisions à l'appui de sa prétention portant que les créanciers chirographaires ne peuvent pas se prévaloir de la doctrine de la collocation en *equity*. L'avocat de la partie opposée n'a invoqué aucune jurisprudence pour contrer cet argument de dernière minute, peut-être parce qu'il a manifestement manqué de temps pour se préparer. Il existe toutefois de la jurisprudence à l'appui de l'argument contraire. J'examinerai d'abord trois décisions représentatives parmi celles citées par l'avocat de la Banque d'Écosse.

[17] Dans *Williamson v. Loonstra et al.* (1973), 34 D.L.R. (3d) 275, aux pages 278 et 279, le juge Ruttan, de la Cour suprême de la Colombie-Britannique, a souligné que la collocation en *equity* ne s'appliquait pas en faveur d'un créancier chirographaire:

[TRADUCTION] Cette doctrine ne s'étend pas à tous les créanciers occupant chaque rang de l'ordre de priorité, elle ne s'applique pas en faveur d'un créancier chirographaire et elle ne s'applique pas en faveur du créancier d'un jugement à moins qu'il ait obtenu une charge grevant les biens à l'égard desquels il demande une collocation en sa faveur.

Le juge Ruttan appuie cette affirmation sur plusieurs sources, mais il n'examine aucune des décisions antérieures qui ont établi et analysé le concept de la collocation en *equity*.

[18] Le juge Saunders de la Cour suprême de l'Ontario a mentionné ce passage de la décision *Williamson* dans *Re Bread Man Inc.* (1979), 21 O.R. (2d) 59, à la page 63. Il a noté:

[TRADUCTION] Il est aussi logique que les créanciers chirographaires des débiteurs ne soient pas protégés car, en l'absence d'une disposition législative, il ne devraient pas avoir, sur le fonds, de droit supérieur à celui du débiteur.

Cette affirmation peut sembler contraire à plusieurs maximes et doctrines d'*equity*. La Division générale de la Cour de l'Ontario a également fait mention de la décision *Loonstra* dans *Allison (Re)* (1995), 22 O.R. (3d) 102, en l'appliquant contre des créanciers chirographaires, mais la Cour d'appel de l'Ontario a adopté une approche assez différente lorsqu'elle s'est penchée sur l'affaire *Re Allison*. J'en reparlerai en temps opportun.

[19] Le courant jurisprudentiel invoqué par l'avocat de la Banque d'Écosse m'embarrasse parce que les

marshalling was, at one time, available to simple contract holders, that is to holders of written or verbal contracts: see for example *Aldrich v. Cooper* (*supra*) in which simple contract creditors were entitled to stand in the place of creditors by specialty, that is in the place of creditors by deed, thus gaining the benefit of marshalling. This concern about simple contract creditors and specialty creditors no longer exists, for as the editors of Halsbury's point out in Volume 16 (*supra*) at paragraph 879: formerly simple contract creditors might look only to a personal estate for satisfaction, yet specialty contract debtors might look to both real and personal estates and thus, as between creditors, simple contract creditors were entitled to have assets marshalled in their favour so as to throw the specialty creditors on the real estate. This distinction between specialty and simple contract debtors was abolished in England by 1869 and subsequent legislation which is summed up in the *Administration of Estates Act*, 1925 (U.K.) [15 Geo. 5, c. 23]. However the concept of allowing contract creditors to marshal still does exist in England. Here I have in mind *National Provincial Bank Ltd. v. Katz*. *Aldrich v. Cooper* was considered in *National Provincial Bank Ltd. v. Katz*, [1960] Ch. 179, at page 190. There Mr. Justice Danckwerts (as he then was) also referred to a wide application of marshalling from Story's Equity Jurisprudence:²

In the sense of the courts of equity, the marshalling of assets is such an arrangement of the different funds under administration as shall enable all parties, having equities thereon, to receive their due proportions, notwithstanding any intervening interests, liens or other claims of particular persons to prior satisfaction, out of a portion of those funds. [Story, 1920 edition, at p. 239.]

From this beginning Mr. Justice Story [at page 239] goes on to note that equity, in engineering redress in cases involving marshalling, in order to prevent the

parties à un contrat nu, c'est-à-dire les parties à un contrat écrit ou verbal, pouvaient autrefois se prévaloir de la collocation en *equity*: voir, par exemple, l'affaire *Aldrich v. Cooper* (précitée) dans laquelle les parties à des contrats nus ont pu accéder au rang des créanciers munis d'un contrat formaliste, c'est-à-dire les créanciers munis d'un contrat scellé, ce qui leur a donné le droit de se prévaloir de la collocation en *equity*. Le problème des créanciers munis d'un contrat nu et des créanciers munis d'un contrat formaliste n'existe plus, car, comme les rédacteurs du Halsbury's le précisent dans le volume 16 (précité) au paragraphe 879, à l'origine, les créanciers munis d'un contrat nu ne pouvaient s'en prendre qu'aux biens meubles pour obtenir le paiement de leur créance, alors que les créanciers munis d'un contrat formalistes pouvaient utiliser tant les biens immeubles que les biens meubles; en conséquence, les créanciers munis d'un contrat nu pouvaient obtenir une collocation en *equity* en leur faveur de façon à diriger les créanciers munis d'un contrat formaliste vers les biens immeubles. Cette distinction entre les créanciers munis d'un contrat nu et d'un contrat formaliste a été abolie en Angleterre par des mesures législatives prises en 1869 et par la suite. Ces mesures sont résumées dans l'ouvrage intitulé *Administration of Estates Act*, 1925 (R.-U.) [15 Geo. 5, ch. 23]. Toutefois, le principe permettant aux créanciers munis d'un contrat d'obtenir la collocation en *equity* existe toujours en Angleterre. Je songe ici à l'affaire *National Provincial Bank Ltd. v. Katz*. On trouve une analyse de la décision *Aldrich v. Cooper* dans l'affaire *National Provincial Bank Ltd. v. Katz*, [1960] Ch. 179, à la page 190. Le juge Danckwerts (tel était alors son titre) s'est également reporté à une application large de la collocation en *equity* tirée de Story's equity Jurisprudence²:

[TRADUCTION] Selon les tribunaux d'*equity*, la collocation des biens constitue un arrangement des différents fonds administrés qui permet à toutes les parties titulaires de droits en *equity* sur ces fonds de recevoir leur juste part, malgré tout intérêt, privilège ou autre créance intermédiaire d'une personne en particulier lui permettant d'être payée en priorité à l'aide de ces fonds. [Story, édition de 1920, à la page 239.]

À partir de ce point de départ, le juge Story (à la page 239) enchaîne en soulignant que l'*equity*, en concevant des réparations dans les cas d'application de la collo-

creditor, with more than one choice of funds from which to satisfy a debt, from defeating other claimants by taking his satisfaction to the exclusion of such claimants, is doing little more than applying the maxim *nemo ex alterius detrimento fieri debet locupletior*: no man ought to be made rich out of another's injury:

... where there exist two or more funds, and there are several claimants against them, and at law one of the parties may resort to either fund for satisfaction, but the others can come upon one only; there, courts of equity exercise the authority to marshal (as it is called) the funds, and by this means enable the parties whose remedy at law is confined to one fund only, to receive due satisfaction. The general principle upon which courts of equity interfere in these cases is, that, without such interference, he who had a title to the double fund would possess an unreasonable power of defeating the claimants upon either fund, by taking his satisfaction out of the other, to the exclusion of them. So that, in fact, it would be entirely in his election, whether they should receive any satisfaction or not. Now, courts of equity treat such an exercise of power as wholly unjust and unconscientious; and therefore will interfere, not, indeed to modify or absolutely to destroy the power, but to prevent it from being made an instrument of caprice, injustice, or imposition. Equity, it affording redress in such cases, does little more than apply the maxim, *Nemo ex alterius detrimento fieri debet locupletior*.

Story notes that the principle of marshalling is not limited to the administration of assets, or competing mortgagees, but indeed applies to cases of double security generally in order to afford equitable redress. Certainly the English cases and authorities which treat marshalling as a broad equitable concept to give relief where needed, including to mere holders of oral and written contracts, are not binding on the Federal Court, yet they are persuasive. There is no suggestion in the early cases setting out the scope of the doctrine of marshalling that it is a remedy barred to ordinary contractual creditors. The opposite is true. Yet some Canadian courts, in certain circumstances, seemed to have applied that limitation, departing from equitable concepts and specifically denying the relief of marshalling to ordinary creditors, but I think without any real reason.

cation en *equity*, afin d'empêcher un créancier qui a le choix de recourir à plus d'un fonds pour obtenir le paiement de sa créance de faire échec aux droits des autres créanciers en procédant d'une façon qui les excluent, va à peine au-delà de l'application de la maxime *nemo ex alterius detrimento fieri debet locupletior*: personne ne doit s'enrichir en lésant autrui:

[TRADUCTION] ... lorsqu'il existe deux ou plusieurs fonds, sur lesquels plusieurs créanciers peuvent faire valoir leurs droits et que, selon la common law, l'une des parties peut recourir à l'un ou l'autre fonds pour obtenir paiement alors que les autres ne peuvent recourir qu'à un seul, les tribunaux d'*equity* exercent leur pouvoir de procéder à une collocation (*to marshal*) à l'égard des fonds, et permettent ainsi aux parties dont les recours reconnus par la common law se limitent à un fonds de recevoir le juste paiement de leur créance. Le principe général en vertu duquel les tribunaux d'*equity* interviennent dans ces cas tient au fait que s'ils s'abstenaient d'intervenir, la personne qui a un titre sur les deux fonds aurait le pouvoir déraisonnable de léser les créanciers qui revendiquent un droit sur l'un ou l'autre fonds en réalisant sa sûreté sur l'autre, ce qui les exclurait. Ainsi, il serait en fait seul à décider s'ils doivent être payés ou non. Les tribunaux d'*equity* considèrent l'exercice d'un tel pouvoir comme totalement injuste et abusif; ils interviennent donc, non pas pour modifier ou annihiler ce pouvoir, mais pour empêcher qu'il soit utilisé de façon arbitraire, injuste ou dominatrice. L'*equity*, permettant une réparation en pareil cas, va à peine au-delà de l'application de la maxime *Nemo ex alterius detrimento fieri debet locupletior*.

Story note que le principe de la collocation en *equity* ne se limite pas à l'administration des biens, ou aux créanciers hypothécaires concurrents, mais s'applique en fait à toutes les sûretés doubles afin d'offrir une réparation équitable. Bien sûr, la jurisprudence et la doctrine émanant d'Angleterre qui considèrent la collocation comme un concept d'*equity* de portée étendue visant à permettre une réparation lorsque c'est nécessaire, notamment en faveur des parties à un contrat oral ou écrit, ne lient pas la Cour fédérale, mais elles sont convaincantes. Rien n'indique dans la jurisprudence antérieure établissant la portée de la doctrine de la collocation en *equity* que ce recours ne peut être exercé par les créanciers ordinaires en vertu d'un contrat. L'inverse est vrai. Pourtant, certains tribunaux canadiens ont semblé appliquer cette limite, dans certaines circonstances, dérogeant ainsi aux concepts d'*equity* et niant expressément aux créanciers

[20] Now it is the policy of courts to stand by applicable precedents, thus avoiding disturbing a point settled by a court of equal or superior jurisdiction. Thus parties can have some general certainty as to the law that ought to be applied when facts are similar. This doctrine, the doctrine of *stare decisis*, is one of policy. It should be departed from only when a departure is necessary to vindicate plain and obvious principles of law. This present dispute over the right to marshal is an issue on which current precedent ought not to be followed blindly, particularly given the law surrounding the equitable roots of marshalling. However the cases cited on behalf of the Bank of Scotland can also be dealt with in another way, by limiting them to their facts.

[21] The *Loonstra* case (*supra*) may be distinguished as the interest of the creditors, in that instance, through the mortgagor, that is, a pure *in personam* claim. In the present instance the creditors have an *in rem* interest. This rationalization does no violence to the original concept of marshalling, which clearly extended to contractual creditors, yet does not disturb either *Loonstra* or *Re Bread Man*, which is based on *Loonstra*.

[22] In deciding that Alfa Bunkering ought to have access to the commitment letter in order to explore marshalling I also take comfort in the approach taken by the Ontario Court of Appeal in its 27 February 1998 decision in *Allison (Re)* (1998), 38 O.R. (3d) 337. There the Court of Appeal agreed with the Trial Judge as to the outcome, but not on the basis that the doctrine of marshalling did not apply in favour of an unsecured creditor. The Court of Appeal refused to deal with this point because the debtors, found by the Trial Judge to be common debtors, were clearly not and to apply the doctrine of marshalling would have required one of them, the holder of a parcel of land,

ordinaires le droit à la collocation en *equity*, mais sans véritable motif, à mon avis.

[20] Les tribunaux ont pour politique de respecter les précédents applicables, évitant ainsi de remettre en cause une question déjà tranchée par un tribunal d'instance égale ou supérieure. Les parties peuvent donc savoir avec certitude, de façon générale, quelles règles de droit s'appliquent lorsque des faits similaires sont en cause. Cette doctrine, la doctrine du *stare decisis*, est une doctrine de principe. On ne peut y déroger que dans les cas où c'est nécessaire pour donner effet à des principes de droit clairs et évidents. Le présent litige concernant le droit à la collocation en *equity* porte sur une question qui ne doit pas être tranchée en suivant aveuglément les précédents existants, plus particulièrement au regard des règles de droit entourant les racines en *equity* de la collocation. Toutefois, il est possible de considérer différemment la jurisprudence citée au nom de la Banque d'Écosse, en la limitant aux faits en cause dans chaque cas.

[21] Il est possible de faire une distinction avec l'affaire *Loonstra* (précitée) quant à l'intérêt des créanciers, dans cette instance, par rapport au débiteur hypothécaire, qui était une créance purement personnelle. En l'espèce, les créanciers ont un intérêt réel. Cette rationalisation est compatible avec le concept initial de la collocation en *equity*, dont la portée s'étendait nettement aux créanciers en vertu d'un contrat, et ne remet pas en cause pour autant les décisions *Loonstra* ou *Re Bread Man*, cette dernière étant fondée sur la première.

[22] Pour décider qu'Alfa Bunkering devrait avoir accès à la lettre d'engagement pour examiner la possibilité d'une collocation en *equity*, je m'appuie en outre sur le raisonnement suivi par la Cour d'appel de l'Ontario dans son arrêt *Allison (Re)* (1998), 38 O.R. (3d) 337. Dans cet arrêt, la Cour d'appel partage l'opinion du juge de première instance quant au résultat, sans toutefois se fonder sur la thèse selon laquelle la doctrine de la collocation en *equity* ne s'applique pas à un créancier chirographaire. La Cour d'appel, à la page 341, a refusé d'examiner cette question parce que les débiteurs, qualifiés de débiteurs communs par le juge de première instance, ne l'étaient

to pay the debts of another debtor, the holder of another parcel of land: thus clearly marshalling did not apply for it was not intended to create such an inequity between two debtors. However, in touching on the doctrine of marshalling and particularly *Aldrich v. Cooper* (*supra*) the Court of Appeal was very careful to leave it open as to the nature of a creditor who might seek marshalling. The Court of Appeal, at page 341, summed up the *Aldrich* case by saying that marshalling is an equitable right to prevent a creditor, who may resort to two funds, from defeating another creditor who is limited to only one fund:

The right to marshal securities is an equitable one intended to prevent a creditor who can resort to two funds from defeating another creditor who can resort to only one of them.

In that paragraph the Court went on to discuss marshalling in terms of creditors. In the next paragraph, at page 342, the Court referred to two criteria to be met before marshalling might be applied:

The first criterion is that there must be a creditor or mortgagee who has access to two properties of a debtor to which he or she can resort for payment of the amount owing The second criterion is that there must be a creditor ranking behind or inferior to another creditor or mortgagee of a common debtor with a claim against one of the properties available to the superior creditor or mortgagee. Such an inferior creditor can invoke the assistance of equity to cause or marshal the superior creditor or mortgagee to satisfy the mortgage debt from the property against which the inferior creditor has no recourse so that the property will be available to the inferior creditor, or if this is impossible, or unfair to the superior creditor, equity may allow the inferior creditor to stand as the superior creditor in relation to the property against which the inferior creditor otherwise has no recourse.

Several points arise from this paragraph. First, the Ontario Court of Appeal makes it clear that

manifestement pas et parce que l'application de la doctrine de la collocation en *equity* aurait exigé que l'un deux, le détenteur d'un terrain, paie les dettes d'un autre débiteur, le détenteur d'un autre terrain: il était donc clair que la doctrine de la collocation en *equity* ne s'appliquait pas car il n'était pas conforme à son objet de créer pareille injustice entre les débiteurs. Cependant, en traitant de la doctrine de la collocation en *equity*, et plus particulièrement de l'arrêt *Aldrich v. Cooper* (précité), la Cour d'appel a pris grand soin de ne pas trancher la question de la nature du créancier qui peut réclamer une collocation en *equity*. La Cour d'appel, à la page 341, a résumé l'arrêt *Aldrich* en déclarant que la collocation était un droit en *equity* visant à empêcher un créancier, qui peut recourir à deux fonds, de faire échec à un autre créancier dont les droits se limitent à un seul fonds:

[TRADUCTION] Le droit de procéder à la collocation des sûretés est un droit en *equity* qui vise à empêcher un créancier qui peut recourir à deux fonds de faire échec aux droits d'un autre créancier qui ne peut recourir qu'à un seul d'entre eux.

