Court File No. CV-19-629552-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

B E T W E E N:

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*,
R.S.C. 1985, C. C-36, AS AMENDED
AND IN THE MATTER OF A PLAN OF ARRANGEMENT OF
DEL EQUIPMENT INC.

Applicant

BOOK OF AUTHORITIES OF THE RESPONDING PARTY, GIN-COR INDUSTRIES INC.

Returnable May 5, 2020

May 1, 2020

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2. Canadian Encyclopedic Digest, CED Restitution VIII.1.(d), Restitution, VIII Unjust Enrichment at §530 citing *Garland v. Consumers' Gas Co.* (2004), 2004 CarswellOnt 1558 (S.C.C.)

3. *Toronto Dominion Bank v. Bank of Montreal*, 1995 CarswellOnt 326 (Ont.G.D.)

4. *Royal Bank v. Harowitz*, 1994 CarswellOnt 836, [1994] (Ont.G.D.) aff'd at 1997 CarswellOnt 2609 (CA)

5. *Ierullo v. Rovan*, 2000 CarswellOnt 109, [2000] O.J. No. 108 (SCJ) aff'd at 2001 CarswellOnt 9827 (DivCt)

6. *McDiarmid Lumber Ltd. v. Canadian Imperial Bank of Commerce*, 1992 CarswellBC 268, [1992] (BCSC)

7. *Toronto Dominion Bank v. Carotenuto* 1998 CarswellBC 23 (BCCA)

8. *Sadie Moranis Realty Corp. v. 1667038 Ontario Inc.* 2012 ONCA 475.

9. *News Canada Marketing Inc. v. TD Evergreen*, 2000 CarswellOnt 3544 (SCJ).

10. *Deol v. Morcan Financial Inc.,* 2011 CarswellOnt 13652 (SCJ – Cmml List).

11. *American Axle & Manufacturing Inc. v. Durable Release Coaters Ltd.*, 2007 CarswellOnt 3444 (SCJ).

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Most Negative Treatment: Distinguished
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Supreme Court of Canada

Telford v. Holt

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TELFORD and TELFORD v. HOLT and HOLT

Dickson C.J.C., Estey, McIntyre, Wilson and Le Dain JJ.

Heard: February 27 and March 2, 1987
Judgment: September 17, 1987
Docket: No. 19175

Counsel: *D.E. Jermyn*, for appellants.
J.P. Low, for respondents.

Subject: Insolvency; Civil Practice and Procedure; Property; Corporate and Commercial

Related Abridgment Classifications

Civil practice and procedure
X Pleadings
X.6 Counterclaim, crossclaim and set-off
X.6.b Set-off

Personal property
III Choses in action
III.8 Equities to which assignments subject
III.8.a Right of set-off

Headnote

Bankruptcy

Choses in Action --- Equities to which assignments subject — Right of set-off

Practice --- Pleadings — Counterclaim, crossclaim and set-off — Set-off

Creditors and debtors — Set-off — Set-off in equity — Equitable set-off available for money sum whether liquidated or unliquidated and mutuality of debts not required — Assignment not barring right to equitable set-off — Set-off available where sum due prior to notice of assignment being given or where sum due arising out of or closely connected to same contract or series of events — Debt to be set off must be enforceable — Reciprocal mortgages subject to equitable set-off despite unenforceability of personal covenant in one mortgage — Foreclosure available and equitable set-off not requiring

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symmetry of remedies or amounts.

Creditors and debtors — Set-off — Set-off at law — Set-off available for debts being mutual cross obligations — Assignment of debt destroying mutuality — Set-off at law not available.

Mortgages — Action on covenant to pay — Personal judgment — Availability — Statutory restrictions — Section 41 of Law of Property Act barring action on personal covenant but not creating unenforceable debt as mortgagee still able to pursue foreclosure remedy.

Mortgages — Payment of mortgage — Set-off — Defendant and third party swapping land and exchanging mortgages — Third party assigning mortgage to plaintiff — Plaintiff seeking judgment on mortgage when defendant willing to make payment equalizing balances owing on mortgages and discharge mortgages — Defendant entitled to set-off in equity in foreclosure action — Defendant to make payment and mortgages to be discharged.

C. Ltd and the appellants traded properties, with each receiving cash and a mortgage back from the other. The appellants gave a mortgage for $150,000 and received a mortgage for $100,000. The mortgage given by the appellants was repayable in three equal instalments of $50,000, the last two of which coincided in time and amount with the two payments to be made by C. Ltd. under its mortgage. The mortgages were separate agreements, neither of which referred directly to the other. Prior to the execution of the mortgages C. Ltd assigned its interest in the appellants' mortgage to the respondents. The appellants were not given notice of this assignment. Prior to the date the appellants were to make their first payment they tendered $50,000 plus accrued interest to C. Ltd. on condition that there be a mutual discharge of the mortgages (as upon payment each party then owed the other $100,000). The appellants were then orally advised of the assignment. Negotiations followed and after the due date for the appellants' first payment passed the respondents brought an action on the mortgage for the full $150,000 owed by the appellants. At trial the court held that the appellants did not have right of set-off at the time the proceedings were commenced and the mortgage contracts did not provide for a set-off by agreement. Furthermore, as the covenant to pay in the mortgage could not be enforced against the appellants, because they were individuals, an enforceable debt did not exist which could be set off in law. Therefore the respondents were entitled to succeed in their action on the appellants' mortgage. The majority of the Court of Appeal adopted this opinion, concluding that for set-off to be available both debts must be enforceable by action at the time set-off is directed. The debt owed by the appellant, arising from a covenant to pay on a mortgage given by an individual, was held to be an unenforceable debt. The appellants further appealed.

Held:

Appeal allowed.

In the absence of an agreement for set-off it may be established that there is a right to set-off at law or in equity. Set-off at law requires that the obligations be debts and the debts be mutual cross obligations. Any assignment will destroy the necessary mutuality. Set-off at law was therefore not available because of the assignment by C. Ltd. to the respondents. Set-off in equity is available where there is a claim for a money sum, liquidated or unliquidated, even if there has been an assignment. No mutuality is required. The courts of equity have held that set-off may be claimed against an assignee in respect of a money sum which has accrued and become due prior to notice of the assignment, or in respect of a money sum which arose out of the same contract or series of events which gave rise to the assigned money sum or was closely connected with that contract or series of events. In addition, both debts must be enforceable. The appellants received written notice of the assignment, as required by s. 150 of the Land Titles Act, prior to the time the debt sought to be set off had accrued due, as that debt was the $100,000 remaining owing on the mortgage which had not yet accrued due. Therefore, they could not succeed on the first branch of the test for availability of an equitable set-off. However, the two mortgages were part of a single land exchange deal, each being part of the consideration for the reciprocal transfers. They were closely connected and therefore met the second criterion for the availability of equitable set-off. The mortgages were made with reference to one another and it would be unfair to enforce only the one side of the land exchange agreement. The appellants and C. Ltd. (and the respondent assignees) did have mutually enforceable debts, as s. 41 of the Law of Property Act does not create an unenforceable debt. It does not extinguish or satisfy the debt, it merely precludes a remedy by way of judgment on the covenant. It does not matter that one debt is enforceable only by way of foreclosure, as the availability of equitable set-off does not require symmetry of remedies or amount.

Table of Authorities

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Cases considered:

Aboussafy v. Abacus Cities Ltd., [1981] 4 W.W.R. 660, 39 C.B.R. (N.S.) 1, 124 D.L.R. (3d) 150, 29 A.R. 607 (C.A.) — *applied*

Atlantic Accept. Corp. v. Burns & Dutton Const. (1962) Ltd., [1971] 1 W.W.R. 84, 14 D.L.R. (3d) 175 (Alta. C.A.) — *considered*

Business Computers Ltd. v. Anglo-African Leasing Ltd., [1977] 1 W.L.R. 578, [1977] 2 All E.R. 741 (Ch. D.) — *considered*

Can. Admiral Corp. v. L.F. Dommerich & Co., [1964] S.C.R. 238, 6 C.B.R. (N.S.) 64, 43 D.L.R. (2d) 1 [Ont.] — *considered*

C.I.B.C. v. Tuckerr Indust. Inc., [1983] 5 W.W.R. 602, 46 B.C.L.R. 8, 48 C.B.R. (N.S.) 1, 149 D.L.R. (3d) 172 (C.A.) — *applied*

Coba Indust. Ltd. v. Millie's Hldgs. (Can.) Ltd., [1985] 6 W.W.R. 14, 65 B.C.L.R. 31, 36 R.P.R. 259 (C.A.) — *applied*

Edmonton Airport Hotel Co. v. Credit Foncier Franco-Can., [1965] S.C.R. 441, 51 W.W.R. 431, 50 D.L.R. (2d) 510 [Alta.] — *considered*