Dans ce paragraphe, la Cour a poursuivi en discutant de la collocation sous l'angle des créanciers. Dans le paragraphe suivant, à la page 342, la Cour a mentionné les deux critères auxquels il faut satisfaire pour que la doctrine de la collocation en *equity* s'applique:

[TRADUCTION] Le premier critère veut qu'il existe un créancier ou un titulaire d'hypothèque qui a accès à deux biens du débiteur auxquels il peut recourir pour obtenir le paiement du montant qui lui est dû Le deuxième critère veut qu'il existe un créancier prenant rang après un autre créancier, notamment hypothécaire, d'un débiteur commun et que ce créancier de rang inférieur puisse exercer sa créance sur l'un des biens auxquels le créancier de rang supérieur a accès. Le créancier de rang inférieur peut avoir recours à l'*equity* pour obliger le créancier ou le titulaire d'une hypothèque de rang supérieur à procéder à la collocation pour obtenir le paiement de sa créance hypothécaire à l'aide du bien à l'égard duquel le créancier de rang inférieur n'a aucun recours afin que le bien demeure disponible pour le paiement de la créance de rang inférieur ou, si c'est impossible ou injuste envers le créancier de rang supérieur, l'*equity* peut permettre au créancier de rang inférieur de se substituer au créancier de rang supérieur relativement au bien à l'égard duquel le créancier de rang inférieur n'aurait autrement aucun recours.

Plusieurs points ressortent de ce paragraphe. Premièrement, la Cour d'appel de l'Ontario établit clairement

marshalling may be invoked against either a doubly secured creditor or mortgagee. Second, the Court of Appeal does not refer to an inferior mortgagee taking the benefit of marshalling, but rather only to a creditor ranking behind or inferior to another creditor or mortgagee of a common debtor. Third, that inferior creditor may take a benefit against a superior creditor or superior mortgagee. Fourth and finally, as an alternative, equity may allow the inferior creditor to stand as the superior creditor in relation to property against which the inferior creditor otherwise has no recourse. It is clear from all of this that the Ontario Court of Appeal, given the broad scope and long-standing of *Aldrich v. Cooper*, did not wish to be dragged into a consideration of whether *Aldrich v. Cooper* was wrongly decided, or whether the case improperly or incompletely stated the law in referring to the right of simple contract creditors, that is creditors by oral or written agreement, to stand in place of creditors by specialty, that is in place of creditors by deed. But the Ontario Court of Appeal, through its choice of words, supports the broad interpretation of marshalling set out in *Aldrich v. Cooper*.

CONCLUSION

[23] The cases referred to by counsel for the Bank of Scotland, assuming they are correct, merely deal with the right of *in personam* creditors, not with the right of *in rem* creditors and as such may be distinguished. However, going back to more basic case law, it is clear from *Aldrich v. Cooper* that unsecured creditors always had, in the past, a right to the benefit of marshalling. This is something which has been overlooked in the more recent Canadian cases concerned with the *in personam* right of creditors in real estate and in bankruptcy situations.

[24] I prefer the basic concept of marshalling set out in *Aldrich v. Cooper*, which the Court of Appeal in *Re*

que la collocation peut être réclamée contre un créancier ou le titulaire d'une hypothèque qui possède une double garantie. Deuxièmement, la Cour d'appel ne parle pas d'un titulaire d'hypothèque de rang inférieur qui bénéficierait de la collocation en *equity*, mais simplement d'un créancier prenant rang après un autre créancier, notamment hypothécaire, d'un débiteur commun. Troisièmement, ce créancier de rang inférieur peut se prévaloir d'un avantage contre le créancier ou le titulaire d'une hypothèque de rang supérieur. Enfin, quatrièmement, l'*equity* peut plutôt permettre au créancier de rang inférieur de se substituer au créancier de rang supérieur relativement au bien à l'égard duquel le créancier de rang inférieur n'aurait autrement aucun recours. Il ressort clairement de tous ces éléments que la Cour d'appel de l'Ontario ne souhaitait pas, compte tenu de la portée étendue et de l'ancienneté de l'arrêt *Aldrich v. Cooper*, être entraînée dans l'analyse de la question de savoir si cette décision était erronée, ni de celle de savoir si elle énonçait le droit de façon incorrecte ou incomplète, en mentionnant le droit des créanciers en vertu d'un contrat nu, c'est-à-dire des créanciers en vertu d'une entente verbale ou écrite, de se substituer aux créanciers en vertu d'un contrat formaliste, c'est-à-dire d'un contrat scellé. Mais, par le choix des termes qu'elle emploie, la Cour d'appel de l'Ontario appuie l'interprétation large de la collocation en *equity* qui a été donnée de l'arrêt *Aldrich v. Cooper*.

CONCLUSION

[23] En supposant qu'elle soit juste, la jurisprudence citée par l'avocat de la Banque d'Écosse traite simplement du droit des titulaires d'une créance personnelle, et non du droit des titulaires d'une créance réelle. Il est donc possible de distinguer cette jurisprudence à cet égard. Toutefois, si l'on remonte aux décisions plus fondamentales, il ressort clairement de l'arrêt *Aldrich v. Cooper* que les créanciers chirographaires ont toujours eu, par le passé, le droit de profiter de la collocation en *equity*. C'est un fait dont n'ont pas tenu compte les causes canadiennes les plus récentes touchant le droit personnel des créanciers dans le contexte du droit immobilier et du droit de la faillite.

[24] Je préfère le concept fondamental de la collocation en *equity* énoncé dans l'arrêt *Aldrich v. Cooper*,

Allison discussed at length, even though it was not interested in deciding the rights of unsecured creditors.

[25] The production of the commitment letter, which may well be pertinent and relevant, were the doctrine of marshalling to be applied, is not to be denied on the somewhat dubious proposition that marshalling cannot be applied in favour of mere *in rem* creditors.

[26] The Court will produce the commitment letter to the *in rem* claimants at the end of the period during which appeal of these reasons may be made or dispose of the commitment letter as ordered following any appeal. Costs shall be in the cause.

¹ The two ships are now named, respectively, *Seagull Harmony* and *Seagull Fame*, however for the purpose of these reasons I shall refer to both by their original names.

² *Commentaries on Equity Jurisprudence*, Honourable Mr. Justice Story, LL.D. 3rd English ed., by A. E. Randall, published 1920 by Sweet and Maxwell, London. While the original author was American the case law referred to is almost entirely English.

que la Cour d'appel a examiné en profondeur dans l'arrêt *Re Allison*, même si elle ne voulait pas trancher la question des droits des créanciers chirographaires.

[25] La production de la lettre d'engagement, qui pourrait bien s'avérer pertinente si l'on doit appliquer la doctrine de la collocation en *equity*, ne doit pas être refusée pour la raison quelque peu douteuse que la collocation en *equity* ne s'applique pas en faveur des simples titulaires d'une créance réelle.

[26] La Cour produira la lettre d'engagement aux créanciers titulaires d'un droit réel à la fin du délai imparti pour interjeter appel des présents motifs ou prendra, relativement à la lettre d'engagement, les mesures qui pourraient lui être imposées à la suite d'un appel. Les dépens suivront l'issue de l'instance.

¹ Les deux navires se nomment maintenant respectivement le *Seagull Harmony* et le *Seagull Fame*; toutefois, aux fins des présents motifs, je les désignerai par leur nom d'origine.

² *Commentaries on Equity Jurisprudence*, l'honorable juge Story, LL.D., 3^e édition anglaise par A. E. Randall, publié en 1920 par Sweet and Maxwell, Londres. Bien que l'auteur initial ait été américain, la jurisprudence qu'il mentionne est presque totalement anglaise.

TAB 11

Court of Queen's Bench of Alberta

Citation: Strategic Acquisition Corp. v Multus Investment Corporation, 2013 ABQB 534

Date: 20130923
Docket: 1301 02303
Registry: Calgary

Between:

Strategic Acquisition Corp.

Plaintiff

- and -

Multus Investment Corporation, Qualia Real Estate Investment Fund V Limited Partnership, Starke Capital Corp., Starke Dominion Ltd., Paragon Capital Corporation, 1680472 Alberta Ltd., John/Jane Doe 1 through 10, XYZ Corporation 1 through 10, ABC Partnership or Limited Partnership 1 through 10, and S.A. Backlin Professional Corporation

Defendants

**Reasons for Judgment
of the
Honourable Madam Justice C. A. Kent**

[1] Paragon Capital Corporation ("Paragon") applies for summary judgment on the claims made against it by Strategic Acquisition Corp. ("Strategic"). The central issue in this lawsuit is the enforceability by Strategic of a Right of First Refusal ("ROFR") against Multus Investment Corporation ("Multus") with respect to Dominion Place, an office tower in Calgary. Strategic says that Multus failed to advise Strategic of a change in the terms of an offer for the purchase of Dominion Place by the Starke group of companies ("Starke") with the result that the sale to Starke should be set aside and there should be specific performance of the sale of the property to Strategic, or damages.

[2] Starke obtained mortgage financing from Paragon. The original mortgage was granted in December 2011 and was registered against the title to Dominion Place. At the time of registration Strategic's ROFR was registered on title. A condition of granting the mortgage to Starke was that the ROFR must be discharged so that the Paragon mortgage would have priority. That was done. It was subsequent to the discharge that Strategic says that it discovered the facts which form the basis for this action. In addition to the December mortgage, Paragon provided further funding to Starke which was secured by mortgages against Dominion Place and two other properties, Plaza 14 and Franklin Crossing. Those two buildings are owned by affiliates of Starke.

[3] In its Amended Statement of Claim, Strategic's only allegation against Paragon was that the mortgages were never funded so that the registration of the mortgages was invalid. Strategic is satisfied now that the mortgages were funded so that non-funding is no longer in issue. However, in an Amended Amended Statement of Claim, Strategic alleges that Paragon had actual or constructive knowledge of the ROFR and the duty of good faith owed by Multus to Strategic, that Paragon knew or ought to have known that Multus breached the ROFR, that Paragon knew that the person who negotiated the mortgages on behalf of Starke was Mr. Chandran, who is also the directing mind of Multus, that the Strategic caveat protecting the ROFR was wrongfully discharged after the Paragon mortgage was registered, and that Paragon is prohibited from enforcing some of the mortgages against Dominion Place because of the doctrine of marshalling.

[4] There is no dispute about the test to be applied on this application. Paragon must show that there is no genuine issue to be tried. There is no onus on Strategic and if both parties provide admissible evidence on the motion, the court is permitted to consider all of the evidence to determine if there is a genuine issue to be tried: *Kwan v Superfly Inc.*, 2011 ABQB 343, 520 AR 234.

[5] There are essentially two issues that I must address: First, did Paragon have actual or constructive knowledge of the ROFR in such a manner that Paragon's mortgages are subject to the ROFR and secondly, what is the effect of the doctrine of marshalling?

Knowledge of the ROFR

[6] Paragon admits that it knew about the ROFR. However, it denies that it had any knowledge of the dealings between Starke and Multus. The ROFR was voluntarily discharged as part of the agreement between Paragon and Starke; Paragon had no involvement in obtaining the discharge from Strategic and since there is no allegation of fraud or conspiracy on the part of Paragon, its mortgage takes priority. Strategic says that because the ROFR caveat was wrongfully discharged, the interest created by the ROFR maintains its priority notwithstanding that it was discharged.

[7] This issue raises a question of priorities under the *Land Titles Act*, RSA 2000, c L-4. Paragon's position is simply that registration is everything. Once the ROFR caveat was discharged, it had priority. Strategic says, correctly, that discharge of an instrument protecting an interest in land does not destroy the interest. Depending on the circumstances, it may result in a loss of priority. However, on the facts of this case, Strategic says that it did not lose priority.

[8] To explain the issues, I refer to The Alberta Law Reform Institute Report, Proposals For a Land Recording and Registration Act For Alberta, October, 1993. It posits a fact situation similar to this case. Substituting in the parties in this case, the example reads as follows. Suppose that Multus, the owner of the land, has granted a legal interest to Strategic. Suppose further that Strategic recorded the interest; that the recording was subsisting at the time Paragon acquired a subsequent interest or at the time that Paragon recorded the subsequent interest, or at both times; that Strategic's recording was subsequently cancelled; and that Strategic's interest was not extinguished. In that situation, the report says that the *Land Titles Act* does not say specifically whether or not Strategic's interest continues to have priority over Paragon's interest despite the discharge of Strategic's caveat. The report notes that in *Boulter Waugh v Union Bank* (1919), 58 SCR 385, [Boulter Waugh], the Supreme Court held that a lapse of a caveat gave the subsequent interest-holder (Paragon in this case) priority. The report says that subsequent appellate cases have interpreted *Boulter Waugh* differently, some of which would support Paragon's position and some of which would support Strategic's position. The report then recommends an amendment, which has not been implemented, which would in this case, maintain the priority of Strategic, unless the subsequent encumbrancer (Paragon) could show that it believed that Strategic's interest was validly cancelled, it had no knowledge of the facts which made the cancellation invalid and must have detrimentally altered its position in reliance of the cancellation.

[9] Very shortly after that report was written, the Supreme Court decided *White Resources Management Ltd. v Durish*, [1995] 1 SCR 633, [Durish]. The issue in *Durish* was who had an interest in the mines and minerals underlying some land in Alberta. There were three chains of title and the facts are complex. The competing interests were a claim by D based on a caveat that was registered versus a claim by W through another chain. The title showed a caveat by H, from whom D acquired its interest, a caveat by W, and then a caveat by D which claimed its interest through an assignment of H's interest. W claimed its interest through another caveat placed by V which was registered prior in time to the H caveat, but had lapsed. McLachlin, J. (as she then was), writing for the court, found that *Boulter Waugh* applied so that the lapse of the caveat resulted in the loss of priority of the underlying interest.

[10] Strategic argues that *Durish* only applies when there is no wrongdoing by any party. Here, Multus improperly and possibly fraudulently transferred the property to defeat Strategic's interest to the benefit of others, including Paragon who is allegedly innocent. However, Strategic says that Paragon had constructive knowledge of Multus' wrongdoing because it knew about the ROFR, it knew about the terms of the agreement between Multus and Starke and it knew that

Chandran was the directing and controlling mind of both Starke and Multus. Strategic relies upon *McFarland v Hauser*, [1979] 1 SCR 337 [*McFarland*] for the proposition that knowledge at this level does not defeat Strategic's priority. In *McFarland* Hauser had a lease on McFarland's land. The lease contained an option to purchase. A third party, Sunderland, made an offer to purchase the land. Sunderland obtained an option to purchase that was subject to the McFarland lease. The caveat protecting the McFarland lease lapsed because McFarland failed to register a *lis pendens* against the title. The court held that because Sunderland's option was subject to McFarland's option, the lapse of the McFarland caveat did not give Sunderland priority.

[11] Those facts are different than this case. The Paragon mortgage did not state that it was subject to the ROFR and, indeed, one of the conditions for Paragon funding the mortgage was the discharge of the ROFR caveat. The knowledge that Paragon had is not sufficient to distinguish it from *Boulter Waugh* and *Durish*.

[12] This is a summary judgment application. The onus on Paragon is high. Based on the authorities referred to above, Paragon's knowledge of the ROFR and its terms is not sufficient to defeat its priority. If that is all that Strategic could prove, there would be no genuine issue to be tried. Strategic says that a judge at trial could infer that Paragon knew more, essentially that it knew that Multus and Starke were acting in breach of Strategic's ROFR. That takes me to the decision in *Holt, Renfrew & Co. v Henry Singer Ltd.*, 37 AR 90, [1982] AJ No 726 (ABCA) [*Holt, Renfrew*]. Much as the dissent in that case is compelling, if the knowledge and actions in *Holt, Renfrew* are not fraud in the context of land titles principles as the majority found, the facts against Paragon are certainly not. Moreover, Strategic has not pled fraud against Paragon. Without that plea, there is no genuine issue to be tried. There will be summary judgment on that portion of the claim.

Marshalling

[13] The principle of marshalling is straightforward. Where there are two creditors of the same debtor and one of those creditors has the ability to recover from two funds of the debtor and the other creditor only has resort to one, the court will marshal the funds to pay out both creditors as much as possible. A first mortgagee, however, cannot be prejudiced by marshalling: *Snell's Principles of Equity*, 28th ed, at 416, cited in *First Investors Corp. v Veeradon Developments Ltd*, 47 DLR (4th) 446, 84 AR 364 at para 11 (ABCA).

[14] There is nothing in the doctrine that says that both creditors must be secured or mortgagees and there is nothing that says that it only operates where there is one debtor rather than related debtors. There is nothing in the evidence before me that shows that Paragon will be prejudiced in recovering on the mortgages at issue if the funds are marshalled. It may be, but it may not. The evidence is simply not before me. Accordingly, the plea of marshalling is not

struck. However, since it is essentially a remedy if Strategic's claims against Multus and Starke are proven, this claim may well be dealt with at the end of the trial.

Heard on the 28th day of August, 2013.

Dated at Calgary, Alberta this 23rd day of September, 2013.

C. A. Kent
J.C.Q.B.A.

Appearances:

Sean S. Smyth and Laurie A. Baptiste
McCarthy Tétrault LLP
for the Plaintiff Strategic Acquisition Corp.

Kenneth T. Lenz
Bennett Jones LLP
for the Defendant Multus Investment Corporation and Qualia Real Estate Investment
Fund V Limited Partnership

Suzanne M. Porteous and Natalie L. Climenhaga
Carscallen LLP
for the Defendants Starke Capital Corp. and Starke Dominion Ltd.

Judy Burke and Derek Nash
Demiantschuk Lequier Burke & Hoffinger LLP
for the Defendant Paragon Capital Corporation

TAB 12



**IN THE SUPREME COURT OF NEWFOUNDLAND AND LABRADOR
GENERAL DIVISION**

Citation: *Bear Creek Contracting Ltd. v. Canadian Western Bank*, 2026 NLSC 13

Date: February 09, 2026

Docket: 202201G0266

BETWEEN:

BEAR CREEK CONTRACTING LTD.

APPLICANT

AND:

CANADIAN WESTERN BANK

FIRST RESPONDENT

AND:

BANK OF MONTREAL

SECOND RESPONDENT

AND:

**MNP LTD., IN ITS CAPACITY AS
RECEIVER OF UNIVERSAL
HELICOPTERS NEWFOUNDLAND
AND LABRADOR LP, 70703
NEWFOUNDLAND AND LABRADOR
INC., UNIVERSAL HELICOPTERS
HOLDINGS LP, 81924
NEWFOUNDLAND AND LABRADOR
INC., LAKELSE HELICOPTERS
LIMITED PARTNERSHIP, LAKELSE
AIR LTD. AND 1167527 B.C. LTD.**

THIRD RESPONDENT

AND:

**PRICEWATERHOUSECOOPERS LLP,
IN ITS CAPACITY AS TRUSTEE IN
BANKRUPTCY OF UNIVERSAL
HELICOPTERS NEWFOUNDLAND
AND LABRADOR LP, 70703**

**NEWFOUNDLAND AND LABRADOR
INC., UNIVERSAL HELICOPTERS
HOLDINGS LP, AND 81924
NEWFOUNDLAND AND LABRADOR
INC.**

FOURTH RESPONDENT

Before: Justice Garrett A. Handrigan

Place of Hearing: St. John's, Newfoundland and Labrador

Date of Hearing: January 16, 2026

Summary:

Bear Creek applied to Court for an order directing that surplus funds held by MNP, Receiver of the Universal Group, be marshalled and paid to Bear Creek by subrogation. PwC, the Trustee in Bankruptcy of the Universal Group, opposed Bear Creek's Application, claiming that the Universal Group's unsecured creditors would be materially prejudiced if Bear Creek received the funds.

PwC also claimed that marshalling should not be allowed since the funds were held by MNP, on behalf of the Universal Group, and the Canadian Western Bank was a creditor of Lakelse, not of the Universal Group. Thus, said PwC the conditions were not present for marshalling: while there were two separate creditors, the Bank and Bear Creek, there were also two separate debtors, the Universal Group and Lakelse; and Bear Creek is a creditor of Lakelse, but not of the Universal Group.

The Court found:

1. The Universal Group and Lakelse are the same entity, operating as the Universal Group;
2. The Bank and Bear Creek are separate creditors of the Universal Group;

3. The Universal Group is a single debtor of the Bank and Bear Creek;
4. Bear Creek's claim to the surplus funds, as a secured creditor, is superior to the Universal Group's unsecured creditors' claims;
5. It is fair and equitable to allow Bear Creek to satisfy the debt from the surplus funds that MNP holds for the Universal Group; and
6. Bear Creek is subrogated to the Universal Group for the surplus funds.

Appearances:

Joshua J. Santimaw	Appearing on behalf of the Applicant
No Appearance	On behalf of the First Respondent
No Appearance	On behalf of the Second Respondent
John C. Taylor-Hood	Appearing on behalf of the Third Respondent
Christopher D.J. Isnor	Appearing on behalf of the Fourth Respondent

Authorities Cited:

CASES CONSIDERED: *Bear Creek Contracting Ltd v. Canadian Western Bank*, 2024 NLSC 92; *Wolfe et al v. Taylor et al*, 2020 MBCA 44; *Williamson v. Loonstra* (1973), 34 D.L.R. (3d) 275, 1973 CarswellBC 291(S.C.); *Bread Man Inc., Re*, (1978) 21 O.R. (2d) 59, 89 D.L.R. (3d) 599 (S.C.);

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

TEXTS CONSIDERED: Elizabeth Portman, *Canadian Encyclopedic Digest, Equity* (N.p.: Thomson Reuters, 2024) at section 11

REASONS FOR JUDGMENT

HANDRIGAN, J.:

INTRODUCTION

[1] On January 19, 2022 Bear Creek Contracting Ltd. (“Bear Creek”) applied to this Court by Originating Application for orders “piercing” the Universal Group’s “corporate veil” so it could proceed against the Universal Group of companies. Bear Creek also asked the Court to “marshal” the assets of the Universal Group to allow Bear Creek to recover from those assets, as a subrogate of the Universal Group. This arose when the Universal Group went bankrupt and the Canadian Western Bank, its major secured creditor, exhausted all of Lakelse’s assets and left nothing from which Bear Creek could recover its debt.

[2] MacDonald, J. of this Court dealt with Bear Creek’s first request for relief, piercing the corporate veil of the Universal Group. He filed his judgment on June 20, 2024 in *Bear Creek Contracting Ltd v. Canadian Western Bank*, 2024 NLSC 92. At paragraph 45, MacDonald, J. refused Bear Creek leave to sue the Bank: “I will not lift the stay to allow Bear Creek to sue Universal to pierce the corporate veil”. However, at paragraph 67, MacDonald, J. did lift the stay to “allow Bear Creek to seek recovery from Universal of the Surplus Funds [that remained after the Trustee in Bankruptcy of the Universal Group paid all of Universal creditors] based on the principles of subrogation and marshalling”. [emphasis added]

[3] Then, in my turn, I heard the second part of Bear Creek’s Application on January 16, 2026, dealing with the subrogation and marshalling issue and reserved my judgment on it until now.

THE ISSUE

[4] May Bear Creek invoke the principles of marshalling and subrogation to recover its unpaid debt from the Universal Group?

The Law

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

- [5] Section 69.3 (1) provides:

69.3 (1) Subject to...[section] 69.4..., on the bankruptcy of any debtor, no creditor has any remedy against the debtor or the debtor's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy.

- [6] Section 69.4 provides:

69.4 A creditor who is affected by the operation of sections 69 to 69.31...may apply to the court for a declaration that those sections no longer operate in respect of that creditor or person, and the court may make such a declaration, subject to any qualifications that the court considers proper, if it is satisfied

(a) that the creditor or person is likely to be materially prejudiced by the continued operation of those sections; or

(b) that it is equitable on other grounds to make such a declaration.
These sections do not relate directly to the issue I am dealing with on this application but they are noteworthy nonetheless, because they undergird the discretion that Bear Creek asks me to exercise on its behalf.

Case Law - *Marshalling*

- [7] The Manitoba Court of Appeal discussed “marshalling” in *Wolfe et al v. Taylor et al*, 2020 MBCA 44 and described it in paragraph 31 as “an equitable remedy, intended to protect the recovery of a junior creditor against the arbitrary action of a senior creditor, and to thereby treat all secured creditors equitably”.

[8] The Court of Appeal also acknowledged “[o]ne of the most recognised statements of the doctrine was set out by Lord Eldon in *Aldrich v. Cooper* (1803), 8 Ves. Jr. 382, 32 E.R. 402 (Eng. Ch. Div.)) (at p 407):

... a person having two funds shall not by his election disappoint the party having only one fund; and equity, to satisfy both, will throw him, who has two funds, upon that, which can be affected by him only; to the intent that the only fund, to which the other has access may remain clear to him” (paragraph 32, *Wolfe et al v. Taylor et al*).

[9] The Court of Appeal elaborated:

[33] To obtain marshalling, certain specific criteria must be met. These criteria include the requirements that: two or more creditors share a *single common debtor*; and the senior creditor has a claim against two of the debtor's funds, while the junior creditor, ranking behind the doubly secured senior creditor, has recourse to only one.

[emphasis in original]

[10] Then the Court also noted that there are “bars to marshalling”:

[38] Jurisprudence recognises bars to marshalling. The first one is that marshalling will not be permitted if it would interfere with the superior right of a secured creditor to pursue its remedy against either of the two funds. The other bar, for our purposes, is that the doctrine is applicable unless it causes prejudice to a third party. Potential prejudice to unsecured creditors is irrelevant....

[11] In *Wolfe*, the Manitoba Court of Appeal cited *Williamson v. Loonstra* (1973), 34 D.L.R. (3d) 275, 1973 CarswellBC 291(S.C.) to support its statement that marshalling is unavailable to “unsecured creditors”. It noted the following at paragraph 12 of *Williamson*, which is pertinent to these presents:

... The doctrine does not extend to all creditors of every degree, it does not apply in favour of an unsecured creditor and it does not apply in favour of a judgment creditor unless he has obtained a charge on the estate that he seeks to have marshalled in his favour....

[12] Kay, J. of the Ontario Superior Court, in Bankruptcy, considered *Williamson in Bread Man Inc., Re*, (1978) 21 O.R. (2d) 59, 89 D.L.R. (3d) 599 (S.C.) and offered this rationale, in paragraph 17 of the judgment, for why unsecured creditors should not be permitted to marshal:

... It is also logical that unsecured creditors of debtors should not be protected, for, in the absence of a statutory provision, they should have no better right to the fund than the debtor himself. ...

[emphasis added]

[13] Finally, I note that McDonald, J. of this Court, also discussed “marshalling” at paragraphs 50 and 51 of the judgment he filed on June 24, 2024 in the related matter to the current Application:

[50] The doctrine of marshalling is described in *Ernst Bros. Co. v. Canada Permanent Mortgage Corp.* (1920), 48 O.L.R. 407, 57 D.L.R. 500 (C.A.).

[51] The court says, “It is a settled principle of law that where there are two funds to which, or to either of which, as he may elect, a creditor may resort, and there is another creditor who is entitled to resort to only one of the funds, the latter has the right to require the former creditor first to exhaust the fund on which the latter has no claim”.

Online Digest – Subrogation

[14] The *Canadian Encyclopedic Digest*, under the heading, *CED Equity § 11, Subrogation*, describes “subrogation” thus:

Subrogation means the substitution of one person in the place of another for a legal claim, so that the person substituted succeeds to the rights of the other in relation to the claim. The principle of subrogation is an equitable one merely, and will be carried out in the exercise of a proper discretion with due regard to the legal and equitable rights of others. It was invented as a means of avoiding injustice by conferring on a person not previously entitled to sue in law or equity a status to assert against a person or property a claim recognized as fair and just but which is not maintainable in contract or tort.

[15] This is the law I will apply to the issue I stated above. I turn now to analyze that issue, starting with the background to it.

ANALYSIS

Background

[16] On December 3, 2024, Bear Creek filed an Interlocutory Application in these proceedings asking for an “order pursuant to the principles of marshalling and subrogation to require PriceWaterHouseCoopers LLP (“PwC”) to pay the surplus proceeds [that remained after the Trustee in Bankruptcy of the Universal Group paid all of Universal Group’s creditors] to Bear Creek and costs”. Ian Munson who lives in Terrace, BC is a businessman and the President and sole Director of Bear Creek.

[17] Bear Creek set out the “Material Facts” in paragraph 2 of its Application, supported by Mr. Munson’s affidavit, saying that “... [he had] personal knowledge of the facts contained therein and they are true to the best of my knowledge, information and belief”. Bear Creek’s Application runs to five pages and some 40 paragraphs. I summarize, in bullet form, the facts that are needed to understand my decision, as they appear in Bear Creek’s Application:

- “Universal Helicopters” is comprised of two partnerships, #70703 (formed from Universal Helicopters LP and 70703 NL Inc) and #81924 (formed from Universal Holdings LP and 81924 NL Inc) and is known by that name;
- “Lakelse Partnership” is comprised of Lakelse LP, 1167537 B.C. Ltd. and Lakelse Air and is known as “Lakelse”;
- Universal Helicopters and Lakelse together are known as “Universal Group”;
- Universal Group is fully integrated and additionally, Lakelse LP is wholly owned by Universal Helicopters LP, which, in turn, is wholly owned by Universal Holdings LP;

- The ultimate owners of all of the entities named in the previous bullets are also the same, being two Trusts and a Fund;
- All entities that form the Universal Group have the same directors, and Shane Cyr is President and CEO of all of them, and is also the acknowledged “directing mind” of the Group;
- The Group’s financial statements were consolidated and all banking decisions were made by the officers of the Universal Group;
- In 2017 Universal Helicopters borrowed \$8.5 million from the Canadian Western Bank (the “Bank”) to refinance existing debt and the Bank secured the debt with a first charge on Universal Helicopters’ fleet of helicopters and other assets;
- In 2018 Universal Helicopters formed Lakelse Partnership to acquire 12 aircraft and two helicopter base properties from Lakelse Air, whose shares were owned by Bear Creek;
- Bear Creek concluded the Lakelse Acquisition with a Purchase Agreement on August 31, 2018, in which Universal Helicopters agreed to pay Bear Creek \$14.25 million for the Lakelse Assets, Shares and Business;
- The Bank provided financing totalling \$11 million, to the Universal Group for the Lakelse Acquisition;
- The Bank took security over all of Lakelse’s present and after-acquired property and all entities of the Universal Group fully guaranteed the financing and signed cross-default agreements;
- The President and CEO of the Universal Group signed off on all commitment letters and loan documents on behalf of the Universal Group;
- The Lakelse Acquisition was partly financed by a \$2.5 million promissory note that Lakelse LP issued to Bear Creek and the Universal Group gave Bear Creek a security interest in the Lakelse Assets to support the promissory note;

- Bear Creek, the Bank and Lakelse entered into an Intercreditor Agreement in September 2018 by which Bear Creek subordinated both its Promissory Note and its security in the assets to the loans that the Bank extended to Bear Creek for the Purchase;
- The Intercreditor Agreement also provided that the first \$10 million recovered under the Bank's General Security Agreements would go to the Bank and the next \$2.5 million would go to Bear Creek;
- In June 2019, the Bank, without informing Bear Creek, issued a further "loan facility" to Lakelse, for which the Universal Group confirmed that all of the security the Universal Group extended to the Bank for the initial loan would apply to the new facility;
- In May 2020 the Universal Group defaulted on both loans with the Bank and the Bank appointed MNP as receiver of the assets of Universal Helicopters and Lakelse;
- MNP took possession of the Universal Group's assets and, with Court approval, sold the assets off by March 2021, realizing \$18.88 million from the sale of the aircraft alone;
- Lakelse Partnership made an assignment in bankruptcy in January 2022, declaring total debt of \$7.3 million dollars, of which it owed \$2.5 million to Bear Creek and \$1.3 million to the Bank;
- On March 5, 2024, Bear Creek filed an affidavit dated December 13, 2021, from Wayne Horachek, Associate VP of Credit Risk Management at the Bank in which he declared at paragraph 10 "...the receivership of the Universal Group has resulted in an anticipated shortfall...owing by the Lakelse Entities to CWM [the Bank] of approximately \$790,407.03, and anticipated surplus...[on] the obligations owing by the Universal Entities to CWB of between approximately \$1,564,000 and \$2,303,000. After allocating certain surplus realization proceeds from the Universal Entities to compensate for the shortfall of realization proceeds from the Lakelse Entities, I anticipate that the remaining total net surplus of realization proceeds from the Universal Entities will be between approximately \$775,592.97 and \$1,512,592.97";

- In the result, because of the Lakelse Purchase Loans for \$11 million dollars and the 2019 Loan for \$1.7 million that the Bank had extended to the Universal Group, Bear Creek could not recover any of the debt that Lakelse owed to it from the proceeds of the Lakelse receivership;
- There was, however, a surplus from the sale of the Universal Helicopter's assets after the amount owing by Universal Helicopters was paid to the Bank and Bear Creek is looking for that surplus;
- MNP holds the surplus funds; and
- PwC, which represents Universal Group's unsecured creditors opposes Bear Creek's Application and says that marshalling will prejudice the unsecured creditors if Bear Creek is allowed to collect its debt before them.

[18] This is the background to the Application. I turn now to discuss the issue stated earlier.

DISCUSSION

[19] In *Wolfe*, the Manitoba Court of Appeal stated the criteria that a creditor claiming the benefit of marshalling must establish. While I set out the quotation earlier in these reasons, I repeat it here for ease of reference:

[33] To obtain marshalling, certain specific criteria must be met. These criteria include the requirements that: two or more creditors share a *single common debtor*; and the senior creditor has a claim against two of the debtor's funds, while the junior creditor, ranking behind the doubly secured senior creditor, has recourse to only one.