Fed. Commerce & Navigation Co. v. Molena Alpha Inc., [1978] Q.B. 927, [1978] 3 W.L.R. 309, [1978] 3 All E.R. 1066 (C.A.) [affirmed in part [1979] A.C. 757, [1978] 3 W.L.R. 991, [1979] 1 All E.R. 307 (H.L.)] — *considered*

Freeman v. Lomas (1851), 9 Hare 109, 68 E.R. 435 — *referred to*

Hanak v. Green, [1958] 2 Q.B. 9, [1958] 2 W.L.R. 755, [1958] 2 All E.R. 141 (C.A.) — *considered*

Nfld. Govt. v. Nfld. Ry. Co. (1888), 13 App. Cas. 199 (P.C.) — *applied*

Pinto Leite & Nephews, Re; Ex parte Des Olivaes, [1929] 1 Ch. 221 — *considered*

Renner v. Racz, [1972] 1 W.W.R. 109, 22 D.L.R. (3d) 443 (Alta. C.A.) — *overruled*

Royal Trust Co. v. Holden (1915), 21 B.C.R. 185, 8 W.W.R. 500, 22 D.L.R. 660 (C.A.) — *considered*

Smith v. Parkes (1852), 16 Beav. 115, 51 E.R. 720 — *referred to*

Watson v. Mid Wales Ry. Co. (1867), L.R. 2 C.P. 593*considered*

Statutes considered:

Insolvent Debtors Relief Act, 1728 U.K. (2 Geo. 2, c. 22)

Land Titles Act, R.S.A. 1980, c. L-5

s. 150

Law of Property Act, R.S.A. 1980, c. L-8

s. 41(1)

s. 43(1)

Set-off Act, 1734 U.K. (8 Geo. 2, c. 24)

Rules considered:

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Alberta Rules of Court

R. 93

Supreme Court Rules, U.K. 1913, Ord. 19,

R. 3

Authorities considered:

42 Hals (4th) 246, para. 421

Words and phrases considered:

EQUITABLE SET-OFF

Equitable set off is available where there is a claim for a money sum whether liquidated or unliquidated: *Abacus Cities Ltd. v. Aboussafy*, [1981] 4 W.W.R. 660 . . . it is available where there has been an assignment. There is no requirement of mutuality.

MUTUAL DEBTS

In *Royal Trust v. Holden* (1915), 22 D.L.R. 660, the British Columbia Court of Appeal discussed the meaning of the phrase "mutual debts" at pp. 662-63:

The expression "mutual debts" is somewhat hard to understand according to the old cases, but when we see in the ancient and approved form of plea given in . . . [S.M.] Leake, Precedents of pleadings in personal actions in the superior courts of common law, 3rd. ed. [London: Stevens, 1868] . . .

That the plaintiff at the commencement of the suit was and still is indebted to the defendant in an amount equal to the plaintiff's claim . . .

we are relieved to find that "mutual debts" mean practically debts due from either party to the other for liquidated sums, or money demands which can be ascertained with certainty at the time of pleading — per Kennedy, L.J., in *Bennett v. White*, [1910] 2 K.B. at 648 . . .

SET-OFF

. . . as was stated by the British Columbia Court of Appeal in *C.I.B.C. v. Tucker Industries Inc.*, [1983] 5 W.W.R. 602 . . . at p. 604 . . . statutory set-off (or set-off at law) "requires the fulfilment of two conditions. The first is that both obligations must be debts. The second is that both debts must be mutual cross obligations."

. . . . .

Equitable set-off is available where there is a claim for a money sum whether liquidated or unliquidated: *Abacus Cities Ltd. v. Aboussafy*, [1981] 4 W.W.R. 660 . . . (Alta. C.A.) at p. 666 . . . it is available where there has been an assignment. There is no requirement of mutuality.

. . . . .

[In *Coba Industries Ltd. v. Millie's Holdings (Can.) Ltd.*, [1985] 6 W.W.R. 14 (B.C. C.A.)] McFarland J.A. reviewed the English authorities and drew from them the following principles at p. 22 . . . :

1. The party relying on a set-off must show some equitable ground for being protected against his adversary's demands: *Rawson v. Samuel*, [1841] . . . 41 E.R. 451 (L.C.)

2. The equitable ground must go to the very root of the plaintiff's claim before a set-off will be allowed: [*Br. Anzani*

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(Felixstowe) Ltd. v. Int. Marine Mgmt (U.K.) Ltd. . . . [1979] 2 All E.R. 1063].

3. A cross-claim must be so clearly connected with the demand of the Plaintiff that it would be manifestly unjust to allow the plaintiff to enforce payment without taking into consideration the cross-claim: [*Fed. Commerce and Navigation Co. v. Molena Alpha Inc.* . . . [1978] 3 All E.R. 1066].

4. The plaintiff's claim and the cross-claim need not arise out of the same contract: *Bankes v. Jarvis*, [1903] 1 K.B. 549 (Div. Ct.); *Br. Anzani*.

5. Unliquidated claims are on the same footing as liquidated claims: [*Nfld. v. Nfld. Ry. Co.*, [1888] 13 App. C. 199 (P.C.)]

STATUTORY SET-OFF

. . . as was stated by the British Columbia Court of Appeal in *Cdn. Imperial Bank of Commerce v. Tuckerr Industries Inc.*, [1983] 5 W.W.R. 602 . . . at p. 604 . . . statutory set-off (or set-off at law) requires the fulfilment of two conditions. The first is that both obligations must be debts. The second is that both debts must be mutual cross obligations.

In *Royal Trust v. Houlden* (1915), 22 D.L.R. 660; The British Columbia Court of Appeal discussed the meaning of the phrase "mutual debts" at pp. 662-62:

. . . "mutual debts" mean practically debts due from either party to the other for liquidated sums, or money demands which can be ascertained with certainty at the time of pleading - per Kennedy L.J., in *Bennett v. White*, [1910] 2 K.B. at 648 . . .

Appeal from judgment, 37 Alta. L.R. (2d) 399, [1985] 4 W.W.R. 573, dismissing appeal from judgment of Foisy J.

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

1. The Facts

1 This appeal concerns a series of transactions entered into by three parties, the Telfords, the Holts and Canadian Stanley Development Ltd., involving contracts for the sale of land and mortgages. The appeal arises out of an action commenced by the Holts alleging default of payment on a mortgage made by the Telfords to Canadian Stanley ("the Telford mortgage"). The Holts had been assigned the Telford mortgage by Canadian Stanley to secure the balance of the purchase price of a piece of land the Holts had sold to Canadian Stanley.

2 The Telford mortgage arose out of a real estate trade between the Telfords and Canadian Stanley. The Telfords sold their land (a domestic residence plus 40 acres) to Canadian Stanley. Canadian Stanley sold a parcel of land to the Telfords. The purchase price for the parcel of land sold by the Telfords to Canadian Stanley was $265,000. The purchase price for the piece of land sold by Canadian Stanley to the Telfords was also $265,000.

3 The transaction between the Telfords and Canadian Stanley required Canadian Stanley to pay the Telfords $165,000 for the Telford land and give a second mortgage back to the Telfords for $100,000 ("the Canadian Stanley mortgage"). The Telfords were to pay Canadian Stanley $115,000 for its parcel of land and give a first mortgage to Canadian Stanley for $150,000. The net effect of the combined transaction was that on closing Canadian Stanley would pay the Telfords $50,000 which the Telfords would use for the purpose of financing the construction of a residence on their new land. The closing date was 1st October 1980.

4 The transaction between the Telfords and Canadian Stanley was closed effective 1st October 1980 by payment by Canadian Stanley to the Telfords of $47,885.93 and the execution and delivery of the Telford mortgage and the Canadian Stanley mortgage. The payment of $47,885.93 by Canadian Stanley was arrived at by subtracting the down payment owed by the Telfords ($115,000) from the down payment owed by Canadian Stanley ($165,000) plus adjustments.

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5 The interest rate on both mortgages was the same, i.e., 14.75 per cent. The last two payments on each mortgage were also the same both as to amount and time of payment. Each mortgagor had to pay $50,000 plus accrued interest on 31st July 1981 and $50,000 plus accrued interest on 31st January 1982. The only difference was that the Telfords also had to pay $50,000 plus interest on 31st January 1981.

6 On 26th September 1980 Canadian Stanley assigned the Telford mortgage to the Holts. The Telfords were not notified of this assign ment. On 5th November 1980 the Telfords met with Mr. Outhwaite, the principal officer and manager of Canadian Stanley. No mention was made of the assignment of the Telford mortgage. Mr. Outhwaite persuaded the Telfords to agree to a postponement of the Canadian Stanley mortgage. The postponement did not affect the date of payment. It did change the order of priority. The effect of the postponement was that the Canadian Stanley mortgage moved from a second position to a third position on the title to the Telford land.