[emphasis in original]

Two Creditors?

[20] It is self-evident that there are two creditors here: Bear Creek and the Canadian Western Bank. The Bank loaned the Universal Group \$8.5 million in November 2017 to refinance some of its existing debt and Universal Group gave the Bank a first charge on its fleet of helicopters and other assets to secure that loan.

[21] The Bank provided further financing of \$11 million to the Universal Group for the Lakelse Acquisition in August 2018. The Bank took security over all of Lakelse's present and after-acquired property, and all members of the Universal Group guaranteed the financing fully and signed cross-default agreements.

[22] Then in June 2019, the Bank extended a third loan to the Universal Group for which the Universal Group confirmed that all of the security the Universal Group gave to the Bank for the initial loan would apply to the new facility. All three loans were still outstanding when the Bank appointed MNP as receiver of the Universal Group's assets in May 2020.

[23] At that time, as indicated in paragraph 34 of Bear Creek's Interlocutory Application, these were the amounts that the Universal Group owed:

Creditor	The Debt	Amount Owing
The Bank	2017 Loan	\$7,600,000
The Bank	2018 Loan	\$10,450,000
Bear Creek	2018 Promissory Note	\$2,500,000
The Bank	2019 Loan	\$1,700,000
Total:		\$22,250,000

[24] Bear Creek noted that the 2018 loan should be apportioned between Universal Group and Lakelse in amounts of \$3.8 million and \$6.65 million respectively. It also noted in paragraph 39 of its Application that MNP “[a]s of March 19, 2021...had received proceeds of about \$18.88 million from the sale of Universal Group aircraft alone. The Applicant [Bear Creek] believes that MNP had also received substantial additional proceeds from sales of other Universal Group assets”.

2. One Debtor?

[25] While it is, as I noted above, self-evident that there are two creditors, it is not so obvious that there is a “single common debtor”. Nonetheless, I am satisfied that for marshalling in this proceeding, there is a single debtor, whose distinct status emerges organically from the relationship between the Universal Group and the Lakelse; as will appear below.

[26] There are several aspects to that relationship which require closer scrutiny and they are: the emergence of the Universal Group; the Universal Group’s acquisition of the Bear Creek assets; and the disposition of the Universal Group’s assets.

[27] I use the designation “Universal Group” deliberately here, referring to the constellation of entities that form part of it:

- Universal Helicopters Newfoundland and Labrador LP; 70703 Newfoundland and Labrador Inc, which is the general partner of Universal Helicopters LP;
- Universal Holdings LP;
- 81924 Newfoundland and Labrador Inc., which is the general partner of Universal Holdings LP;
- Lakelse Helicopters Limited Partnership; 1167537 B.C. Ltd., which is the general partner of Lakelse LP; and

- Lakelse Air Ltd, the shares of which are owned by the Lakelse Partnership.

[28] I noted earlier in these reasons, that the 81924 and 70703 Partnerships were generally referred to as “Universal Helicopters”; that the Lakelse Partnership and Lakelse Air were referred to as Lakelse; and that Universal Helicopters and Lakelse were referred to, together as the “Universal Group”.

- All of these companies shared common management and ownership control;
- Universal Helicopters LP wholly owned Lakelse LP and Universal Holdings LP;
- Labrador Inuit Capital Strategy Trust and the Tasiujatsoak Trust and the CAPE Fund LP owned Universal Holdings LP, Universal Helicopters LP and Lakelse LP.
- The directors of each of the corporate entities in the Universal Group were the same;
- All executive decisions that each of the corporate entities in the Universal Group took, issued from its head office in Goose Bay, NL or its corporate office in St. John’s, NL;
- Shane Cyr was the President and CEO of all of the corporate entities in the Universal Group, as well as their directing mind. Mr. Cyr made all major decisions related to the day-to-day management and overall operations of the corporate entities, including taking on debt; and negotiating credit facilities and loans. Mr. Cyr treated all corporate entities as one group and he presented himself as the CEO of the Universal Group to everyone who interacted with the Group and its entities;
- The financial statements of the Universal Group were prepared on a consolidated basis; and
- All decisions regarding the transfer of funds to and from operating bank accounts within the Universal Group were made by officers of the Universal Group.

[29] I drew the preceding information from paragraphs 6-13 of the Originating Application that Bear Creek filed on January 19, 2025. As to that information, it is replicated and verified in an affidavit that Ted Howell, who was the Chief Financial Officer of Universal Helicopters Newfoundland and Labrador LP from June 2017 to March 2019, filed to support the Originating Application.

[30] Further, I refer again to an affidavit that I quoted from earlier in these reasons from Wayne Horachek, the Associate Vice-President-Credit Risk Management of Canadian Western Bank. Mr. Horachek presented as "...the senior member of CWB [the Bank] for managing CWB's recovery and realization efforts in respect of various loans advanced by CWB to Lakelse Helicopters Limited Partnership, 1167537 B.C. Ltd., Lakelse Air Ltd. (collectively, the "**Lakelse Entities**"), and Universal Helicopters Newfoundland and Labrador LP, 70703 Newfoundland and Labrador Inc., and 81924 Newfoundland and Labrador Inc. (collectively, the "**Universal Entities**", and together with the Lakelse Entities, the "**Universal Group**")".

[31] Mr. Horachek, like Mr. Howell replicates and verifies the information provided in the Originating Application. Mr. Horachek also stated how the aggregate collectivity of the Universal Group dictated the Bank's posture towards the Universal Group as a borrower:

8. Because the Universal Group acted as a single economic unit, CWB [the Bank] required, among other things, that all obligations of Universal Entities and Lakelse Entities be cross-guaranteed, and that each entity comprising the Universal Group grant security over all present and after-acquired personal property for the payment of all obligations to CWB under the Purchase Loans and the subsequent 2019 Loan. I confirm that, in the course of CWB's [the Bank's] credit evaluation and approval process in deciding to advance the Purchase Loans, 2019 Loan, and any other credit facilities to the Universal Group entities, CWB treated the Universal Group as a single, consolidated economic entity.

[emphasis added]

[32] Ian Munson, the President and sole Director of Bear Creek also reflected on the Universal Group's status in the affidavit that he filed in support of Bear Creek's

Interlocutory Application. This, from paragraphs 6 and 7 of that affidavit on the “Ownership and Management of the Universal Group”, is relevant:

6. As far as I was concerned, as a businessperson, “Universal” was a helicopter company based in Goose Bay, Newfoundland and Labrador. It has one set of directors and officers, with Shane Cyr at the top. I did not concern myself, particularly, with the intricacies of the corporate structure of the Universal Group. As far as I was concerned, I was dealing with “Universal”.

7. As far as I was concerned, Universal was purchasing the Lakelse Assets to add them to, and operate them as part of, the Universal Group.

[33] I find on this evidence and, for the purposes of this Application, that the Universal Group and all of its corporate entities are a single debtor to the two creditors, the Canadian Western Bank and Bear Creek Contracting Ltd. I find further, on the same evidence, that the Bank and Bear Creek are “senior” and “junior” creditors respectively of the Universal Group.

[34] I need also inquire if there any “bars to marshalling” as the Manitoba Court of Appeal contemplated in *Wolfe*, when it suggested two potential bars to consider: 1. Would it interfere with the rights of the senior creditor; or 2. Would it cause prejudice to a third party.

1. Interfering with Senior Creditor

[35] If I marshal Universal Group’s assets to apply surplus proceeds that MNP holds for the Universal Group to Bear Creek’s debt that will not interfere with the Bank as senior creditor. Quite simply, the Bank has already recovered all of the money that the Universal Group owed to it and is no longer involved in the Universal receivership.

2. Prejudice to Third Party

[36] This potential bar is more contentious and requires closer consideration.

[37] PwC was appointed Trustee in Bankruptcy of the Universal Group on June 15, 2021. MNP was appointed Receiver of the Universal Group on May 27, 2020 and sold the assets of the Universal Group, with Court approval on October 30, 2020. Both events happened before PwC was appointed Trustee.

[38] PwC filed a written submission opposing Bear Creek's Interlocutory Application for marshalling and subrogation. It noted that MNP still holds the surplus funds from the sale of the Universal Group's assets but it says that I should deny Bear Creek the relief that it is seeking.

[39] These are the bases that PwC relies on for its opposition:

- i. Bear Creek did not seek marshalling when MNP sold the assets;
- ii. Universal Group and Lakelse are separate and distinct entities and the creditors of one are not creditors of the other, so that Bear Creek is not a creditor of Universal Group; and
- iii. To allow Bear Creek marshalling will materially prejudice Lakelse's unsecured creditors and Bear Creek can only succeed if it proves that its prejudice will exceed any prejudice to the unsecured creditors.

[40] I will examine each of these submissions in its turn.

i. Bear Creek Failed to Seek Marshalling

[41] I do not know if Bear Creek sought marshalling previously. In paragraph 19(a) of its written submission, PwC submits that "Bear Creek had ample opportunity to make this Application and it failed to do so until after the assets were sold". That may be true, although PwC has offered no evidence to support its submission and it was not engaged in the process when MNP sold off the Universal Group's assets.

[42] In any event, the relief that Bear Creek is asking for is equitable in nature and it is fairer to decide the question on the equities in play, than if Bear Creek simply passed on its chance at marshalling at a more opportune time. I expect that the Universal receivership was a dynamic process and that it ushered in an unsettling time for all involved, whereupon it may have been difficult for Bear Creek to focus on the nuances of marshalling and subrogation and assert them then, as it does now.

ii. Universal Group and Lakelse as Separate Entities

[43] I dealt with this argument earlier in these reasons and need not repeat that discussion here. I regard the Universal Group as a tightly cohesive unit, whose operations were so inextricably entwined that even the Bank, its biggest creditor, regarded it as one entity.

iii. Material Prejudice to Unsecured Creditors

[44] I will not deal with this concern by simply saying, as the Manitoba Court of Appeal did in *Wolfe* that “[p]otential prejudice to unsecured creditors is irrelevant”. Indeed, I note as my colleague, MacDonald, J. did in paragraph 64 of *Bear Creek*, the companion piece to this matter, that “Bear Creek will have to satisfy a court that:...(d)...it is materially prejudiced more than other creditors, including Universal’s unsecured ones...”?

[45] Counsel for PwC advised me when I heard Bear Creek’s Application that \$2,595,886 is owed to the unsecured creditors of the Universal Group, while \$2,500,000 is owed to Bear Creek; or put another way for the Bear Creek debt, the Universal Group still owes the full amount of the Promissory Note that Bear Creek took back from the Universal Group to finalize the transaction between them. Doubtlessly, the unsecured creditors of the Universal Group will suffer material prejudice from Universal Group’s bankruptcy. But Bear Creek will suffer greater prejudice. In either event, the surplus funds that MNP holds was estimated for me at the hearing as between \$350,000-\$400,000.

[46] Ian Munson, President and sole Director of Bear Creek, to whom I referred earlier in these reasons, filed an affidavit to support Bear Creek's Interlocutory Application. At paragraph 16, he agreed that Bear Creek "...did receive interest payments [on the Promissory Note] of about \$244,000 between September 2018 and March 2020", but "[t]he balance of the purchase price (\$2,500,000) has never been paid". In the same affidavit, Mr. Munson also reflected on the impact that the Universal Group's default had on Bear Creek's business:

28 As a result of the non-payment of the \$2.5 million in principal owing and secured by the Promissory Note, together with accumulated interest, Bear Creek has been unable to refinance at favourable rates and has been unable to pay down other existing debts, which has caused ongoing and significant expense to Bear Creek".

[47] When Bear Creek took back the Promissory Note for \$2.5 million from the Universal Group, it became as one of the Universal Group's "secured creditors", as section 8 of the Promissory Note, dated September 6, 2018 shows:

7. Security

As general and continuing security for the due performance and payment of any and all of its obligations to the Holder [Bear Creek] of this Note, the Maker [Lakelse Helicopters LP] has granted a security interest in the Aircraft pursuant to a security agreement dated as of the date hereof".

[emphasis added]

[48] There were, in fact, two security agreements which Bear Creek was a party to with the Universal Group, the first a "General Security Agreement" ("GSA") and the other an "Aircraft Security Agreement" ("ASA"), both dated September 8, 2018, and each concurrent with and in support of the Promissory Note. The GSA gave Bear Creek security over "...all of the Debtor's present and after acquired property" and the ASA gave Bear Creek security over "...the aircraft described in Schedule "A"", of which the list included twelve helicopters and one "Rotable (spare SD2 engine)". The GSA appears as Exhibit "C" to Ian Munson's affidavit and the ASA as Exhibit "D".

[49] The Bank required that Bear Creek and Lakelse Helicopters LP subordinate their claims to the Bank's interest in the assets listed in Schedule "A", which it took to secure the money that the Universal Group owed to it. To that end, the Bank insisted that Bear Creek, and Lakelse Helicopters LP enter into an "Intercreditor Agreement" dated September 6, 2018 with it. The Bank designated Bear Creek in the Agreement as "Subordinate Lender" (reminiscent of my finding that Bear Creek was a "junior" creditor to the Bank) and referred to the two Lakelse entities as "Borrower" and "Indemnitor".

[50] Clause G of the Intercreditor Agreement states the status of the Borrower and Indemnitor to the Bank's security:

G. It is a condition, among others, of the Bank's willingness to extend the Credit Facilities to the Borrower that the Subordinate Lender [the Bank], the Indemnitor and Borrower [the Lakelse entities] execute and deliver this Intercreditor Agreement pursuant to which the Subordinate Security [held by Bear Creek] will at all times be postponed and subordinate to the Bank Security.

[emphasis added]

[51] By this clause the Bank acknowledged unequivocally that Bear Creek held a security interest in the assets it acquired from the Universal Group, subject only, of course, to the Bank's claim.

[52] Earlier in these reasons, I quoted from Kay, J. of the Ontario Superior Court, in Bankruptcy, in *Bread Man*:

...It is also logical that unsecured creditors of debtors should not be protected, for, in the absence of a statutory provision, they should have no better right to the fund than the debtor himself. ...

[53] When I develop that "logic" that Kay, J. speaks of in this quotation, it becomes readily apparent what distinguishes the unsecured creditors of the Universal Group from Bear Creek and explains why Bear Creek has a better right to the surplus funds that MNP holds than the unsecured creditors do: Bear Creek (except as to the Bank)

was a secured creditor of the Universal Group. It worked assiduously to ensure that the Universal Group would repay the \$2.5 million loan it extended by the Promissory Note and took as much security as it could avail of subject only as, I repeat, to the Bank. The Bank is no longer in play in these proceedings, and it is eminently fair and equitable to allow Bear Creek to recover as much of its “secured” debt as is available from the surplus proceeds.

[54] Regrettably, Bear Creek will recover only about 15 percent of what is owed to it (\$350,000-\$400,000/\$2,500,000) in roughly the same proportion as the unsecured creditors would have had available to them if they could share the surplus (\$350,000-\$400,000/\$2,595,886).

[55] In sum, Bear Creek has a superior claim to the unsecured creditors, for the surplus proceeds and because of Bear Creek’s superior claim it is fair and equitable that the surplus funds be paid to Bear Creek, and I so direct; by employing the mechanism of subrogation.

SUBROGATION

[56] I quoted from the CED earlier in these reasons, and from that excerpt I note that subrogation “means the substitution of one person in the place of another for a legal claim, so that the person substituted succeeds to the rights of the other in relation to the claim”. In this matter, but for the outstanding claims by Bear Creek and the unsecured creditors to the surplus funds that MNP holds for the Universal Group, those funds would belong to the Universal Group. Between Bear Creek and the unsecured creditors, the former has the superior claim to the funds as I have just found and Bear Creek is subrogated to the Universal Group to receive the funds.

[57] In effect, and to paraphrase my earlier quotation from the CED, I substitute Bear Creek for the Universal Group and I direct MNP, the Receiver of the Universal Group, to pay the surplus funds into this Court to be distributed to Bear Creek.

DISPOSITION

[58] Bear Creek applied to Court for an order directing that surplus funds held by MNP, Receiver of the Universal Group, be marshalled and paid to Bear Creek by subrogation. PwC, the Trustee in Bankruptcy of the Universal Group, opposed Bear Creek's Application, claiming that the Universal Group's unsecured creditors would be materially prejudiced if Bear Creek received the funds.

[59] PwC also claimed that marshalling should not be allowed since the funds were held by MNP, on behalf of the Universal Group, and the Canadian Western Bank was a creditor of Lakelse, not of the Universal Group. Thus, said PwC the conditions were not present for marshalling: while there were two separate creditors, the Bank and Bear Creek, there were also two separate debtors, the Universal Group and Lakelse; and Bear Creek is a creditor of Lakelse, but not of the Universal Group.

[60] The Court found:

1. The Universal Group and Lakelse are the same entity, operating as the Universal Group;
2. The Bank and Bear Creek are separate creditors of the Universal Group;
3. The Universal Group is a single debtor of the Bank and Bear Creek;
4. Bear Creek's claim to the surplus funds, as a secured creditor, is superior to the Universal Group's unsecured creditors' claims;
5. It is fair and equitable to allow Bear Creek to satisfy the debt from the surplus funds that MNP holds for the Universal Group; and

6. Bear Creek is subrogated to the Universal Group for the surplus funds.

[61] In the result, I order that:

1. MNP, the Receiver of the Universal Group, pay the surplus funds into this Court to be distributed to Bear Creek; and
2. Bear Creek will have its costs of the Interlocutory Application to be taxed on Column 3 of the Scale of Costs.

GARRETT A. HANDRIGAN
Justice

TAB 8

KeyCite treatment

Most Negative Treatment: Distinguished

Most Recent Distinguished: [Upper Room Alliance Group Ltd. v. John Volken Foundation](#) | 2008 CarswellOnt 5980, [2008] O.J. No. 3960, 77 R.P.R. (4th) 47, 170 A.C.W.S. (3d) 519, 54 B.L.R. (4th) 97 | (Ont. S.C.J., Oct 9, 2008)

1996 CarswellOnt 1699

Ontario Court of Justice (General Division)

Transamerica Life Insurance Co. of Canada v. Canada Life Assurance Co.

1996 CarswellOnt 1699, [1996] O.J. No. 1568, 28 O.R. (3d) 423, 2 O.T.C. 146, 62 A.C.W.S. (3d) 891

Transamerica Life Insurance Company of Canada (plaintiff / respondent) and The Canada Life Assurance Company and Canada Life Mortgage Services Ltd. (defendants / moving party)

Sharpe J.

Judgment: May 1, 1996

Docket: Toronto 92-CQ-27566

Counsel: *Earl Cherniak, Q.C., Paul Bates and Simon Clements*, for plaintiff / respondent.

Robert Armstrong, Q.C., Robert Rueter and Stephanie Willson, for defendants / moving party.

Subject: Civil Practice and Procedure

Related Abridgment Classifications

Business associations

I Nature of business associations

I.3 Nature of corporation

I.3.a Distinct existence

I.3.a.i From owner

I.3.a.i.A Lifting the corporate veil

Headnote

Corporations --- Nature of corporation --- Distinct existence --- Lifting the corporate veil

Corporations — Nature of corporation — Distinct existence — Lifting the corporate veil — Defendant parent and wholly-owned subsidiary being completely separate entities — Parent company not having any control over subsidiary nor involved in any way with plaintiff's dealing with subsidiary — No basis existing for piercing corporate veil.

The plaintiff made 54 mortgage loans between 1983 to 1989 which had been arranged by the defendant. A number of those mortgages had fallen into default in an alleged loss of approximately \$60 million. The plaintiff alleged that the defendants owed it a duty to do the underwriting for the loans and that it failed to do so. The plaintiff sued the defendants for damages for breach of contract, breach of fiduciary duty, fraud, misrepresentation and negligence. One of the defendants was the wholly owned subsidiary of the other. The plaintiff asserted that the parent company is liable for the wrongs of its subsidiary. The parent company moved for summary judgment dismissing the action against it on the basis that there was no triable issue as to its liability to the plaintiff. The plaintiff contended that there existed a basis for piercing the corporate veil, and for holding the parent company liable as an accessory to a breach of fiduciary duty of its subsidiary and liable as an accessory for the alleged misrepresentation of the subsidiary.

Held:

The motion was granted.

The parent company satisfied the onus of demonstrating that there was no genuine issues for trial respecting its liability to the plaintiff. The subsidiary and parent companies had their own head offices and branch offices, their own bank accounts and were managed and operated independently of one another. There was an arm's length relationship between the defendants. There was no evidence that any officer, employee or agent of the parent company was in any way involved with the dealings between the

plaintiff and the subsidiary. There was no basis for piercing the corporate veil as there existed no principal-agent relationship between the two defendants. The parent did not control the subsidiary and there was no evidence to indicate any involvement in the impugned transactions between the plaintiff and the parent company. The plaintiff failed to demonstrate that there existed any triable issues with respect to the parent company's liability on the basis of its being an accessory to a breach of fiduciary duty or a misrepresentation.

Table of Authorities

Cases considered:

Air Canada v. M p; L Travel Ltd. (1993), 50 E.T.R. 225, 159 N.R. 1, [1993] 3 S.C.R. 787, 67 O.A.C. 1, 15 O.R. (3d) 804 (note), 108 D.L.R. (4th) 592 — considered

Aluminum Co. of Canada v. Toronto (City), [1944] S.C.R. 267, [1944] 3 D.L.R. 609 — referred to

Australian Securities Commission v. A.S. Nominees Ltd. (1995), 133 A.L.R. 1 — referred to

B.G. Preeco I (Pacific Coast) Ltd. v. Bon Street Holdings Ltd. (1989), 4 R.P.R. (2d) 74, 37 B.C.L.R. (2d) 258, 43 B.L.R. 67, (sub nom. *B.G. Preeco I (Pacific Coast) Ltd. v. Bon Street Developments Ltd.*) 60 D.L.R. (4th) 30 (C.A.) — applied

Bank of Montreal v. Canadian Westgrowth Ltd. (1990), 102 A.R. 391, 72 Alta. L.R. (2d) 319 (Q.B.) [affirmed (1992), 2 Alta. L.R. (3d) 221, 135 A.R. 49, 33 W.A.C. 49 (C.A.)] — referred to

Barnes v. Addy (1874), 9 Ch. App. 244 (C.A.) — referred to

Clarkson Co. v. Zhelka, [1967] 2 O.R. 565, 64 D.L.R. (2d) 457 (H.C.) — distinguished

Covert v. Nova Scotia (Minister of Finance), [1980] 2 S.C.R. 774, 8 E.T.R. 69, (sub nom. *Jodrey Estate v. Nova Scotia*) 41 N.S.R. (2d) 181, 32 N.R. 275, (sub nom. *Jodrey v. Nova Scotia (Minister of Finance)*) [1980] C.T.C. 437 — distinguished

Gold v. Rosenberg (1995), 9 E.T.R. (2d) 93, 129 D.L.R. (4th) 152, 86 O.A.C. 116, 25 O.R. (3d) 601 (C.A.) — considered

Gregorio v. Intrans-Corp. (1994), 4 M.V.R. (3d) 140, 18 O.R. (3d) 527, 72 O.A.C. 51, 115 D.L.R. (4th) 200, 15 B.L.R. (2d) 109 (C.A.) [additional reasons at (1994), 15 B.L.R. (2d) 109n (Ont. C.A.)] — considered

Kosmopoulos v. Constitution Insurance Co., 22 C.C.L.I. 296, [1987] 1 S.C.R. 2, (sub nom. *Kosmopoulos v. Constitution Insurance Co. of Can.*) [1987] I.L.R. 1-2147, 74 N.R. 360, 21 O.A.C. 4, (sub nom. *Constitution Insurance Co. of Can. v. Kosmopoulos*) 34 D.L.R. (4th) 208, (sub nom. *Kosmopoulos v. Constitution Insurance Co.*) 36 B.L.R. 233 — considered

Pizza Pizza Ltd. v. Gillespie (1990), 75 O.R. (2d) 225, 45 C.P.C. (2d) 168, 33 C.P.R. (3d) 515 (Gen. Div.) — referred to

Royal Brunei Airlines Sdn Bhd v. Tan, [1995] 3 W.L.R. 64 (P.C.) — referred to

Salomon v. Salomon p; Co., [1897] A.C. 22, [1895-99] All E.R. Rep. 33, 4 Mans. 89 (H.L.) — applied

W.D. Latimer Co. v. Dijon Investments Ltd. (1992), 12 O.R. (3d) 415 (Gen. Div.) — referred to

801962 Ontario Inc. v. MacKenzie Trust Trust Co., [1994] O.J. 2105 [unreported] — considered

1061590 Ontario Ltd. v. Ontario Jockey Club (1995), 43 R.P.R. (2d) 161, 16 C.E.L.R. (N.S.) 1, 21 O.R. (3d) 547, 77 O.A.C. 196 (C.A.) — referred to

Statutes considered:

Competition Act, R.S.C. 1985, c. C-34

s. 36(4)referred to

s. 52(1)considered

MOTION for summary judgment dismissing action against moving party for disclosing no genuine triable issue.

Sharpe J.:

Introduction

1 In the period 1983 to 1989, the plaintiff, Transamerica Life Insurance Company of Canada, made fifty-four mortgage loans which were arranged by the defendant Canada Life Mortgage Services Ltd. ("CLMS"). A number of the mortgages have fallen into default, resulting in an alleged loss of some \$60 million. Transamerica asserts that CLMS owed it a duty to do the underwriting (due diligence, risk assessment and analysis) for these loans, that CLMS failed in that regard, and that Transamerica has suffered loss as a consequence. In its claim against CLMS, Transamerica pleads breach of contract, breach of fiduciary duty, fraud, misrepresentation and negligence. CLMS denies that it owed Transamerica any duty to underwrite the loans, asserts that

it acted throughout simply as a mortgage broker, and contends that it was for Transamerica to do its own underwriting and due diligence with respect to the loans in question.

2 CLMS is the wholly owned subsidiary of The Canada Life Assurance Company. Transamerica asserts that Canada Life liable for the wrongs of CLMS on a variety of grounds and has joined Canada Life as a defendant to this lawsuit. Canada Life asserts that it had nothing to do with the mortgages in question and that there is no basis for the claim that it is legally responsible for the alleged wrongs of its wholly-owned subsidiary, CLMS. Canada Life brings this motion for summary judgment on the grounds that Transamerica had failed to show that there is a triable issue as to Canada Life's liability and asks that the action against it be dismissed.

Issues

3 Transamerica bases its claim against Canada Life on three grounds which, it asserts, permit the court to look behind the separate corporate existence of CLMS and attach liability to its sole shareholder, Canada Life. These assertions give rise to the following issues on this motion for summary judgment.

1. Is there a basis for "piercing the corporate veil" and holding Canada Life liable for the acts of its wholly owned subsidiary, CLMS?
2. Is there a basis for holding Canada Life liable as an accessory to a breach of fiduciary duty by CLMS?
3. Is there a basis for holding Canada Life liable for the alleged misrepresentations of CLMS either at common law, or under the *Competition Act*?

Facts

4 CLMS was incorporated in 1974 to carry on business as a mortgage correspondent and general financial agent. Before the creation of CLMS, Canada Life had regularly invested in mortgages originated by its branch offices. The branches produced more mortgage investment opportunities than Canada Life could handle and Canada Life decided to incorporate CLMS to carry on the business of mortgage correspondent and to deal with both Canada Life and other institutional investors. As CLMS was to be a wholly owned subsidiary, governing legislation required Canada Life to obtain the consent of the Department of Insurance, now Office of the Superintendent of Financial Institutions ("OSFI"), to its incorporation. The Department of Insurance was satisfied that the proposed business of CLMS was ancillary to the business of insurance as required by [s. 65 of the Canadian and British Insurance Companies Act](#). Henry Heft, the employee of the Department of Insurance who dealt with the CLMS matter, testified that under the legislation, the Department was not interested in the way in which CLMS carried on its business, but only that it was ancillary to the business of insurance, that Canada Life's investment was not unreasonable and properly accounted for, and that CLMS did not exceed the powers it was given under its letters patent. It was Heft's understanding that the activity of a mortgage correspondent was to "be there for the service of people wanting to invest funds, and also for the service of people looking for the funds." The Department took no interest in whether the borrower or the lender paid CLMS a fee and knew that CLMS would be dealing with borrowers in all aspects of the proposed mortgage business. Para. (a)(ii) of the CLMS objects provides:

to assist in the development, financing, construction and promotion of various real and immovable properties, including research and feasibility studies relating to commercial, industrial, residential and public and private undertakings.

Heft understood this to refer to providing or obtaining financing for owners of real estate, in other words, borrowers.

5 It was Heft's evidence that the Department was not concerned about CLMS engaging in the business of assisting borrowers. Heft also testified that the Department did not address the particular matter of whether the due diligence review, analysis and risk assessment was the function of the insurance company lender or CLMS as mortgage broker. It was, however, his own personal understanding that this would be the responsibility of the lender.

6 In March 1981, Transamerica and CLMS established a "Master Agreement" to govern their relationship, and in the period to 1989, Transamerica invested in 54 mortgages originated by CLMS pursuant to this agreement. The terms of this agreement do not specifically provide that CLMS is to perform any underwriting function on Transamerica's behalf. CLMS takes the position that the agreement excludes this duty and asserts that it does not engage in the business of underwriting mortgage loan proposals for any lender. CLMS has an agreement with Canada Life in terms virtually identical to the Transamerica agreement and Canada Life does its own due diligence, review and risk assessment of proposed loans and does not look to CLMS to perform this function. The interpretation of the agreement and the nature of the relationship between CLMS and Transamerica is hotly disputed as Transamerica takes the position that CLMS was responsible for the underwriting function with respect to the loans it made.

7 The relationship between CLMS and Canada Life is as follows. CLMS has its own head office and branch offices distinct from those of Canada Life. CLMS has its own bank accounts. It is and was managed and operated independently of Canada Life. CLMS management exercises independent discretion in conducting the business of CLMS. Apart from the president, the senior management of CLMS is independent of Canada Life. Two vice-presidents have overall responsibility for the affairs of CLMS. The president of CLMS is a Canada Life employee. He spends a very small percentage of his time on CLMS business and he plays no role on the day to day management of CLMS. While his salary is paid by Canada Life, the portion of it attributable to the time he spends on CLMS business is charged back to CLMS. Canada Life does provide CLMS with certain administrative services, including payroll, salary records and legal services. The cost of these services is billed to CLMS by Canada Life, and responsibility for hiring, promotion and remuneration of CLMS employees remains that of CLMS management. All members of the CLMS board of directors and the president of CLMS are senior executives of Canada Life.

8 Canada Life and CLMS take the position that the exigencies of the market required there to be an arm's length relationship between the two companies. They contend that prospective lenders, including Transamerica, were concerned that Canada Life would be in a favoured position and "cherry-pick" the best investments, and for that reason, CLMS was operated as a business entirely separate and independent of Canada Life.

9 The individual who dealt directly with Transamerica during the relevant period, Stuart Pearson, was the branch manager of the Toronto Regional Branch. He reported to Tom Deegan, one of the two vice-presidents. Pearson and Deegan were both employees of CLMS and neither had any duties or responsibilities to Canada Life. The affidavit of J. Gordon Fleming, President and Chairman of the Board of CLMS from 1984 to 1994 describes the involvement, or lack thereof, of Canada Life in the dealings between CLMS and Transamerica:

All business dealings between CLMS and Transamerica were conducted by CLMS employees directly with Transamerica employees. There has been absolutely no involvement in the business dealings between CLMS and Transamerica by directors, officers or employees of Canada Life other than the presence of representatives of Canada Life in discussion with Transamerica about this litigation commencing in 1992. There was never any involvement in the actual business dealings between CLMS and Transamerica that gives rise to this litigation by the directors, officers or employees of Canada Life not indeed was there even any knowledge of it by them.

10 There is no evidence, subject to what follows relating to certain meetings in 1989, that Mr. Fleming or any other Canada Life officer or employee were involved in any way in the dealings between CLMS and Transamerica. The relationship between CLMS and Transamerica was not discussed by the Board of Directors of CLMS. Apart from six letters from the legal department of Canada Life, acting in the capacity of solicitors for CLMS, there is no evidence of any communication whatsoever between Canada Life and Transamerica in relation to the transactions at issue in this suit prior to the initiation of proceedings.

11 As noted already, the president of CLMS, Mr. Fleming and his predecessor, R.D. Radford, were the only officers of CLMS who were also officers of Canada Life. There is no evidence to suggest that Mr. Radford was aware of or involved with Transamerica. Fleming's involvement prior to the initiation of proceedings was as follows. In 1989, senior officers from Transamerica's parent came to Toronto to conduct a review of the mortgage investment practices and procedures of Transamerica. The inferences to be drawn from this review is a matter of dispute between CLMS and Transamerica.

Transamerica takes the position that this review should have made it apparent to CLMS that Transamerica was relying on CLMS for underwriting advice in relation to the mortgages in which it was investing. CLMS takes the position that the review suggested otherwise and points to the fact that a report of the review recognized that Transamerica should not be relying on CLMS for underwriting but rather should ensure it had internal capacity to perform that function. The significance of this review will be an issue for trial as between CLMS and Transamerica. For the purposes of this motion, Transamerica argues that there is evidence that Fleming became aware of the review and that his failure to set the record straight as to the nature of the service being provided by CLMS to Transamerica is sufficient to fix liability on Canada Life. The only evidence of Fleming's awareness is as follows. The defendants have produced an extract from a minute of a CLMS management meeting of June 28, 1989, of Fleming and the two vice-presidents, Curtin and Deegan:

Mr. Fleming was advised of a visit from the Senior Vice-President of Transamerica who was conducting an "underwriting audit" of their mortgage dealings in Canada. Attending the meetings were Joseph Barbieri, Bob Clarke and myself.

Transamerica was interested in mortgage financing in Canada and their questions were mainly directed to types of financings, building construction, appraisals, etc. There was no criticism of our services either from the branch or head office.