7 On 13th November 1980 the Telfords tendered the first payment of $50,886.60 on the Telford mortgage. As is apparent, this tendering occurred well before the agreed 31st January 1981 due date for the first payment. The payment of $50,886.60 was forwarded to Canadian Stanley's solicitor, Beaumont Proctor, along with a letter which stated:

> I am enclosing herewith my cheque in the amount of $50,886.60 being the amount required to payout and discharge your clients mortgage on the property. The balance of the $150,000 is being offset by the amount owing on your clients mortgage to my client.
>
> The monies are sent in trust that you forward to my office a registerable discharge of mortgage and the duplicate registered mortgage for which I will in turn forward to you a discharge of mortgage for my clients mortgage on your clients property.

8 On 1st December 1980 Beaumont Proctor returned the $50,886.60 to the Telfords' solicitor informing him that they were no longer acting for Canadian Stanley. The firm of Eden and Pirie was now acting for Canadian Stanley. The Telfords' solicitor forwarded the $50,886.60 to Eden and Pirie with the same trust conditions attached as previously.

9 In a letter dated 16th December 1980 Eden and Pirie informed the Telfords' solicitor that the Telford mortgage had been assigned to the Holts. Various negotiations ensued. On 29th January 1981 the Telfords' solicitor indicated that if the matter was not resolved by 6th February 1981 he would proceed with a court application for a discharge of the mortgage. On 2nd February 1981 the Telfords, for the first time, heard from the representatives of the Holts. The Holts' solicitor demanded the payment of the $50,000 plus accrued interest. The Telfords' solicitor asked Eden and Pirie to return the $50,886.60. The funds were refunded on or about 19th February 1981.

10 The Holts filed a statement of claim against the Telfords on 13th March 1981 for $150,000 plus interest. Their claim for the entire amount was based on cl. 3 of the Telford mortgage which provided that upon default of any payment of the principal the whole principal would become payable as if the time frame stipulated for the payment of such principal had expired.

11 After the Telfords received notice of the Holts' statement of claim they paid the $50,886.60 into court.

2. The Courts Below

12

(1) The trial

13 The Holts in their statement of claim asked for the total amount due under the assigned mortgage — $157,375. The Telfords' counterclaim stated that, having paid the $50,000 plus interest into court, they were entitled to a discharge of the mortgage. The trial judge decided that the Telfords owed the Holts $150,000 plus interest. He made an order for sale with a redemption period of one year.

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14 The trial judge held that no notice of the transfer of mortgage was given to the Telfords as required by s. 150(2) of the Land Titles Act, R.S.A. 1980, c. L-5, until the statement of claim was served in the action in March 1981 and that the Holts therefore took the mortgage subject to the state of accounts existing between the Telfords and Canadian Stanley as of the date of service of the notice. He then considered whether there was a right of set-off in existence at that time. First, he concluded that there was no agreement to set-off between the Telfords and Canadian Stanley. In reaching this conclusion he considered the oral evidence of the events leading up to the execution of the mortgage and subsequent documentation. He found that the Telfords believed that, after payment of the sum of $50,000 plus interest due on 31st January 1981, the remaining payments due on the Telford and Canadian Stanley mortgages would set each other off. However, the documents in the two transactions were not drafted so as to provide for a set-off. Each mortgage provided for two payments subsequent to the 31st January 1981 payment. A right of set-off does not arise until the debt or payment on each mortgage becomes due and payable. It follows that there was no enforceable agreement to set-off between the parties.

15 Further, the Telford mortgage was made by the Telfords in their personal capacity as mortgagors and, pursuant to the Law of Property Act, R.S.A. 1980, c. L-8, s. 41(1), the personal covenant is not enforceable as a debt against them. The Canadian Stanley mortgage on the other hand is a mortgage made by a corporation and the personal covenant is enforceable as a debt against the corporation when such debt becomes due and payable under s. 43(1) of the Law of Property Act. The fact that there never was any enforceable debt against the Telfords would, in the trial judge's view, preclude any right of set-off in law.

16 The trial judge found the Holts' claim for $150,000 plus interest well-founded. Clause 3 of the Telford mortgage provided that on default of payment of the principal or interest or any money thereby secured, the whole principal should become payable as if the time frame stipulated for the payment of such principal had expired. The Telfords made a conditional payment in advance of the due date for such payment. The condition attached was that a registrable discharge of the mortgage would be forwarded to the Telfords. Since this condition was never met, payment was not made and the Holts were free to accelerate payment of the entire mortgage.

(2) The Alberta Court of Appeal

Lieberman J.A. (for the majority)

17 The majority stated that the issue on the appeal was not whether there was an agreement for a set-off but whether in the circumstances of this case there could be a set-off between the mortgages in question. This issue was governed by the earlier decision of the Alberta Court of Appeal in *Renner v. Racz*, [1972] 1 W.W.R. 109, 22 D.L.R. (3d) 443. For a court to direct the set-off of one debt against another both debts must be enforceable by action at the time the set-off is directed.

18 The debt owed by the Telfords under the agreement for sale fell into the category of an unenforceable debt. This was how a mortgage debt was characterized by the Supreme Court of Canada in *Edmonton Airport Hotel Co. v. Credit Foncier Franco-Can.*, [1965] S.C.R. 441, 51 W.W.R. 431, 50 D.L.R. (2d) 510. Therefore, the Telfords' claim for set-off could not succeed.

Kerans J.A. (dissenting)

19 Kerans J.A. followed the dissenting judgment in *Renner*. He agreed that a debtor cannot set off an unenforceable debt of his creditor against a debt of his to the creditor which the creditor can enforce. This would be to permit the debtor to, in effect, enforce his unenforceable debt. But Kerans J.A. held that the converse was not true. A creditor who could enforce his debt should be allowed to set it off against a debt owing by him which he could not be forced to pay by personal action. Kerans J.A. found that that was the situation here.

3. The Issue

20 It is not disputed that under the provisions of the Telford mortgage the Telfords owe the Holts $150,000 plus interest.

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The Tel fords submit, however, that they have the right to set off the debt owed to them by Canadian Stanley against the Holts' claim. Their first argument is that the parties agreed to create a right of set-off. Agreement, express or implied, may confer such a right: see *Freeman v. Lomas* (1851), 9 Hare 109, 68 E.R. 435, at p. 114. Whether there is agreement or not is, however, a matter of evidence. The trial judge concluded that there was no such agreement in this case. He said:

> What then was the state of accounts as it existed as at the date of the service of the statement of claim? Was there in fact a right of set-off in existence as at that time? Assuming that the oral evidence adduced as to what transpired prior to the execution of Ex. 18 [the agreement of sale of the Telford land] and subsequent documentation, does not offend the parol evidence rule, a point which was not brought up nor argued, I am of the view that there was not such a right of set-off and that the plaintiffs should succeed.
>
> There is no doubt that the defendants believed that after payment of the sum of $50,000 plus interest due on 31st January 1981 the remaining payments due under Exs. 7 [Telford mortgage] and 17 [Canadian Stanley mortgage] would set each other off. This result they felt would be a logical consequence of the two transactions in question.
>
> However, the documents on the two transactions were drafted in such a way that it was never certain that a right or [sic] set-off would or could arise. A number of contingencies could possibly arise before the right of set-off if any ever existed could be triggered. Firstly, the right of set-off does not arise until the debt or payment on each mortgage becomes due and payable. This was not to occur until firstly the $50,000 payment plus interest due on Ex. 7 on 31st January 1981 had been paid and secondly, until each of the payments for $50,000 plus interest on each mortgage due 31st July 1981 and 31st January 1982 had become due, and this is assuming no intervening factors such as an assignment of either Ex. 7 or Ex. 17 with proper notice or seizure under a writ or other such type of event would occur.

21 The Alberta Court of Appeal stated that whether there was an agreement to set-off was not at issue on the appeal. The Telfords testified that on an occasion prior to the execution of the documents and an occasion subsequent to the execution of the documents Canadian Stanley orally agreed that upon the payment by the Telfords of $50,000 the mortgages would be off-set. This testimony was extremely sketchy. The written agreement, on the other hand, is clear. The parties did not prepare a simple straightforward mortgage from the Telfords to Canadian Stanley for $50,000. Instead, they prepared two separate mortgage documents each of which provided for payments subsequent to the Telfords' payment of $50,000. In these circumstances I think the trial judge was correct in finding that there was no agreement to set-off.

22 In the absence of such an agreement the Telfords must demonstrate that they have a right of set-off at law or a right of set-off in equity.

(1) Set-off at law

23 Set-off at law originally arose from two statutes: the Insolvent Debtors Relief Act, 1728 U.K. (2 Geo. 2, c. 22), and the Set-off Act, 1734 U.K. (8 Geo. 2, c. 24). These statutes were repealed but their effect was preserved in subsequent legislation. In the rules promulgated under the Supreme Court of Judicature Act, 1873 U.K. (36 & 37 Vict., c. 66), the following was included:

> 199.3 A defendant in an action may set-off, or set up by way of counterclaim against the claims of the plaintiff, any right or claim, whether such set-off or counterclaim sound in damages or not, and such set-off or counterclaim shall have the same effect as a cross-action, so as to enable the Court to pronounce a final judgment in the same action, both on the original and on the cross-claim. But the Court or a Judge may, on the application of the plaintiff before trial, if in the opinion of the Court or Judge such set-off or counterclaim cannot be conveniently disposed of in the pending action, or ought not to be allowed, refuse permission to the defendant to avail himself thereof.