12 Transamerica takes the position that this is sufficient to fix Fleming, and through Fleming, Canada Life, with knowledge of the breach of contract, breach of fiduciary duty, and misrepresentations alleged against CLMS. In my view, this assertion reads far more into the minute than is warranted by the minute itself and by the balance of the evidence surrounding the meetings of the visiting Transamerica executives. Fleming denies that he was told that Transamerica thought that CLMS was doing the underwriting. It was his evidence that during the course of a meeting that lasted about two minutes, he was told that CLMS had had a visit from Transamerica. He stated that he is almost certain that this was the first time he learned that CLMS was doing business with Transamerica and that he considered it to be a routine matter for an investor to come to learn more about the mortgage market in Canada. He agreed that if he had been made aware that Transamerica was operating under the mistaken impression that CLMS was doing the underwriting for the loans, he would have instructed the CLMS staff to set the matter straight, but the information he was given did not convey that information.

Analysis

1. Is there a basis for "piercing the corporate veil" and holding Canada Life liable for the acts of its wholly owned subsidiary, CLMS?

13 On behalf of Transamerica, Mr. Bates submits that the applicable legal test for piercing the corporate veil can be stated no more precisely than this: the corporate veil will be pierced when it is "just and equitable" to do so. As authority for that proposition, reliance is placed on the following passage from the judgment of Wilson J. in *Constitution Insurance Co. v. Kosmopolous*, [1987] 1 S.C.R. 2 at pp. 10-11:

As a general rule a corporation is a legal entity distinct from its shareholders: *Salomon v. Salomon & Co.* [1897] A.C. 22 (H.L.). The law on when a court may disregard this principle by "lifting the corporate veil" and regarding the company as a mere "agent" or "puppet" of its controlling shareholder or parent corporation follows no consistent principle. The best that can be said is that the "separate entities" principle is not enforced when it would yield a result "too flagrantly opposed to justice, convenience or the interests of the Revenue": L.C.B. Gower, *Modern Company Law* (4th ed. 1979) at p. 112. I have no doubt that theoretically the veil could be lifted in this case to do justice ... But a number of factors lead me to think it would be unwise to do so.

14 If accepted, the argument advanced by Transamerica would represent a significant departure from the principle established in *Salomon v. Salomon & Co.*, [1897] A.C. 22 (U.K. H.L.) at 51 per Lord Macnaughten:

The company is at law a different person altogether from the subscribers to the memorandum; and, though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same

hands receive the profits, the company is not in law the agent of the subscribers or trustee for them. Nor are the subscribers as members liable, in any shape or form, except to the extent and in the manner provided by the Act.

15 In my view, the argument advanced by Transamerica reads far too much into a dictum plainly not intended to constitute an in depth analysis of an important area of the law or to reverse a legal principle which, for almost 100 years, has served as a cornerstone of corporate law.

16 It was conceded in argument that no case since *Kosmopolous* has applied the preferred "just and equitable" test. In *Kosmopolous* itself, the Supreme Court, including Wilson J., rejected the submission that the corporate veil be lifted. Moreover, it will be noted that Wilson J. does not use the phrase "just and equitable" but rather quotes a passage from an English text which describes the test in much more stringent terms.

17 Two recent judgments of this court have refused to read the *Kosmopolous* dictum as granting carte blanche to lift the corporate veil absent fraudulent or improper conduct: *W.D. Latimer Co. v. Dijon Investments Ltd.* (1992), 12 O.R. (3d) 415 (Gen. Div.); *801962 Ontario Inc. v. MacKenzie Trust Co.*, [1994] O.J. No. 2105 [unreported]. In the *MacKenzie* case, Spence J. reviewed the case-law in detail and concluded:

These decisions do not support a claim that the test in *Salomon v. Salomon* has been superseded by a new "business entity" or "single business entity" test. They merely illustrate the principle that, in particular fact situations, where the nature of the legal issue in dispute makes it appropriate to have regard to the larger business entity, the court is not precluded by *Salomon v. Salomon* from doing so. In a few cases, there are statements that the court will lift the corporate veil "where injustice would otherwise result." I am not able to conclude that such statements are intended to remove the authority of the *Salomon* principle. I think they may be more in the nature of a shorthand formulation reflecting the approach of the courts in the cases discussed above.

18 The proposition that the dictum of Wilson J in *Kosmopolous* suggests a fundamental shift in the law was also rejected by the British Columbia Court of Appeal in *B.G. Preeco I (Pacific Coast) Ltd. v. Bon Street Holdings Ltd.* (1989), 37 B.C.L.R. (2d) 258 (C.A.). Seaton J. observed (at 267) that the passage quoted in *Kosmopolous* from Gower, *Modern Company Law*, concluded with a passage which disapproved of the free-wheeling "just and equitable" approach:

The most that can be said is that the courts' policy is to lift the veil if they think that justice demands it and they are not constrained by contrary binding authority. The results in individual cases may be commendable, but it smacks of palm-tree justice rather than the application of legal rules.

Seaton J.A. went on to quote a Canadian text, *Welling, Corporate Law in Canada* (1984) at p. 129, which disapproved of the approach of some American cases to adopt a general fairness test:

Little need be said about this rationale, other than that it simply will not do. There are, so far as we know, no such broadly enforceable standards of "fair play and good conscience," at least in Canadian corporate law.

19 It should also be noted that the most recent edition of Gower, *Modern Company Law*, (5th ed., 1992) puts the test for lifting the corporate veil in much more stringent terms. The authors review the decision of the English Court of Appeal in *Adams v. Cape Industries plc*, [1991] 1 All E.R. 433 which, they state (at p. 125) "subjected lifting the veil to the most exhaustive treatment that it has yet received in the English (or Scottish) courts." The authors conclude that the *Adams* decision significantly attenuates the grounds for lifting the veil, and they make no suggestion, as they did in the earlier edition cited in *Kosmopolous*, that the test is anything like a "just and equitable standard: (at 132-133)

There seem to be three circumstances only in which the courts can do so. These are:

- (1) When the court is construing a statute, contract or other document.
- (2) When the court is satisfied that a company is a "mere facade" concealing the true facts.

(3) When it can be established that the company is an authorized agent of its controllers or its members, corporate or human.

20 In a recent judgment of the Ontario Court of Appeal, *Gregorio v. Intrans-Corp.* (1994), 18 O.R. (3d) 527 (C.A.) at 536, Laskin J.A. restated the legal principles relating to the liability of a parent company for the acts of its subsidiary as follows:

Generally, a subsidiary, even a wholly owned subsidiary, will not be found to be the alter ego of its parent unless the subsidiary is under the complete control of the parent and is nothing more than a conduit used by the parent to avoid liability. The alter ego principle is applied to prevent conduct akin to fraud that would otherwise unjustly deprive claimants of their rights.

21 There are undoubtedly situations where justice requires that the corporate veil be lifted. The cases and authorities already cited indicate that it will be difficult to define precisely when lifting the corporate veil is to be lifted, but that lack of a precise test does not mean that a court is free to act as it pleases on some loosely defined "just and equitable" standard. There may be a principal-agent relationship between two related corporations which leads to liability despite separate legal personalities: see *Gower, supra*; *Clarkson Co. v. Zhelka*, [1967] 2 O.R. 565 (H.C.) at 578. It is also the case that the courts will look behind corporate structures where necessary to give effect to legislation, especially taxation statutes: see *Gower, supra*; *Covert v. Nova Scotia (Minister of Finance)*, [1980] 2 S.C.R. 774. Neither of these two exceptions applies to the situation of the case at bar.

22 As just indicated, the courts will disregard the separate legal personality of a corporate entity where it is completely dominated and controlled and being used as a shield for fraudulent or improper conduct. The first element, "complete control", requires more than ownership. It must be shown that there is complete domination and that the subsidiary company does not, in fact, function independently: *Aluminum Co. of Canada v. Toronto (City)*, [1944] S.C.R. 267 at 271; *Bank of Montreal v. Canadian Westgrowth Ltd.* (1990), 72 Alta. R. (2d) 319 (Q.B.). The evidence before me indicates that the relationship between Canada Life and CLMS was that of a typical parent and subsidiary. While CLMS is wholly owned by Canada Life and its board of directors is comprised of Canada Life executives, I have found that it does have an independent management and conducts a business separate and distinct from that of its parent. There is, in my opinion, no evidence sufficient to give rise to a triable issue that CLMS is the mere puppet of Canada Life.

23 The second element relates to the nature of the conduct: is there "conduct akin to fraud that would otherwise unjustly deprive claimants of their rights?" In my view, while Transamerica has alleged fraud against CLMS, there is no evidence to suggest that Canada Life has any involvement in that alleged fraud, apart from the fact that CLMS is its wholly-owned subsidiary. The officers and employees of Canada Life were not involved in the dealings between CLMS and Transamerica, and no evidence has been advanced sufficient to give rise to a triable issue that Canada Life is somehow using CLMS as a shield for some nefarious purpose.

24 It is submitted that this is a developing area of the law, and that it would be wrong for me to grant summary judgment and thereby preclude having the issue fully considered at trial in light of all the evidence. As I have already indicated, it is my view that the law in this area is not developing at anything close to the extent submitted by Mr. Bates. Moreover, there is nothing in the facts of this case to suggest that this would be a case where the court might be tempted to lift the corporate veil in the interest of doing justice between the parties. Transamerica has simply not been able to make out a triable issue or arguable case that the court should look behind the corporate veil. There has been extensive discovery, cross-examination on affidavits and this motion has been pending for almost an entire year. Transamerica has had the fullest possible opportunity to advance its case. It is clearly established that on a motion for summary judgment, a party is no longer entitled to sit back and rely on the possibility that more favourable facts may develop at trial. To avoid summary judgment, a party is required to put its best foot forward. The onus remains on the moving party to show that there is no genuine issue for trial, but the responding party must "lead trump or risk losing": *Pizza Pizza Ltd. v. Gillespie* (1990), 75 O.R. (2d) 225 (Gen. Div.); *1061590 Ontario Ltd. v. Ontario Jockey Club* (1995), 21 O.R. (3d) 547 (C.A.). In my view, Transamerica has failed to present evidence to indicate that there is a triable issue on this point and Canada Life has met the onus of showing that it should be granted summary judgment on this issue.

2. Is there a basis for holding Canada Life liable as an accessory to a breach of fiduciary duty by CLMS?

25 In my view, Transamerica has failed to demonstrate that there is a triable issue on the claim that Canada Life is liable as an accessory to a breach of fiduciary duty.

26 This area of the law was canvassed at length in the recent decision of the Supreme Court of Canada, *Air Canada v. M. p; L. Travel Ltd.*, [1993] 3 S.C.R. 787. That case affirms the principle that a stranger to a trust may become personally liable for a breach of trust committed by the trustee. It involved the liability of directors of a closely held corporation for a breach of trust committed by the corporation. On the surface, this is analogous to the case at bar where Transamerica alleges that Canada Life should be held to account for a breach of fiduciary duty committed by its wholly owned subsidiary, CLMS. However, it should be noted that in the *Air Canada* case, the directors were directly and personally involved in the misappropriation of trust funds. The Supreme Court of Canada found that to support a claim against an accessory, the plaintiff must show a breach of trust of a fraudulent or dishonest nature. An innocent breach of trust will not suffice. The opinion of Iacobucci J. also makes it clear that the stranger to the trust must be involved in the breach with actual knowledge, recklessness or wilful blindness. Iacobucci J. expressly excludes the possibility of liability on the basis of constructive knowledge (knowledge of circumstances which would indicate the facts to an honest person or put an honest person on inquiry). This conclusion is consistent with a long line of authority with respect to accessorial liability for breach of trust. In an early leading case, cited with approval by Iacobucci J., it was stated that persons who "assist with knowledge in a dishonest and fraudulent design on the part of the trustees" will be held liable: *Barnes v. Addy* (1874), 9 Ch. App. 244 (U.K. C.A.) at 252. The statement of the principle cited by Transamerica is that from the judgment of Finn J. in *Australian Securities Commission v. A.S. Nominees Ltd.* (1995), 133 A.L.R. 1 at 19:

For present purposes, that liability rule can be formulated (conservatively) as one which exposes a third party to the full range of equitable remedy available against the trustee if that person knowingly or recklessly assists in or procures a breach of trust or of fiduciary duty by a trustee.

27 The recent judgment of the Privy Council in *Royal Brunei Airlines Sdn Bhd v. Tan*, [1995] 3 W.L.R. 64 (P.C.) describes the level of misconduct required as "dishonesty": "A liability in equity to make good resulting loss attaches to person who dishonestly procures or assists in a breach of trust or fiduciary obligation" (at 76 per Lord Nicholls). The Ontario Court of Appeal has also recently had occasion to review the law in this area. In *Gold v. Rosenberg* (1995), 25 O.R. (3d) 601 (C.A.), Laskin J.A. held that the Supreme Court of Canada's decision in the *Air Canada* case, supra, had "settled" two crucial questions in this area, first, whether the trustee's breach had to be fraudulent and dishonest, and second, whether the agent must have actual knowledge to be held liable or whether constructive knowledge is sufficient. As Laskin J.A. observed, the judgment of Iacobucci J. *Air Canada* makes it clear that the breach of trust must be fraudulent or dishonest and the agent must have actual knowledge of the breach.

28 The nature of the breach alleged against CLMS is essentially an allegation that CLMS had a contractual obligation to perform certain duties with respect to underwriting the loans and that it breached those contractual duties by failing to perform as it had promised. Mr. Cherniak submits that where the contract is such as to give rise to a fiduciary duty, the party complaining of the breach is clearly entitled to ground its claim in equity if that is more beneficial. Accepting that proposition still leaves Transamerica well short of a fraudulent or dishonest breach of trust of the kind contemplated by *Air Canada* and *Gold v. Rosenberg* as being necessary to support a claim for the liability if the accessory. But even if the claim of Transamerica against Canada Life could survive that first hurdle, there is no evidence to support the allegation that Canada Life knowingly assisting CLMS in committing a breach of trust or breach of fiduciary duty. Certainly, there is no evidence of "dishonesty" (said to be necessary by the Privy Council in *Royal Brunei Airlines Sdn Bhd v. Tan*) on the part of Canada Life. As indicated above, until 1989, no Canada Life officer or employee knew that CLMS had dealings with Transamerica, let alone that CLMS was acting in breach of trust or breach of fiduciary duty. Transamerica relies on the undertaking given to OSFI at the time of CLMS's incorporation. That undertaking was not given to or even known by Transamerica and the evidence of Heft, the party who received the undertaking, is clear that there is no basis to support the very specific meaning and significance Transamerica seeks to attribute to it. The information conveyed to Fleming in relation to the visit from the senior executives of Transamerica's parent in 1989 falls well short of evidence capable of grounding a triable issue on this point. In my view, the contentions of

Transamerica on this point are wholly unsupported by the evidence and there is no triable issue of liability of Canada Life. It is apparent that this argument amounts to an attempt to overcome the limitation of liability created by the separate corporate existence of Canada Life and CLMS. It is also apparent from the *Air Canada* case and the other authorities already cited that without proof of knowing involvement in the breach of trust, the law does not impose equitable liability simply on the basis that the targeted defendant is the owner of the corporate entity which committed the equitable wrong.

3. Is there a basis for holding Canada Life liable for the alleged misrepresentations of CLMS either at common law or under the Competition Act?

29 In the statement of claim, Transamerica contends that CLMS represented to it that Canada Life "would stand behind CLMS and ensure that it discharge its obligations to Transamerica" and that "CLMS' business for Transamerica was that of a mortgage correspondent acting on behalf of Transamerica in the acquisition and servicing of the mortgage investments." With respect to Canada Life, it is pleaded:

Canada Life knew or ought to have known that the [above] representations ... were made by CLMS to Transamerica for the purpose of inducing Transamerica to do business with, and to continue to do business with, CLMS pursuant to the Mortgage Correspondent Agreement. Canada Life caused, and consented to, the making of these representations for the purpose of realizing economic gain conducted by CLMS with Transamerica.

In response to a demand for particulars of these allegations against Canada Life, Transamerica was unable to specify any communication from Canada Life. On this motion for summary judgment, no evidence has been offered that Canada Life "caused" any misrepresentation to be made to Transamerica. Nor has any evidence been offered to support the allegation that Canada Life "consented to" any such misrepresentation if, indeed, "consenting" to such a statement would give rise to liability.

30 Transamerica submits that it is entitled to succeed against Canada Life on the theory that it must have known of certain misrepresentations made by CLMS. It is submitted that these alleged misrepresentations give rise to a common law cause of action and to an action under the *Competition Act* s. 52(1):

52(1) No person shall, for the purpose of promoting, directly or indirectly, the supply or use of a product or for the purpose of promoting, directly or indirectly, any business interest, by any means whatever,

(a) make any representation to the public that is false or misleading in a material respect.

31 This argument was essentially based upon three marketing brochures which describe the activities of CLMS and its relationship to Canada Life. In addition, reliance was placed on the fact that the CLMS financial statements are consolidated with those of Canada Life.

32 The first of the marketing brochures relied upon was in use for 1976 to 1978, well before Transamerica had any dealings with CLMS and Transamerica has been unable to produce a copy of this brochure from its records. Transamerica does state, however, that its officers saw and relied upon certain statements in the brochure, in particular, that CLMS would act as "the investor's own Mortgage and Real Estate Department" and that CLMS was a "Canada Life company". The second brochure was in use for the period 1982-85 and the third was released in 1989. All the brochures clearly indicate that CLMS provides services to both borrowers and lenders. They also refer to the fact that CLMS is a wholly owned subsidiary of Canada Life.

33 Radford saw the first brochure, signed a letter contained in the second as "Chairman of the Board and President" of CLMS, and Fleming saw the third brochure. Apart from that, there is no evidence that any officer or employee of Canada Life had any involvement with the writing, printing or distribution of these brochures.

34 In my view, the allegations based on these brochures fail to give rise to a triable issue against Canada Life. I will deal first with the issue of the definition of the role of CLMS. The language of the brochures is, at best, ambiguous with respect to the role of CLMS. It is difficult to give credence to the suggestion that at the relevant time, Transamerica attached to these brochures the significance it now does for the purposes of this action. Transamerica was investing millions of dollars in mortgages and had a

detailed written agreement with CLMS to govern their dealings. It strains credibility to imagine that a sophisticated institutional investor would rely on marketing materials of this nature as the basis for defining the legal obligations of CLMS and Canada Life.

35 However, assuming for present purposes that the brochures contain statements which are capable of grounding a claim for deceit, misrepresentation or breach of the provisions of the *Competition Act*, is there evidence to suggest a triable issue that liability should attach to Canada Life? In my view, there is not. They were prepared, printed and distributed by CLMS. In cross-examination, Fleming stated that the authority to put forward marketing materials

existed within the subsidiary itself. This was their brochure, not Canada Life's. So there would be no need for approval from Canada Life. They wouldn't know it existed. So it was a CLMS document. And they produced it and had the authority to produce it themselves for their own corporate purpose.

This is entirely consistent with the rest of the evidence as to the independent management of CLMS and there is no evidence to suggest that Canada Life had any greater involvement in the preparation of the brochures. As indicated, the only involvement of any Canada Life officer or employees was that 1) Radford saw the first brochure; 2) in his capacity as Chairman of the Board and President of CLMS, Radford signed the second brochure; and 3) Fleming saw the third brochure. In my view, this minimal involvement by these two individuals, acting in their capacity with CLMS, falls well short of a factual basis for finding liability on the part of Canada Life.

36 The second issue is the claim that the brochures represent Canada Life as being legally responsible for the acts of CLMS. In addition to the brochures, it is submitted that the consolidated financial statements of Canada Life and CLMS and led Transamerica to believe that Canada Life would "stand behind" CLMS. The evidence with respect to the financial statements is as follows. In June, 1989, as part of its review of the mortgage investment procedures of its subsidiary, a representative of the parent of Transamerica asked CLMS to provide its financial statements. This request was answered by letter from RF Clarke of CLMS dated June 27, 1989:

As you requested in your recent visit to our office, I have enclosed a copy of the Financial Statements of the Canada Life Assurance Company (which includes Canada Life Mortgage Services in its consolidation).

The consolidation of CLMS' financial statements with those of its parent corporation is in accordance with accepted accounting principles, a matter well known to Transamerica as it follows precisely the same practice with respect to its statements.

37 In my view, the evidence advanced to support this claim is insufficient to give rise to a triable issue. The brochures accurately state that CLMS is a wholly owned subsidiary of Canada Life and the financial statements reflect accepted accounting practice. While from a business perspective, the relationship between CLMS and Canada Life was undoubtedly significant to Transamerica, it is inconceivable that a sophisticated corporate entity such as Transamerica would read such statements in a marketing brochure to amount to a representation that Canada Life would be legally liable for any wrongs committed by CLMS. The affidavit of James Roszak is carefully crafted. His statement that Transamerica "understood that Canada Life would stand behind CLMS and ensure that it discharged its obligations" falls well short of a sworn statement that he or anyone else at Transamerica actually thought that when Transamerica dealt with CLMS, that from a legal perspective, it was dealing with Canada Life or that legal liability would attach to Canada Life for the acts of CLMS.

38 In argument, Mr Armstrong placed particular emphasis with respect to this area of the case on the fact Transamerica has failed to adduce any evidence from Ken Hennessy, the officer of Transamerica who was responsible for the day to day dealings with CLMS. In view of the failure of Transamerica to come forward with evidence from Hennessy to say that when he was dealing with Pearson and CLMS, he thought he was really dealing with Canada Life, Mr. Armstrong submits that an adverse inference can be drawn.

39 Mr. Cherniak resists this point on the basis that the Roszak affidavit is based in part upon information from Hennessy. It was also argued that as Hennessy is now a party to the action, having been added as a third party by Canada Life, Transamerica cannot be expected to adduce his evidence.

40 In my view, the failure of Transamerica to provide any evidence on this motion from Hennessy is telling. He is without question the individual with the most direct and immediate knowledge of the dealings between CLMS and Transamerica. It is difficult to imagine how Transamerica could make out its case at trial that when it dealt with CLMS, it honestly thought it was dealing with Canada Life, without strong evidence from this individual. While he has recently been made a third party, this motion for summary judgment has been pending for over one year, and his involvement as a third party does not explain why his evidence was not adduced. I have already indicated the significant weakness in the evidence adduced by Transamerica on the misrepresentation issue. The failure of Transamerica to lead any evidence from Hennessy or to provide an adequate explanation for the fact that no such evidence has been adduced provides a further basis for granting summary judgment on this point.

41 A further point was raised by the defendants, namely, that the claim under the *Competition Act* is statute barred in light of s. 36(4) which requires that any action be brought within "two years from the day on which the conduct was engaged in". This matter was raised in reply argument, and as the limitation defence had not been pleaded, a motion was made to amend the statement of defence. In view of my finding with respect to the misrepresentation claim, it is not necessary for me to deal with this point in relation to the summary judgment motion brought by Canada Life. However, as the action is proceeding against CLMS and the plaintiff asserts a cause of action under the *Competition Act*, I grant leave to amend the statement of defence to plead the limitation defence.

Conclusion

42 For the foregoing reasons, I conclude that the moving party, Canada Life, has met the onus of demonstrating that there is no genuine issue for trial. The responding party, Transamerica, has had full opportunity to come forward with evidence to show that there is a genuine issue for trial but has failed to do so. Accordingly, Canada Life is entitled to summary judgment dismissing the action against it. The remaining defendant CLMS is hereby granted leave to amend the statement of defence to plead the limitation defence pursuant to s. 36(4) of the *Competition Act*. I may be spoken to with respect to costs.

Motion allowed.

TAB 13

1985 CarswellOnt 729

Ontario Supreme Court, High Court of Justice

Brown v. Canadian Imperial Bank of Commerce

1985 CarswellOnt 729, 30 A.C.W.S. (2d) 468, 37 R.P.R. 128, 50 O.R. (2d) 420

BROWN v. CANADIAN IMPERIAL BANK OF COMMERCE et al.

Southey J.

Heard: March 4 and 5, 1985

Judgment: April 22, 1985

Docket: No. 12802/83

Counsel: *C.C. Mark, Q.C.* and *M.P. Thompson*, for plaintiff.

Kenneth Rosenberg, for defendant Canadian Imperial Bank of Commerce.

Stephen Bale, for defendants Constantine and Julie Amourgis and Strawrene Ltd.

Subject: Property; Corporate and Commercial

Related Abridgment Classifications

Real property

VIII Mortgages

VIII.14 Priorities

VIII.14.a Doctrines

VIII.14.a.ii Marshalling

Headnote

Mortgages --- Priorities — Between types of creditors — Registered mortgagees — Marshalling

Marshalling — Debtor being surety debtor for one creditor, principal debtor for another — Debts of surety creditor and other creditor secured by mortgages on same property — Surety creditor having additional security for same debt — Surety creditor being paid out of proceeds of sale of mortgaged property — Applicability of doctrine of marshalling.

Plaintiff, as trustee, was mortgagee under a third mortgage given by J.A. against a property on D Road. The result of proceedings brought by plaintiff to enforce that mortgage was the sale of the property to one S. The full amount of the proceeds from that sale was used to pay prior encumbrancers, including the second mortgagee, Canadian Bank of Commerce (C.I.B.C.).

C.I.B.C.'s second mortgage on the D Road property was collateral security to the guarantee of J.A. for the indebtedness of one Strawrene Ltd. to C.I.B.C. C.I.B.C. also held a second mortgage, securing the same debt, against an S Street property owned by Strawrene Ltd. There were three subsequent mortgages on that property. C.I.B.C. also had taken an assignment of a chattel mortgage in favour of Strawrene Ltd. as security for the same debt.

As the result of enforcement proceedings previously taken against the S Street property and under the chattel mortgage, there were two funds that, pending the determination of certain outstanding issues, were available to C.I.B.C. to discharge the indebtedness of the principal debtor, Strawrene Ltd., and of its surety, J.A. Plaintiff sued for an order requiring C.I.B.C. to marshal its debts. Plaintiff requested that it be subrogated to C.I.B.C.'s interest in the two funds. C.I.B.C. appeared but did not defend.

Held:

The fund originating in the S Street property was not subject to the doctrine of marshalling. The fund originating in the chattel mortgage was subject to the doctrine of marshalling and plaintiff was entitled, therefore, to a transfer of C.I.B.C.'s interest therein.

The doctrine of marshalling is intended to achieve fairness. It was not an objection to its application in this case that C.I.B.C.'s debt had been paid voluntarily by plaintiff out of the sale proceeds of the D Road property. In that respect, plaintiff had no real

choice but to pay C.I.B.C. as the holder of a prior mortgage which S, its purchaser, was not willing to accept. Nor was it an objection that J.A. was only the surety of the C.I.B.C. debt and the principal debtor on plaintiff's debt.

Allowing plaintiff to be subrogated to C.I.B.C.'s claim in the fund originating in the S Street property would prejudice the position of the subsequent encumbrancers of that property. On that basis, the doctrine of marshalling could not be applied to that fund. It could be applied only to the chattel security fund.

Table of Authorities

Cases considered:

Neff v. Miller, 8 Barr. 347 (Pennsylvania C.A.) — *applied*

Quay v. Sculthorpe (1869), 16 Gr. 449 (C.A.) — *applied*

Ruso (G.) Const. Ltd. v. Laviola (1976), 27 Chitty's L.J. 136 (Ont. H.C.) — *distinguished*

APPLICATION for order to marshal funds.

Southey J.:

1 The plaintiff, as trustee, was mortgagee under a third mortgage given by the defendant Julie Amourgis against a property at 24 Dunloe Road in Toronto. The result of proceedings brought by the plaintiff to enforce that mortgage was the sale of the property to one Stieglitz for \$435,000. The full amount of the purchase price was used to pay the costs of the sale and the claims of first and second mortgagees and execution creditors whose claims had priority over that of the plaintiff. The second mortgage was in favour of the defendant Canadian Imperial Bank of Commerce; \$174,937.50 was paid to discharge it. The bank had claims against two other funds for satisfaction of the indebtedness for which the second mortgage against 24 Dunloe was security. The issue in the case is whether the plaintiff can invoke the equitable doctrine of marshalling to require the bank to transfer to the plaintiff its rights against the two other funds so that the plaintiff can recoup therefrom the said sum of \$174,937.50.

2 The bank took no position on the issue. Counsel agreed at the opening of trial that the costs of the bank should be fixed at \$500, and that that sum should be paid first out of any fund to which the plaintiff was found to have access. Counsel for the bank was then excused.

3 The doctrine of marshalling is stated thus in 16 Hals. (4th ed.,) p. 962:

Where one claimant, A, has two funds, X and Y, to which he can resort for satisfaction of his claim, whether legal or equitable, and another claimant, B, can resort to only one of these funds, Y, equity interposes so as to secure that A shall not by resorting to Y disappoint B. Consequently, if the matter is under the court's control, A will be required in the first place to satisfy himself out of X, and only to resort to Y in case of deficiency; and if A has already been paid out of Y, it will allow B to stand in his place as against X. This is known as the doctrine of marshalling, and is adopted in order to prevent one claimant depriving another claimant of his security. The doctrine is applied chiefly in regard to securities and to the administration of assets.

4 The authors go on in the next paragraph to state 3 conditions that are generally necessary for the application of the doctrine. The first of these is relevant to this case, as is a condition respecting third persons. The text reads as follows on pp. 962-963:

Generally, three conditions must be satisfied in order that the doctrine of marshalling may be applied as regards claims by creditors. First, the claims must be against a single debtor. If one creditor has a claim against C and D, and another creditor has a claim against D only, the latter creditor cannot require the former to resort to C unless the liability is such that D could throw the primary liability on C, for example where C and D are principal and surety. The doctrine will not be applied to the prejudice of third persons, even if they are volunteers;

The Facts

5 It is not clear from the authorities whether the doctrine of marshalling applies in this case, and I must describe in some detail the mortgages given on two properties, 24 Dunloe Road and 63 Shuter Street in Toronto, and the origin of two funds from which the bank claimed the right to payment of the debts of the defendant Strawrene Limited. The payment to the bank of the said sum

of \$174,937.50 out of the proceeds of the sale of 24 Dunloe was in satisfaction of the indebtedness of Strawrene to the bank, which had been guaranteed by both of the defendants Amourgis. The two other funds resulted from orders of Houlden J.A. dated November 26, 1982, and of John Holland J. dated April 29, 1983. The former contained about \$77,250, with additional interest; the latter now stands at about \$103,000, with further amounts totalling about \$50,000 to be paid into it.

Title to 24 Dunloe Road

6 Julie Amourgis acquired title to 24 Dunloe as trustee on September 14, 1973. At the time of the sale to Stieglitz in November 1983, the property was subject to the following:

- (1) a first mortgage to Harold Kay, as trustee, on which \$179,577.42 was owing at the date of closing of the Stieglitz sale.
- (2) A second mortgage to the defendant bank which was discharged on the closing of the Stieglitz sale by payment of \$174,937.50. This mortgage was collateral security for the liability of Julie Amourgis on a guarantee of the indebtedness of Strawrene to the bank. Such indebtedness was paid in full by the said sum of \$174,937.50.
- (3) A third mortgage to the plaintiff as trustee, for \$350,000, which was collateral security for the 3rd, 4th and 5th mortgages given by Strawrene on 63 Shuter to Nugate Holdings, May Ekstein, and Rose and Bernard Fluxgold. Those mortgages are referred to in paras. (iii), (iv) and (v) below. When this 3rd mortgage on 24 Dunloe fell into arrears, the plaintiff commenced foreclosure proceedings early in 1982. Julie and Constantine Amourgis defended the action, and on December 14, 1982, Master Sandler gave judgment against them for \$351,132.05, being the amount owing on the mortgage with costs, and directed that the property be sold with the approbation of the Master at Toronto unless that sum was paid into court by June 14, 1983. The sum was not paid, and the sale to Stieglitz for \$435,000 resulted in November, 1983.

Title to 63 Shuter Street

7 Strawrene Limited, in Trust, acquired 63 Shuter Street in May, 1978. The following mortgages were outstanding against the property, in the following priority, as of January 1982:

- (i) Mortgage for \$450,000 in favour of Harold Kay as trustee, dated 12th March, 1979. Constantine and Julie Amourgis joined in this mortgage as covenantors and principal debtors.
- (ii) Mortgage for \$250,000 in favour of the bank, dated March 13, 1979.
- (iii) Mortgage for \$70,000 in favour of Nugate Holdings Limited dated 9th May, 1978. Constantine and Julie Amourgis joined in this mortgage as covenantors and principal debtors.
- (iv) Mortgage for \$50,000 in favour of May Ekstein, dated 7th July, 1981.
- (v) Mortgage for \$150,000 in favour of Rose and Bernard Fluxgold, dated 7th July, 1981.

Fund resulting from order of Houlden J.A., November 26, 1982

8 Harold Kay proceeded under the power of sale contained in the mortgage to him of 63 Shuter Street. By deed dated January 15, 1982, he conveyed the property to Ming Sun Holdings Inc. Strawrene brought an action to set aside the conveyance on the ground that the power of sale was improperly exercised, and registered a *lis pendens* against the property. Montgomery J. dismissed the action and vacated the *lis pendens* by order dated October 19, 1982. The order dismissing the action was set aside on appeal, but not the order vacating the *lis pendens*. Instead, by order of Houlden J.A. dated November 26, 1982, Messrs. Hall, Baker, Goodman, the then solicitors for Harold Kay, as Trustee, were directed to continue to hold in trust in interest bearing certificates of deposit the surplus available for distribution to subsequent encumbrancers upon the sale under the power of sale, and that the surplus should not be distributed except upon a further order of the Court made upon notice to all subsequent encumbrancers. Strawrene has not proceeded with the action. The said surplus is presently being held in trust by the law firm of

Saunders and Spring, which is the firm with which Mr. Harold Spring is now associated. He was associated with Hall, Baker, Goodman at the time of the order of Houlden J.A. The fund now amounts to about \$77,250 together with accrued interest.