24 In Alberta the relevant provisions are found in the Alberta Rules of Court. Rule 93 of the Alberta Rules of Court reads as follows:

> 93(1) A defendant may by way of counterclaim against the plaintiff's claim or cause of action set up any claim or cause of action by the defendant either against the plaintiff alone or one or more of several plaintiffs or against the plaintiff and

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> another person whether a party to the action or not.
>
> (2) All matters which might be pleaded by way of set-off shall if it is desired to set the same up in the action, be pleaded by way of counterclaim.
>
> (3) A counterclaim has the same effect as a cross-action so as to enable the court to pronounce a final judgment in the same action both on the original and on the counterclaim.
>
> (4) The counterclaim shall be conjoined and pleaded with the statement of defence.
>
> (5) A defence to counterclaim shall be conjoined and pleaded with the reply.

The Alberta Court of Appeal discussed the relevant Alberta legislation in *Atlantic Accept. Corp. v. Burns & Dutton Const. (1962) Ltd.*, [1971] 1 W.W.R. 84, 14 D.L.R. (3d) 175. At p. 90 Allen J.A. stated:

> Rule 95 contains provision enabling the court to direct a counterclaim to be excluded or tried separately if it cannot be conveniently disposed of in the same action. Thus it would appear that there are no essential differences in principle between the English R. 199.3 quoted above and our Rules dealing with the same subject matter.
>
> It would therefore seem that decisions of English courts on the question of enforceability of claims sought to be set off by a defendant against a claim of a plaintiff may still be helpful in resolving the problems faced in this case and in dealing with the first question propounded above we find some assistance from certain cases to which I will now refer.

25 The English common law interpretation of the statutory right of set-off is neatly summarized in Halsbury's Laws of England, 4th ed., vol. 42, para. 421:

> 421. Nature of the right. The right conferred by the Statutes of Set-Off was a right to set off mutual debts arising from transactions of a different nature which could be ascertained with certainty at the time of pleading. Thus, no legal set-off could exist against a claim which sounded in damages, nor could a claim which sounded in damages be set off at law against a plaintiff's claim. The fact that a claim was framed in damages precluded the raising of a set-off at law, notwithstanding that the claim might have been differently framed in a way which would have permitted such a set-off. Where a claim for a liquidated debt was joined by a plaintiff with a claim for damages, set-off at law might only be pleaded in defence to the former claim. Set-off at law operates as a defence.

Thus, as was stated by the British Columbia Court of Appeal in *C.I.B.C. v. Tuckerr Indust. Inc.*, [1983] 5 W.W.R. 602 at 604, 46 B.C.L.R. 8, 48 C.B.R. (N.S.) 1, 149 D.L.R. (3d) 172, statutory set-off (or set-off at law) "requires the fulfilment of two conditions. The first is that both obligations must be debts. The second is that both debts must be mutual cross obligations". The claim in this case is a debt. The major hurdle the appellant faces is the requirement of "mutuality".

26 How has this mutuality requirement been interpreted by the courts? In *Royal Trust Co. v. Holden* (1915), 21 B.C.R. 185, 8 W.W.R. 500, 22 D.L.R. 660 (C.A.), the British Columbia Court of Appeal discussed the meaning of the phrase "mutual debts" at pp. 662-63:

> The expression "mutual debts" is somewhat hard to understand according to the old cases, but when we see in the ancient and approved form of plea given in *Bullen v. Leake*, 3rd ed. 682, viz.: —
>
>> That the plaintiff, at the commencement of the suit was and still is indebted to the defendant in an amount equal to the plaintiff's claim ...
>
> we are relieved to find that "mutual debts" mean practically debts due from either party to the other for liquidated sums, or money demands which can be ascertained with certainty at the time of pleading — *per* Kennedy, L.J., in *Bennett v. White*, [1910] 2 K.B. at 648, 79 L.J.K.B. 1133.

It seems that under this definition any assignment would destroy mutuality and hence destroy the possibility of set-off at law.

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This was the view taken by the British Columbia Court of Appeal in *Coba In dust. Ltd. v. Millie's Hldgs. (Can.) Ltd.*, [1985] 6 W.W.R. 14, 65 B.C.L.R. 31, 36 R.P.R. 259 , at pp. 28-29:

> None of the authorities cited by the appellant is applicable to the case before us and none of them detracts in any way from the authority of the *Nfld.* case. Each of them is an example of a set-off at law. In such cases the assignment of a debt prevents fulfilment of the requirement that the debts sought to be set off against each other must be mutual. Once a debt is assigned, it is owed to a third party and the debts are no longer mutual cross-claims: see *C.I.B.C. v. Tuckerr Indust. Inc.*, 46 B.C.L.R. 8, [1983] 5 W.W.R. 602 at 605, 48 C.B.R. (N.S.) 1, 149 D.L.R. (3d) 172 (C.A.).

Since there was an assignment in this case, it appears that a set-off at law is not available to the Telfords. It is necessary, therefore, to decide whether a set-off is available in equity.

(2) Set-off in equity

27 The distinction between set-off at law and set-off in equity was canvassed by the British Columbia Court of Appeal in *C.I.B.C. v. Tuckerr Indust. Inc.*, supra, at p. 605:

> Such a set-off has its origin in equity and does not rest on the statute of 1728. It can apply where mutuality is lost or never existed. It can apply where the cross obligations are not debts.

Equitable set-off is available where there is a claim for a money sum whether liquidated or unliquidated: see *Aboussafy v. Abacus Cities Ltd.*, [1981] 4 W.W.R. 660, 39 C.B.R. (N.S.) 1, 124 D.L.R. (3d) 150, 29 A.R. 607 (C.A.), at p. 666. More importantly in the context of this case, it is available where there has been an assignment. There is no requirement of mutuality. The authorities to be reviewed indicate that courts of equity had two rules regarding the effect of a notice of assignment on the right to set-off. First, an individual may set off against the assignee a money sum which accrued and became due prior to the notice of assignment. And second, an individual may set off against the assignee a money sum which arose out of the same contract or series of events which gave rise to the assigned money sum or was closely connected with that contract or series of events.

28 The first case to consider is *Watson v. Mid Wales Ry. Co.* (1867), L.R. 2 C.P. 593. In that case the assignees of a Lloyd's bond sued the makers of the bond in the name of the original bondholder. The makers sought to set off arrears of rent due from the original bondholder which had accrued due since the notice of the assignment under a lease entered into prior to the notice of assignment. The question was whether a debtor had, in equity, a right to set off against the assignee of his debt a debt to him from his original creditor which has accrued due subsequent to the notice to him of the assignment. The three judges, in separate reasons, answered that a debtor had no right to set-off in such a case. Montague Smith J. said at pp. 600-601:

> If the debt sought to be set off in an action brought on behalf of the assignee of a debt had existed at the time of the transfer, equity would not interfere to restrain the legal set-off which the parties had. But here, at the time of transfer and notice, no debt existed to be set off. It is said that if debts are accruing mutually under independent contracts, neither of which is due at the time of the transfer, the right of set-off exists, if at the time of action brought upon one of them the liability of the other has ripened into a debt actually due. But the time to be looked at is, not the time of action brought, but the time when the transfer was made and notice given, and the rights of parties must be determined by the state of things then existing.

However, each judge made it clear that the answer would be different in a case where "the two transactions were in some way connected together, so as to lead the Court to the conclusion that they were made with reference to one another" (p. 598). For example, Bovill C.J., referring to *Smith v. Parkes* (1852), 16 Beav. 115, 51 E.R. 720, expressed the view at p. 598 that:

> ... the decision went on the footing that both debts arose out of the same partnership dealings and transactions, and were inseparably connected together. That case, therefore, is not applicable to the one before us, where the transactions appear entirely separate, and where we have no allegation or statement from which we can infer any connection to have existed.

29 *Nfld. Govt. v. Nfld. Ry. Co.* (1888), 13 App. Cas. 199 (P.C.), is the seminal case on the right to set off debts arising

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under the same or interrelated contracts. The court construed the contract before it in that case and concluded that (1) each claim by the railway to a grant of land from the Newfoundland government was complete at the time the construction of the railway section which was the quid pro quo for the grant was completed and (2) upon the completion of construction of each section a proportionate part of the government subsidy became payable for the specified term subject to the condition of continuous efficient operation. On 15th July 1882 the railway assigned the southern division of the railway to another company. On 20th April 1886 the railway, according to the contract, should have been completed. It was not completed. The government, therefore, ceased making the requisite payments. The assignee made a claim for these payments. The government of Newfoundland counterclaimed for unliquidated damages against the assignees of the railway company. Their Lordships stated at pp. 212-13:

> The present case is entirely different from any of those cited by the plaintiffs' counsel. The two claims under consideration have their origin in the same portion of the same contract, where the obligations which gave rise to them are intertwined in the closest manner. The claim of the Government does not arise from any fresh transaction freely entered into by it after notice of assignment by the company. It was utterly powerless to prevent the company from inflicting injury on it by breaking the contract. It would be a lamentable thing if it were found to be the law that a party to a contract may assign a portion of it, perhaps a beneficial portion, so that the assignee shall take the benefit, wholly discharged of any counter-claim by the other party in respect of the rest of the contract, which may be burdensome. There is no universal rule that claims arising out of the same contract may be set against one another in all circumstances. But their Lordships have no hesitation in saying that in this contract the claims for subsidy and for non-construction ought to be set against one another.
>
> It is hardly necessary to cite authorities for a conclusion resting on such well-known principles. Their Lordships will only refer to *Smith v. Parkes* [16 Beav. 115], not so much on account of the decision as for the sake of quoting a concise statement by Lord Romilly of the principle which governed it. He says, "All the debts sought to be set off against the defendant Parkes are debts either actually due from him at the time of the execution of the deed" (this was the deed by which the third party who resisted the set-off was brought in) "or flowing out of and inseparably connected with his previous dealings and transactions with the firm." That was a case of equitable set-off, and was decided in 1852, when unliquidated damages could not by law be the subject of set-off. That law was not found conducive to justice, and has been altered. Unliquidated damages may now be set off as between the original parties, and also against an assignee if flowing out of and inseparably connected with the dealings and transactions which also give rise to the subject of the assignment.

30 The court found that the government was entitled to set off their counterclaim against the assignees' claim since the claim and counterclaim had their origin in the same portion of the same contract and the obligations which gave rise to them were closely intertwined.

31 In *Re Pinto Leite & Nephews; Ex parte Des Olivaes*, [1929] 1 Ch. 221, the question was whether a trustee was entitled to set off the debt of £15,000 which became due after receipt of the notice of assignment. The court held that although the liability existed at or before the date of the notice of assignment, yet as that debt had not then accrued due, it was not debitum in praesenti and therefore was not a debt which the trustee was entitled to set off. Clauson J. stated at p. 233:

> It is, of course, well settled that the assignee of a chose in action ... takes subject to all rights of set-off which were available against the assignor, subject only to the exception that, after notice of an equitable assignment of a chose in action, a debtor cannot set off against the assignee a debt which accrues due subsequently to the date of notice, even though that debt may arise out of a liability which existed at or before the date of the notice; but the debtor may set off as against the assignee a debt which accrues due before notice of the assignment, although it is not payable until after that date.

And at p. 236 he further stated:

> ... when the debt assigned is at the date of notice of the assignment payable in futuro, the debtor can set off against the assignee a debt which becomes payable by the assignor to the debtor after notice of assignment, but before the assigned debt becomes payable, if, but only if, the debt so to be set off was debitum in praesenti at the date of notice of assignment.

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Clauson J. then went on to add at p. 236:

> In order to prevent any misunderstanding I ought to make it clear that it is not suggested that the debt assigned, and the liabilities sought to be set off against it, are so connected as to bring the case within the authorities of which the case of *Government of Newfoundland v. Newfoundland Ry. Co.* is typical.

32 In *Business Computers Ltd. v. Anglo-African Leasing Ltd.*, [1977] 1 W.L.R. 578, [1977] 2 All E.R. 741 (Ch. D.), the defendant owed the plaintiff £10,587 in respect of two transactions for computers bought by the defendant and sold on hire purchase to third parties. Under a third transaction the plaintiff manufactured a computer for its own use, sold it to the defendant, and by a hire purchase agreement leased it back. The plaintiff became insolvent and a receiver was appointed on 17th June 1974. By 17th June the defendant was entitled under a condition of the hire purchase agreement to terminate that agreement. It did not do so. On 31st July the receiver repudiated the agreement. On 8th August the defendant accepted the repudiation. It sold the computer and claimed a sum in excess of £32,000 as damages under another condition of the hire purchase agreement. Templeman J. reviewed the relevant authorities and concluded at p. 585:

> The result of the relevant authorities is that a debt which accrues due before notice of an assignment is received, whether or not it is payable before that date, or a debt which arises out of the same contract as that which gives rise to the assigned debt, or is closely connected with that contract, may be set off against the assignee. But a debt which is neither accrued nor connected may not be set off even though it arises from a contract made before the assignment.

He found that in this case the debt was neither accrued nor connected. There was, accordingly, no right of set-off.

33 In *Can. Admiral Corp. v. L.F. Dommerich & Co.*, [1964] S.C.R. 238, 6 C.B.R. (N.S.) 64, 43 D.L.R. (2d) 1 [Ont.], this court affirmed the rule that a debt which has accrued due before a notice of assignment is received may be set off against the assignee. In that case an assignee sought to claim money from a corporation. The corporation sought to set off a debt owed to it by the assignor. This debt had accrued due prior to the notice of assignment. The court allowed the set-off stating at p. 240: "There is no doubt as to the general rule. The debtor has as against the assignee the same right of set-off as he would have had against the assignor at the time at which he receives notice of the assignment".

34 Thus, cases involving debts that arise from the same contract or closely interrelated contracts form an exception to the general rule. In these cases a debt arising out of the contract or closely interrelated contracts may be set off against the assignee even if the debt accrues due after the notice of the assignment. The issue in our case therefore turns on whether the debt assigned and the liability sought to be set off against it were so connected as to fall within the principle of the *Nfld. Ry.* case.

35 I have found no judgment of this court in which an equitable set-off was permitted on the *Nfld. Ry.* principle. Nor was any cited to us. However, in *Coba Indust.*, supra, the British Columbia Court of Appeal applied the *Nfld. Ry.* case to the following transaction. The respondents bought a commercial property from one Polacco. The interim agreement provided for a second mortgage to be given to Polacco and for Polacco to lease the premises from the respondents for a period of three years. During the lease the respondents were to make second mortgage payments of approximately $5,000 to Polacco and Polacco was to make monthly payments of approximately $10,000 to the respondents. Post-dated cheques were exchanged. Polacco almost immediately assigned his second mortgage to the petitioner and endorsed over all of the respondents' cheques. Shortly thereafter Polacco defaulted on his lease payments. The mortgage went into default and the petitioner commenced foreclosure proceedings. The respondents successfully applied for a declaration that they were entitled to an equitable set-off against amounts owing under the mortgage to the petitioner. The petitioner's appeal was dismissed. Macfarlane J.A. reviewed the English authorities and drew from them the following principles at p. 22:

> 1. The party relying on a set-off must show some equitable ground for being protected against his adversary's demands: *Rawson v. Samuel* (1841), Cr. & Ph. 161, 41 E.R. 451 (L.C.).
>
> 2. The equitable ground must go to the very root of the plaintiff's claim before a set-off will be allowed: [*Br. Anzani (Felixstowe) Ltd. v. Int. Marine Mgmt. (U.K.) Ltd.*, [1980] Q.B. 137, [1979] 3 W.L.R. 451, [1979] 2 All E.R. 1063].
>
> 3. A cross-claim must be so clearly connected with the demand of the plaintiff that it would be manifestly unjust to

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allow the plaintiff to enforce payment without taking into consideration the cross-claim: [*Fed. Commerce and Navigation Co. v. Molena Alpha Inc.*, [1978] Q.B. 927, [1978] 3 W.L.R. 309, [1978] 3 All E.R. 1066].

4. The plaintiff's claim and the cross-claim need not arise out of the same contract: *Bankes v. Jarvis*, [1903] 1 K.B. 549 (Div. Ct.);*Br Anzani*.

5. Unliquidated claims are on the same footing as liquidated claims: [*Nfld. v. Nfld. Ry. Co.* (1888), 13 App. Cas. 199 (P.C.)].

36 Macfarlane J.A. found that although the mortgage and lease were separate documents evidencing two different legal relationships and did not refer to one another, and although the amounts payable and the payment dates were totally different in each document, the evidence disclosed that the lease payments were intended by the parties to be the source of the funds required to satisfy the mortgage payments. This was why the term of the lease exceeded the term of the mortgage and the amounts payable under the lease exceeded the amounts falling due on the mortgage. In view of the connection between them the differences in the two documents were immaterial.

37 The English Court of Appeal decision in *Hanak v. Green*, [1958] 2 Q.B. 9, [1958] 2 W.L.R. 755, [1958] 2 All E.R. 141, on which Macfarlane J.A. placed substantial reliance for the interrelated obligations principle, involved an action by the plaintiff against the builder for failure to complete the construction of a house. The builder counterclaimed or claimed by way of set-off on a quantum meruit for extras outside the purview of the contract. The Court of Appeal held that the defendant had an equitable set-off which totally defeated the plaintiff's claim. Because of the close relationship between the dealings which gave rise to the respective claims, equity would not permit one of them to be insisted upon without taking the other into account. The *Nfld. Ry.* case was followed.