9 The indebtedness of Strawrene to the bank, for which the second mortgage on 63 Shuter was security, has been satisfied by payment of the sum of \$174,937.50 out of the proceeds of the sale of 24 Dunloe. That payment resulted in the discharge of the second mortgage on 24 Dunloe. The plaintiff claims in this action under the doctrine of marshalling the right to have transferred to him the bank's rights against the surplus held by Harold Spring's firm as a subsequent encumbrancer under its second mortgage on 63 Shuter Street. Unless Strawrene is successful in its action to set aside the sale of 63 Shuter Street under the first mortgage, the plaintiff, if entitled to stand in the position of the bank, would be entitled to the whole of the said surplus, if marshalling is permitted.

Fund resulting from order of John Holland J., April 29, 1983.

10 By indenture dated December 15, 1978, the bank received an assignment from Strawrene of a chattel mortgage that had been given by a numbered company, 383782 Ontario Limited, to Strawrene on 13 June, 1978, and which was guaranteed by Edward A. Lai. The assignment was collateral security for the indebtedness of Strawrene to the bank. Strawrene and the bank sued Lai on the guarantee, and the action was settled by minutes of settlement dated November 9, 1982, in which Lai agreed to pay to or at the direction of the plaintiffs the sum of \$145,616.25 in a series of payments over a period of time. Because of a dispute between the bank and Strawrene as to the disposition of payments from Lai, John Holland J. made an order on April 29, 1983, that all payments under the settlement be made into court. The amount paid into court as of December 13, 1984, with interest, was \$103,512.21. A further sum of about \$50,000 remains to be paid into court under the minutes of settlement.

Application of the doctrine of marshalling

11 The result of the foregoing is that the bank, when it received payment from the plaintiff of the sum of \$174,937.50 in satisfaction of the indebtedness of Strawrene to the bank and of the indebtedness of Julie Amourgis under the second mortgage on 24 Dunloe, had, in addition to that second mortgage, two other funds from which it could claim payment of the indebtedness of Strawrene. The plaintiff, on the other hand, had only the security of his third mortgage on 24 Dunloe in respect of his claims against Julie Amourgis. The funds arose out of the debts of Strawrene, while the second mortgage on 24 Dunloe was a liability of Julie Amourgis, so that the claims of the creditors, the bank and the plaintiff, were not against a single debtor. But the second mortgage on 24 Dunloe was given by Julie Amourgis as collateral security for her guarantee of the debt of Strawrene to the bank. To use the words in the passage from Halsbury quoted above, Julie Amourgis was the surety and Strawrene was the principal (i.e. principal debtor), so that she could throw the primary liability on Strawrene. The exception to the general rule that there must be a single debtor for marshalling was therefore fulfilled.

12 I think Mr. Mark was right in his submission that *Quay v. Sculthorpe* (1869), 16 Gr. 449 (Ont. C.A.), is authority for applying the doctrine of marshalling in this case, even though there is no common debtor. Van Koughnet C., with whom Mowat V.C. concurred, quoted at p. 456 and applied the following passage from the decision of Bell J., delivering the judgment of the Supreme Court of Pennsylvania in *Neff v. Miller*, 8 Barr 347:

Here is a surety, whose money has been applied in payment of the debt of his principal, to the exclusion of his own proper creditors. That he would be entitled to come in, by way of substitution, upon the estate of the principal, is every-day equity; and I think it equally clear that his creditor, who has suffered by the appropriation of a fund which otherwise would have been available for the discharge of his claim, may well ask to stand upon this equity, to the extent of the deprivation to which he has been subjected.

13 The decision of Haines J. in *G. Ruso Const. Ltd. v. Laviola* (1976), 27 Chitty's L.J. 136 (Ont. H.C.), on which Mr. Bale relied, is clearly distinguishable, in my view, because there the debtor whose property was taken had no right to require the other debtor to pay in the first instance.

14 Mr. Bale further submitted that there should be no marshalling in this case, because the doubly secured creditor (the bank) had not taken proceedings to enforce its mortgage against 24 Dunloe. Those proceedings were brought by the singly secured

creditor (the plaintiff), who then paid off the bank in order to obtain a discharge of the second mortgage against 24 Dunloe, when he was under no obligation to do so. Mr. Bale argued that the plaintiff could have sold the property to Stieglitz without paying off the second mortgage, and that, in fact, it was Steiglitz, not the plaintiff, who paid off the bank's indebtedness.

15 Although the doctrine of marshalling is usually relied upon in proceedings brought by the doubly secured creditor, I do not think it should be limited to such cases. There was evidence in the case at Bar that Julie Amourgis was in breach of her obligation under the third mortgage to pay the taxes on 24 Dunloe. I do not think the singly secured creditor should be required to stand by and watch his security deteriorate. Nor do I think the plaintiff had any real choice but to pay off the second mortgage to the bank. It would be most unlikely that the purchaser, Stieglitz, would have been willing to assume it, in view of the fact that it was a collateral mortgage. Had he done so, he would have become involved in the dealings between the bank and its debtor, Strawrene.

16 The doctrine of marshalling is intended to achieve fairness. In the absence of any authority to the contrary, I can see no reason why marshalling should be denied in this case simply because the proceedings were brought by the singly secured creditor, and he paid off the doubly secured creditor out of a practical necessity to do so, but without any legal obligation.

17 There is only one other point raised by Mr. Bale that I think should be mentioned, but it provides a complete defence to the claim for marshalling in respect of the fund created by the order of Houlden J.A. It is the equitable rule that marshalling will not be applied to the prejudice of third persons.

18 If the plaintiff is not permitted to be subrogated to the bank's rights against the surplus realized on the sale of 63 Shuter Street by power of sale under the first mortgage, then that surplus would be paid successively to the 3rd, 4th and 5th mortgagees. Most of it would be used to satisfy the 3rd mortgage for \$70,000 to Nugate Holdings Limited. Although I was told by counsel that the plaintiff holds the 3rd mortgage on 24 Dunloe as trustee for the mortgagees under the 3rd, 4th and 5th mortgages on 63 Shuter, there was no evidence that the benefits to them of marshalling would be identical with the benefits they would enjoy from having the surplus applied to one or more of their mortgages. If such benefits were not identical, marshalling, in respect of such surplus, would have the effect in this case of prejudicing the rights of third parties.

19 I do not think it is any answer to this last point to say, as did Mr. Thompson, that the 3rd, 4th and 5th mortgagees would not be prejudiced by marshalling, because they never expected to be given priority over the claim of the bank against 63 Shuter Street under the 2nd mortgage. As it turned out, if marshalling is not permitted, they would be permitted to share the surplus as though they had priority over the bank's 2nd mortgage. It has not been shown that marshalling would not prejudice the rights of some of the 3rd, 4th and 5th mortgagees.

20 There do not appear to be any third parties whose rights would or might be prejudiced by marshalling in respect of the funds accumulated in court under the order of John Holland J. The action will succeed in respect of that fund, but not in respect of the fund held pursuant to the order of Houlden J.A.

21 There will be an order directing that the sum of \$500 be paid forthwith to the bank in respect of its costs in this action out of the moneys paid into court pursuant to the order of John Holland J. dated April 29, 1983. The order will further direct that the bank transfer to the plaintiff its interest in the balance of the moneys paid into court pursuant to the said order of John Holland J., and that the plaintiff be entitled to realize the sum of \$174,937.50 together with interest on that amount from the date of the order at the rate presently being paid for post judgment interest. The defendants Constantine Amourgis, Julie Amourgis and Strawrene Limited will pay to the plaintiff his costs of the action after taxation thereof, and the plaintiff may realize the amount of those costs out of the bank's interest in the funds in court pursuant to the said order of John Holland J., if the funds are sufficient for that purpose.

Order accordingly.

TAB 14

TAB 15

In the Court of Appeal of Alberta

Citation: Griffon Partners Operation Corporation (Re), 2024 ABCA 279

Date: 20240826

Docket: 2401-0142AC

Registry: Calgary

**In the Matter of the *Companies' Creditors Arrangement Act*,
RSC 1985, c C-36 as amended;**

**And in the Matter of the Compromise or Arrangement of Griffon Partners
Operation Corporation, Griffon Partners Holding Corporation, Griffon Partners
Capital Management Ltd., Stellion Limited, 2437801 Alberta Ltd.,
2437799 Alberta Ltd., 2437815 Alberta Ltd. and Spicelo Limited**

Between:

Tamarack Valley Energy Ltd.

Applicant

- and -

**Griffon Partners Operation Corporation, Griffon Partners Holding Corporation, Griffon
Partners Capital Management Ltd., Stellion Limited, 2437801 Alberta Ltd., 2437799
Alberta Ltd., 2437815 Alberta Ltd., and Spicelo Limited**

Respondents

- and -

Alvarez & Marsal Canada Inc., Trafigura Canada Limited and Signal Alpha C4 Limited

Not Parties to the Application

**Reasons for Decision of
The Honourable Justice April Grosse**

Application for Leave to Appeal

Reasons for Decision of The Honourable Justice April Grosse

Introduction

[1] The applicant, Tamarack Valley Energy Ltd., seeks leave to appeal a decision of the Court of King’s Bench rendered in the course of proceedings under the *Companies’ Creditors Arrangement Act*, RSC 1985, c C-36 (CCAA): *Griffon Partners Operation Corporation (Re)*, 2024 ABKB 277 (the marshalling decision). Tamarack is a subordinate secured creditor of the respondent Griffon Partners Operation Corporation (GPOC) pursuant to a \$20 million promissory note secured against all of GPOC’s present and after-acquired property. The chambers judge refused to apply the equitable doctrine of marshalling to require, in effect, that amounts owed to the senior secured creditors be satisfied first from a guarantee granted to the senior creditors by the respondent Spicelo Limited before having resort to proceeds from the sale of GPOC’s assets. The latter sale took place by way of a court-ordered sale and investment solicitation process and resulting reverse vesting order. The net result of the marshalling decision is that Tamarack will not recover on its note.

[2] The senior creditors are not parties to this appeal and have never opposed marshalling. Spicelo and its beneficial shareholder, Mr Klesch, vigorously oppose an order for marshalling. The monitor appointed under the CCAA for GPOC is now also the monitor for Spicelo and takes the position that marshalling is not applicable in these circumstances.

[3] The chambers decision sets out the facts and procedural history in more detail.

[4] Leave to appeal is required pursuant to section 13 of the CCAA. An applicant must demonstrate “serious and arguable grounds that are of real and significant interest to the parties” by reference to the following factors: a) whether the issues raised by the proposed appeal are significant to the practice; b) whether the issues are of significance to the action itself; c) whether the appeal is *prima facie* meritorious or, on the other hand, whether it is frivolous; and d) whether the appeal will unduly hinder the progress of the action: *Liberty Oil & Gas Ltd (Re)*, 2003 ABCA 158 at paras 15-16; *BMO Nesbitt Burns Inc v Bellatrix Exploration Ltd*, 2020 ABCA 264 at para 7. Leave to appeal is generally granted “sparingly”: *Bellatrix* at para 8.

[5] It is agreed that the facts of this case do not fit within the traditional formulation of the doctrine of marshalling, succinctly summarized by the Ontario Court of Appeal as follows:

...the right to marshal securities is an equitable one intended to prevent a creditor who can resort to two funds of a debtor from defeating another creditor who can resort to only one of them. Fundamentally, the doctrine is applied for the purpose of regulating the rights of the two creditors among themselves, although in so regulating their rights the court will never interfere with the paramount claim of the superior creditor (the one which has the choice of the two funds of the debtor from

which to collect) to pursue his or her remedy against either fund, but provides that if he or she resorts to the fund which the inferior creditor can alone resort, then the inferior creditor shall not be prejudiced. The doctrine is applicable unless some other equity prevents its application such as in the case where its application would prejudice third parties. There are five criteria: (a) two creditors; (b) one common debtor; (c) two funds of the debtor with the superior creditor having access to both and the inferior creditor to but one; (d) no interference with the choice of remedy of the superior creditor and (e) no prejudice to third parties.

Green v Bank of Montreal (1999), 128 OAC 324, 16 CBR (4th) 79 at para 10 (ONCA)

[6] Tamarack and the senior lenders are common creditors of GPOC. Both have security against the present and after-acquired property of GPOC. The senior lenders have access to an additional fund not available to Tamarack, but on its face, it is not a fund of the debtor GPOC. Rather, the senior lenders have the benefit of a guarantee from Spicelo. Relatedly, this fact pattern gives rise to Spicelo's argument that it is a third party who would suffer prejudice as a result of marshalling.

[7] Marshalling has been applied in cases where the two funds in issue did not belong to the same debtor and a surety or guarantee was involved: for example, see *Ernst Bros Co v Canada Permanent Mortgage Corp* (1920), 47 OLR 362, aff'd 57 DLR 500 (ONCA); *Brown v Canadian Imperial Bank of Commerce* (1985), 50 OR (2d) 420, 1985 CanLII 2116 (ONSC) (marshalling refused for other reasons). However, the presence of a guarantor or surety is by no means an automatic path to marshalling; it depends on the roles and relationships of the parties: for example, see *Wolfe v Taylor*, 2020 MBCA 44. The chambers judge interpreted the scope of the recognized exception to the single debtor requirement as follows, at para 31:

There clearly is an exception to the general rule that there be one debtor. That exception appears to be that marshalling may be employed in cases involving more than one debtor when one of the debtors can put primary liability upon the other, for example, when the debtors are principal and surety: *Halsbury's Laws of England*, vol. 16, 4th ed (1980) at p 786, para 877. Such a relationship must exist, otherwise it would be inequitable to force one debtor to pay the other's debt when that debtor was not under any obligation to do so: *Paddon*.

[8] The applicant acknowledges that there are no known Canadian examples of a court applying marshalling where the second fund is a guarantee provided by a third party for the benefit of the senior creditor. On the other hand, the parties are not aware of any case that expressly says marshalling cannot apply on these facts.

[9] The merits threshold for leave to appeal in CCAA cases has been formulated in a variety of ways: for example, see *Resurgence Asset Management LLC v Canadian Airlines Corporation*,

2000 ABCA 149 at paras 34-35; *Wells Fargo Securities Canada Ltd v Sanjel Corporation*, 2017 ABCA 120 at para 11; *Wiebe v Weinrich Contracting Ltd*, 2019 ABCA 323 at para 17; *North American Tungsten Corporation v Global Tungsten and Powders Corp*, 2015 BCCA 426 at paras 28 and 40; *Callidus Capital Corporation v 9354-9186 Quebec Inc*, 2018 QCCA 632. In my view, the applicant's proposed appeal is arguable and has sufficient merit to weigh in favour of granting leave to appeal in the context of this case and the issue raised.

[10] The applicant advances a seemingly novel argument, but equitable doctrines and remedies are flexible. Just as courts have made exceptions to the "single debtor rule" in the cases set out above, they could reasonably find such an exception to be equitable on other facts or otherwise relax the criteria for marshalling where justified by the equities in a particular case. The circumstances in this case are such that it is reasonable for the applicant to argue that the equities weigh in its favour and that applying marshalling would be consistent with the principles that underpin the doctrine.

[11] I note that the issue goes beyond a mere challenge to the exercise of discretion of a chambers judge and that the chambers judge did not have an ongoing supervisory role in the CCAA action.

[12] There is no question that the issue raised in the appeal is of significance to the action. Whether Tamarack is able to recover on any of its \$20 million note and how much of the senior creditors' debt may be enforced against Spicelo is important to the parties and will, for the most part, allow for final distributions.

[13] The appeal does not raise an issue that necessarily arises regularly in CCAA cases. However, I accept that it nonetheless has significance to the practice and more generally to the development of the equitable doctrine of marshalling. Based on the jurisprudence cited by the parties, there is appellate authority on the general principles of marshalling but many of the decisions are dated. Most of the cases fleshing out the flexibility of the doctrine and the extent to which the standard criteria can be relaxed in Canada are first instance decisions. Regardless of whether the applicant is ultimately successful, a decision by this Court would contribute to the body of law and it will provide some certainty for parties in similar circumstances as to whether marshalling is potentially available.

[14] The respondents are concerned that the time required for an appeal will interfere with their ability to sell the Greenfire shares pledged as security for the guarantee at a favourable price. While this is a fair concern, I am not convinced that it amounts to undue hinderance of the action in all the circumstances. In pledging the shares, Spicelo accepted the risk that it may lose control over them. Further, the interests of all parties should be aligned to sell the shares at a favourable price. I appreciate that there may be differing views as to what is "favourable". However, there is certainly room for an agreement between the stakeholders as to the sale of some or all of the shares with the proceeds held pending the outcome of the appeal. The parties are expected to work cooperatively to ensure that the appeal is heard in a timely way.

[15] Looking at the factors as a whole, I am satisfied that the proposed appeal raises “serious and arguable grounds that are of real and significant interest to the parties”: *Bellatrix* at para 7; *Liberty* at para 15. The application for leave to appeal the marshalling decision is granted.

Application heard on June 13, 2024

Reasons filed at Calgary, Alberta
this 26th day of August, 2024

Grosse J.A.

Appearances:

M.C.C.L. Lemmens

J. Maslowski

for the Applicant

R.S. Van de Mosselaer

J.L. Treleaven

for the Respondents, with permission of the Monitor

K. Kashuba (not present)

J. Opolsky

for Alvarez & Marsal Canada Inc., Monitor

K.L. Fellowes, KC (not present)

N. Doelman (not present)

for Trafigura Canada Limited and Signal Alpha C4 Limited, Not parties to the Application