38 Macfarlane J.A. relied also on the English Court of Appeal decision in the *Fed. Commerce* case, supra, where charterers of a vessel were held entitled to deduct from hire by way of equitable set-off claims which they had against the shipowners. The case is interesting because Lord Denning indicates in the course of his reasons that it is no longer necessary since the merger of law and equity to probe the technicalities of the common law of set-off. He said ([1978] 3 All E.R. 1066) at p. 1078:

> Over 100 years have passed since the Supreme Court of Judicature Act 1873. During that time the streams of common law and equity have flown together and combined so as to be indistinguishable the one from the other. We have no longer to ask ourselves: what would the courts of common law or the courts of equity have done before the Supreme Court of Judicature Act 1873? We have to ask ourselves: what should we do now so as to ensure fair dealing between the parties? (see *United Scientific Holdings Ltd v. Burnley Borough Council* [[1977] 2 All E.R. 62 at 68, [1977] 2 W.L.R. 806 at 811-12] per Lord Diplock). This question must be asked in each case as it arises for decision; and then, from case to case, we shall build up a series of precedents to guide those who come after us. But one thing is quite clear: it is not every cross-claim which can be deducted. It is only cross-claims that arise out of the same transaction or are closely connected with it. And it is only cross-claims which go directly to impeach the plaintiff's demands, that is, so closely connected with his demands that it would be manifestly unjust to allow him to enforce payment without taking into account the cross-claim.

The court held that it would be unfair for the creditor to be paid his claim without allowing the debtor to raise an equity against the creditor in the form of his own claim to the extent it had been held to be well-founded.

39 I return now to the facts of this case in order to determine the effect of the notice of assignment on the Telfords' claim for set-off. Section 150 of the Land Titles Act, R.S.A. 1980, c. L-5, identifies the prerequisites for an effective assignment of a mortgage. Section 150 states:

> 150(1) Any contract in writing for the sale and purchase of any land, mortgage or encumbrance is assignable notwithstanding anything to the contrary therein contained, and any assignment of any such contract operates according to its terms to transfer to the assignee therein mentioned all the right, title and interest of the assignor both at law and in equity, subject to the conditions and stipulations contained in the assignment.

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(2) Nothing in this section shall be deemed to affect any rights at law or in equity of the original vendor or owner of the land, mortgage or encumbrance, until notice in writing of the assignment has been either sent to him by registered mail or served on him in the way process is usually served, and the notice mentioned in section 134 shall be deemed to be such notice.

The Telfords did not receive any notice of assignment in compliance with the provisions of this statute until the Holts filed their notice of statement of claim. The date of notice of assignment was accordingly 13th March 1981. Under the original schedule of payments the only debt which accrued due prior to 13th March 1981 was the 31st January 1981 payment of $50,000 from the Telfords to Canadian Stanley. The debts which the Telfords are seeking to set off did not accrue due before the date of the notice of assignment. Thus, the debts can be set off only if the Telfords can demonstrate that they arise out of the same contract or closely interrelated contracts. In my view, the Telfords have succeeded in demonstrating this. In essence, what happened here was that the Telfords and Canadian Stanley "swapped" parcels of land. The Telfords bought land from Canadian Stanley and gave a mortgage to Canadian Stanley but they also sold land to, and received a mortgage from, Canadian Stanley. The mortgages were entered into on the same date. The purchase price for both parcels was the same, namely, $265,000. Except for the 31st January 1981 payment the payments under the two mortgages were on the same dates and for the same amounts. It is these two latter payments under the Canadian Stanley mortgage and the Telford mortgage that the Telfords seek to set off against each other. Because the Telford mortgage and the Canadian Stanley mortgage are part of the land exchange deal, being part of the consideration for the reciprocal transfers, they are, in my view, closely connected and meet the requirements for an equitable set-off. They were made with reference to one another. It would be unfair to enforce only one side of the land exchange agreement.

40 However, the Telfords have one more obstacle to overcome, namely, the view expressed by the Alberta Court of Appeal that their debt was unenforceable and could not be set off for that reason. In reaching this conclusion the majority of the Court of Appeal followed their own earlier precedent in *Renner v. Racz*, supra. In *Renner* the court considered the Alberta Law of Property Act, R.S.A. 1980, c. L-8. Section 41(1) of that Act states:

41(1) In an action brought on a mortgage of land, whether legal or equitable, or on an agreement for the sale of land, the right of the mortgagee or vendor is restricted to the land to which the mortgage or agreement relates and to foreclosure of the mortgage or cancellation of the agreement for sale, as the case may be, and no action lies

(*a*) on a covenant for payment contained in the mortgage or agreement for sale,

(*b*) on any covenant, whether express or implied, by or on the part of a person to whom the land comprised in the mortgage or agreement for sale has been transferred or assigned subject to the mortgage or agreement for the payment of the principal money or purchase money payable under the mortgage or agreement or part thereof, as the case may be, or

(*c*) for damages based on the sale or forfeiture for taxes of land included in the mortgage or agreement for sale, whether or not the sale or forfeiture was due to, or the result of, the default of the mortgagor or purchaser of the land or of the transferee or assignee from the mortgagor or purchaser.

Section 43(1) states:

43(1) Sections 41 and 42 do not apply to a proceeding for the enforcement of any provision

(*a*) of any agreement for sale of land to a corporation, or

(*b*) of a mortgage given by a corporation.

41 The Court of Appeal, in interpreting these sections, made reference to this court's judgment in *Edmonton Airport Hotel Co. v. Credit Foncier Franco-Can.*, supra, and, in particular, to the court's observation that the predecessor section to s. 41 created "an unenforceable debt". The Alberta Court of Appeal concluded therefore that in a case where the debt was a mortgage debt and where, because of the statute, an action on the personal covenant was not available, the court could not

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order set-off. It could not order set-off because there was no enforceable debt.

42 With respect, I must disagree with this interpretation of the *Edmonton Airport Hotel* case. This court's comment in that case must be viewed in context. In *Edmonton Airport Hotel* a guarantor had given a personal guarantee in respect of a mortgagor's indebtedness. The guarantor argued that any guarantee of any mortgage indebtedness is void under the terms of the statute as an indirect method of attempting to impose personal liability under the mortgage. The court disagreed since the guarantor was not (and could not be) the mortgagor. In the course of its reasoning the court said at pp. 444-45:

> As to the guarantee, Superstein submitted that he was under no liability as guarantor since there was no debt owing by the principal debtor. He said that the effect of s. 34(17)(*a*) was to render it impossible that there should be any debt owing by the hotel company. The simple answer is that the hotel borrowed money from Credit Foncier on the security of land and chattels. This borrowing was neither illegal nor *ultra vires* and gave rise to a debt. *Swan v. Bank of Scotland* [(1836), 10 Bli. N.S. 627] does not apply. It was a case of illegality. But here, s. 34(17) is a procedural limitation. There was a borrowing and there was an unenforceable debt which will not disappear by the terms of s. 34(18) until a vesting order is made.

In my view, the court was emphasizing that enforcing the guarantee was not equivalent to enforcing a mortgagor's personal covenant. The reference to the unenforceable debt was simply a reference to the fact that a mortgagor's personal covenant for payment is unenforceable under the terms of the statute. Section 41 does not create an unenforceable debt. Section 41 does not extinguish or satisfy the debt. It merely precludes the remedy by way of a personal judgment against the mortgagor on the covenant. The mortgagee may still pursue the remedy of foreclosure. Therefore, both the Telfords and Canadian Stanley have enforceable debts. It is true that pursuant to the statute a different range of remedies is available to an individual from that available to a corporation. Set-off does not however require either symmetry of remedies or of amounts.

4. Conclusion

43 In summary, the Telfords are not entitled to legal set-off because the debts are not mutual. The Telfords are entitled to equitable set-off because they are entitled to set off against the assignee, the Holts, a money sum which arises out of the same contract or interrelated contracts which gave rise to the assigned money sum. The provisions of the Alberta Law of Property Act do not preclude this result.

44 The appeal is allowed. The balance due on the Telford mortgage is the sum of $50,886.60 and, upon the payment of that amount by the Telfords to the Holts, the order for foreclosure should be vacated or set aside and the mortgage expunged from the title. The appellants should have their costs both here and in the courts below to be withheld from the said sum of $50,886.60.

Appeal allowed.

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TAB 2

CED Restitution VIII.1.(d)

Canadian Encyclopedic Digest

Restitution
VIII — Unjust Enrichment
1 — Determination of Unjust Enrichment
(d) — Absence of Juristic Reason

For print citation information and the currency of the title, please click here.

VIII.1.(d)

See Canadian Abridgment: RST.I.2.c Restitution and unjust enrichment — General principles — Requirements for unjust enrichment — No juristic reason for enrichment

§529 The third requirement in order to establish an unjust enrichment is an absence of any juristic reason for an enrichment of the defendant and a corresponding deprivation of the plaintiff.[1]

§530 To determine whether there is an absence of a juristic reason, the Supreme Court has set out a two step process. First, the claimant must show that the circumstances are not within any of the established categories for denial of recovery, including the existence of a contract, disposition of law, donative intent or other valid statutory, common law or equitable obligations. Once the claimant has demonstrated that no established category applies, the claimant has a *prima facie* case for unjust enrichment. The second step allows the defendant to rebut the *prima facie* claim by demonstrating another reason for denying recovery. At this step, the court may examine the reasonable expectations of the party, public policy arguments and all other circumstances of the situation to determine whether a reason exists to deny recovery.[2]

§531 Legislative purpose is a relevant consideration when considering whether there is a policy reason for refusing to grant unjust enrichment.[3]

§532 If a person invests in a limited company as a result of improper advice given to the person by his or her investment adviser in breach of a fiduciary duty, a claim by the person against one of the principal shareholders of the company based on unjust enrichment will fail when the principal shareholder did not know of the improper advice or the source of the funds to the company. Where no impropriety can be shown in the payment to the defendant shareholder and there are no facts upon which the court can conclude there is no juristic reason for the shareholder to receive the funds paid, fairness does not require that the shareholder be deprived of funds lawfully received to reimburse the investor.[4]

§533 If an equipment lessor fails to make the required registrations under personal property security legislation to protect its leasehold interest and as a result registered secured creditors have priority over the equipment lessor's interest, the receiver acting on behalf of the secured creditors may use the equipment without paying for its use under the equipment leases as the failure to make the necessary registrations to maintain priority is a juristic reason for the enrichment of the secured creditors.[5]

§534 If provincial legislation provides that retail taxes collected by retailers are deemed to be held in trust for the Crown but in the case of bankruptcy, such provincial legislation cannot change the priorities provided for under federal bankruptcy legislation, the federal bankruptcy legislation constitutes a juristic reason for the trustee in bankruptcy to distribute funds in accordance with federal legislation to the detriment of some and the enrichment of others as compared to what they would have received under provincial legislation.[6] However, a legislative scheme which regulates the parties may not constitute a juristic reason if the statute does not bar equitable remedies or is not a complete code.[7]

§535 The failure of a lawyer to disclose his fees prior to provision of legal services, contrary to his professional obligations, was held to constitute a juristic reason to bar recovery of otherwise legitimate fees.[8]

§536 A probated will in which property is left to certain beneficiaries can constitute a juristic reason for an enrichment of the beneficiaries.[9]

§537 An employment contract can constitute a juristic reason for an enrichment.[10] This may be so even if afterwards the employee believes that he or she should have been paid more.[11]

§538 A contract between the parties can constitute a juristic reason for an enrichment of the defendant by the plaintiff,[12] however, it is not necessary for an enforceable contractual obligation to have existed between the parties in order to find a juristic reason for the enrichment.[13] If, however, the defendant does not know about a contract between other parties under

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which a benefit is conferred on the defendant, nor does the defendant acquiesce in such contract and has no special relationship with the plaintiff, such as a contractual, fiduciary or matrimonial relationship, then the remedy of unjust enrichment will not be granted, absent exceptional circumstances.[14]

§539 In some circumstances where an enrichment and a corresponding deprivation have occurred in a contractual setting and no remedy is provided for in the contract to remedy an unjust enrichment, the contractual setting may not constitute a juristic reason for an unjust enrichment.[15]

§540 If a plaintiff's action against the defendant is dismissed as contravening a limitations statute and a subsequent claim is brought by the plaintiff against the defendant for unjust enrichment based on the same evidence, a juristic reason, being the expiration of the limitation period, may be found to exist for the enrichment of the defendant.[16]

§541 A final judgment of a foreign court recognized by the domestic court constitutes a juristic reason for an enrichment.[17] A valid court order from which appeal is not taken, which is final and binding on the parties, constitutes a juristic reason for enrichment.[18]

§542 The fact that only a purchaser only holds a default judgment to the title of land is not a juristic reason to bar recovery of improvements made to land, however, upon notice of a motion to set aside default judgment, any further improvements will be at the risk of the purchaser and will not be recoverable.[19]

§543 A juristic reason for an enrichment does not have to be connected to the party making the claim of unjust enrichment; a legitimate transaction between other parties may be enough.[20]

§544 A former valid statute now repealed can constitute a juristic reason for the retention of a benefit for what would otherwise constitute an unjust enrichment, even if such statute would, if still in existence today, by present day laws be considered invalid.[21]

§545 The rents received from properties conveyed contrary to legislation governing fraudulent conveyances, and retained and rented out by transferees who were not *bona fide* purchasers for value, are subject to a constructive trust to prevent unjust enrichment.[22]

§546 To determine whether there is an absence of juristic reason for an enrichment, the court must consider not only what is fair to the plaintiff but also what is fair to the defendant.[23] Since unjust enrichment is an equitable remedy the party claiming it must establish that its conduct leading to the deprivation was untainted.[24]

§547 Many of the cases in which unjust enrichment is found have dealt with spouses or cohabitants who have contributed financially or through labour to the relationship but where one party has acquired property in his or her own name. In such a situation, there is clearly a benefit conferred and a corresponding deprivation. The reasonable expectations of such parties is not an established category of juristic reason for enrichment. Such expectations are only directly relevant to the second step of the analysis in which the defendant may argue the expectations of the parties are a reason to deny recovery. For instance, the defendant may allege that domestic services provided were part of a bargain which existed between the parties. In that case, the defendant must demonstrate the bargain was based on the expectations of both parties and the court must find that based on those expectations, the retention of the benefit is just.[25]

§548 Cohabitation by itself does not constitute a juristic reason for an unjust enrichment as there is no general duty presumed by law on a common law spouse, or a person about to become such, to perform work or services or to pay the other cohabitant to use his or her property.[26] When two persons cohabit and provide mutual home maintenance, each person's work cancels out the other.[27] Further, the court is not to automatically impose an equal interest where one person contributes to the property held in the name of the other.[28]

§549 Each party may have made important contributions to a venture so that their claims for relief offset each other. Mutual enrichments should mainly be considered at the defence and remedy stages but they may be considered at the juristic reason stage to the extent that the provision of reciprocal benefits constituted relevant evidence of the existence of juristic reason for the enrichment.[29]

Footnotes

1 *Mellco Developments Ltd. v. Portage la Prairie (City)* (2001), 11 C.L.R. (3d) 227 (Man. Q.B.); affirmed (2002), 19 C.L.R. (3d) 1 (Man. C.A.); leave to appeal refused (2003), 2003 CarswellMan 106 (S.C.C.) (juristic reason for enrichment shown in request for land development proposal when competitor to plaintiffs convincing city to deal with it instead of plaintiffs to develop land and competitor paying purchase price for land); *United Canso Oil & Gas Ltd. v. Washoe Northern Inc.* (1991), 121 A.R. 1 (Alta. Q.B.) (incorrect construction of complex oil and gas agreements resulting in improper accounting procedures; agreements not addressing question of improper distribution of fruits of contracts; implied term requiring restitution if distribution improper; valid contracts not constituting juristic reason for refusing plaintiff's claim in unjust enrichment); *Bezdek v. Bezdek* (2002), 165 Man. R. (2d) 127

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(Man. Q.B.) (wife left inheritance by her father; in division of matrimonial property, inheritance to be shared equally with husband; no unjust enrichment as juristic reason for sharing; during marriage wife treating inheritance as joint asset by using it to purchase other property in joint names with husband); *Maple Valley Acres Ltd. v. Canadian Imperial Bank of Commerce* (2003), 2003 CarswellOnt 4592 (Ont. C.A.) (mortgagor giving undertaking to bank to provide it with first mortgage as security for loan; mortgagor having given first and second mortgages to vendor; bank's solicitor obtaining postponement of first and second mortgages to bank's third mortgage by misrepresentation; mortgagor's undertaking to provide first mortgage to bank not juristic reason to justify unjust enrichment at expense of prior mortgagees); *West Shore Ventures Ltd. v. K.P.N. Holding Ltd.* (2001), 152 B.C.A.C. 55 (B.C. C.A.); leave to appeal refused (2001), 166 B.C.A.C. 160 (note) (S.C.C.) (tenant defaulting under lease and becoming bankrupt; bank paying landlord under letter of credit provided for tenant; bank in turn realizing on security provided by plaintiff for letter of credit to be issued; letter of credit providing any excess received by landlord to be returned; under bankruptcy and commercial tenancy legislation amount owed by bankrupt tenant less than amount received under letter of credit; landlord to refund excess to plaintiff as unjust enrichment); *Bratsch Holding Inc. v. LeBrooy* (1996), 73 B.C.A.C. 244 (B.C. C.A.) (agreement specifying that deposit not refundable; agreement made without authority; no juristic reason for enrichment when agreement void ab initio); *Hill Estate v. Chevron Standard Ltd.* (1992), [1993] 2 W.W.R. 545 (Man. C.A.); leave to appeal refused (1993), [1993] 4 W.W.R. lxvii (S.C.C.) (mental incapacity of landowner invalidating power of attorney granted to wife and lease to oil company given by wife; oil company enriching estate and suffering deprivation, but juristic reason for deprivation being oil company's trespass); *Man-Shield (Alberta) Construction Inc. v. 1117398 Alberta Ltd.* (2007), 2007 CarswellAlta 1347 (Alta. Master) (contractor missing time line for filing builders' lien under *Builders' Lien Act* not constituting juristic reason to summarily dismiss claim for unjust enrichment).

2 *Garland v. Consumers' Gas Co.* (2004), 2004 CarswellOnt 1558 (S.C.C.).

3 *Safeway Shouldering Ltd. v. Nackawic (Town)* (2001), 17 M.P.L.R. (3d) 118 (N.B. C.A.) (contractor carrying out road work for municipality without signed contract; statute requiring all municipal contracts to be in writing under seal except those contracts exempted by regulation; no regulations passed; absurd result if all municipal contracts required to be in writing under seal; municipality standing by and watching work being done, unjust not to pay; legislative purpose not undermined); *Hussey Seating Co. (Canada) Ltd. v. Ottawa (City)* (1997), 32 O.R. (3d) 633 (Ont. Gen. Div.); additional reasons at (1997), 145 D.L.R. (4th) 493 at 499 (Ont. Gen. Div.); affirmed (1998), 41 O.R. (3d) 254 (Ont. C.A.) (plaintiff supplying stadium seating to club before bankruptcy; club's stadium lease with city contemplating new seating and other improvements and requiring city's approval for all improvements; city forgoing certain revenues but never agreeing to pay club for improvements; city not liable to pay for seating; not certain that city would otherwise refurbish stadium or that city capable of recovering cost from other users; plaintiff failing to protect itself under *Construction Lien Act* or negotiate contract better anticipating club's bankruptcy; returning stadium to earlier state impractical); *Central Guaranty Trust Co. v. Dixdale Mortgage Investment Corp.* (1994), 24 O.R. (3d) 506 (Ont. C.A.) (plaintiff first mortgagee registering discharge of mortgage by mistake; second mortgagee selling property under power of sale but not relying on discharge of first mortgage; plaintiff's claim of unjust enrichment allowed; *Registry Act* not expressly forbidding claim and purpose not undermined by allowing plaintiff to recover); *Scotia Mortgage Corp. v. Ludwig* (2010), 2010 CarswellBC 387 (B.C. S.C.) (in some limited circumstances, courts will not permit party to rely on state of title certificate if result is unjust enrichment).

4 *Brodie v. Thomson Kernaghan & Co.* (2002), 27 B.L.R. (3d) 246 (Ont. S.C.J.).

5 *British Columbia Central Credit Union v. Skyview Hotels Ltd.* (1993), [1994] 2 W.W.R. 341 (Alta. Q.B.) (lessor's failure to perfect security interest providing juristic reason for enriching receiver; *Personal Property Security Act* not providing otherwise); *Best, Re* (1997), 33 O.R. (3d) 416 (Ont. Bktcy.) (incorrect personal property security registration by vendor of boat resulting in trustee in bankruptcy of purchaser taking free of vendor's interest in boat; vendor suffering deprivation but trustee having juristic reason for enrichment resulting from failure of vendor to follow requirements of personal property security legislation); **see also** *KBA Canada Inc. v. 3S Printers Inc.* (2014), 2014 CarswellBC 832 (B.C. C.A.) (claimant registered security interest in printing press under *Personal Property Security Act* which was mistakenly discharged without his notice, knowledge or direction; Court of Appeal concluded that Act did not allow court to exercise equitable jurisdiction to override balance of statutory priorities scheme).

6 *British Columbia v. National Bank of Canada* (1994), [1995] 2 W.W.R. 305 (B.C. C.A.); leave to appeal refused (1995), [1995] 9 W.W.R. lxxix (note) (S.C.C.) (security agreement and priority scheme of *Bankruptcy and Insolvency Act* justifying enrichment).

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7 *Apotex Inc. v. Abbott Laboratories Ltd.* (2010), 2010 CarswellOnt 9625 (Ont. S.C.J.) (generic drug manufacturer claimed unjust enrichment of patent holder who allegedly put forward unmeritorious claim of infringement in order to delay introduction of generic drug into market; not plain and obvious regulation is complete code dealing with remedies; motion to strike dismissed).

8 *Gutheil v. Billesberger* (2010), 2010 CarswellSask 637 (Sask. Q.B.).

9 *Meisner v. Bourgaux Estate* (1994), 131 N.S.R. (2d) 244 (N.S. S.C.) (woman cohabiting with man under arrangement whereby woman living in man's house in return for payment of rent and share of household expenses; woman making no contribution to purchase of house; either party could withdraw at any time; woman to pay small amount for life insurance on mortgage; no payment in fact made when man died; even if payment made, amount very small, not constituting deprivation to woman; man leaving property to parents by will; probated will constituting juristic reason for enrichment).

10 *Franklin v. University of Toronto* (2001), 56 O.R. (3d) 698 (Ont. S.C.J.) (class action by retired female university professors based on unequal pay compared to male counterparts; contracts not illegal unless some statute breached; statute might have been breached by certain date; claim allowed to proceed); *Heon v. Heon* (1989), 69 O.R. (2d) 758 (Ont. H.C.); *Scott v. Noble* (1994), 99 B.C.L.R. (2d) 137 (B.C. C.A.) (contract of employment providing sufficient juristic reason for any deprivation suffered by plaintiff; plaintiff agreeing to work for one year on salary and to consider purchasing partnership interest; parties could not agree on value of partnership; defendants not breaching agreement as making partnership offer which plaintiff not accepting); *Wilcox v. DeWolfe* (1994), 21 Alta. L.R. (3d) 160 (Alta. Q.B.).

11 *Hesjedal v. Granville Estate* (1993), 109 D.L.R. (4th) 353 (Sask. Q.B.) (housekeeper accepting wages as satisfactory; juristic reason for enrichment existing).

12 *Rillford Investments Ltd. v. Gravure International Capital Corp.* (1997), [1997] 7 W.W.R. 534 (Man. C.A.) (commission agent expressly agreeing no commission payable by defendant if transaction not closing within one year of introduction of purchaser by defendant; purchaser introduced but negotiations breaking off; transaction resurrected and completed long after expiry date; fee agreement constituting complete answer to plaintiff's claim); *Martens v. Gulfstream Resources Canada Ltd.* (1998), 221 A.R. 252 (Alta. Q.B.); affirmed (1999), 250 A.R. 62 (Alta. C.A.); leave to appeal refused (2000), 261 A.R. 400 (note) (S.C.C.); reconsideration refused (2001), 2001 CarswellAlta 201 (S.C.C.) (agent not satisfying contractual preconditions to payment of commission; express contract between parties precluding claim based on quantum meruit and providing juristic reason for any enrichment); *Bramalea Ltd. v. 620923 Ontario Inc.* (1992), 8 O.R. (3d) 151 (Ont. Gen. Div.) (vendor of real estate selling property and purchaser agreeing to construct building upon it within certain period; parties later signing letter stating purchaser to look for buyer and in meantime not in default of building obligation; ultimately purchaser selling property for large profit because of rising real estate market; vendor not entitled to any part of profit as profit made in accordance with contracts vendor made with purchaser); *Green Key Solutions Inc. v. Wiebe* (2006), 2006 CarswellMan 345 (Man. Q.B.); affirmed on other grounds (2007), 2007 CarswellMan 149 (Man. C.A.) (remedy of *quantum meruit* not available when there is express contract between parties).

13 *Toronto Dominion Bank v. Carotenuto* (1998), [1998] 9 W.W.R. 254 (B.C. C.A.) (in assessing juristic reason for enrichment, legitimate expectation of parties forming fundamental concern).

14 *Wile v. Clearwater Well Drilling Ltd.* (1996), 148 N.S.R. (2d) 306 (N.S. S.C.) (defendant not requesting or acquiescing in drilling of well; no special relationship between parties and no exceptional circumstances existing to justify granting relief in absence of such relationship); *Cusimano v. D.A.D. Construction Inc.* (2011), 2011 CarswellOnt 11056 (Ont. S.C.J.); *Barrie Trim & Mouldings Inc. v. Country Cottage Living Inc.* (2010), 2010 CarswellOnt 2289 (Ont. Div. Ct.) (supplier cannot sue homeowner in unjust enrichment when no contract exists between them; remedy lies against general contractor).

15 *Aber Resources Ltd. v. Winspear Resources Ltd.* (2000), 33 E.T.R. (2d) 1 (B.C. S.C.) (defendant fully funding diamond prospecting program and refusing to allow plaintiff to fund its proportionate share under terms of contract, in effect appropriating part of plaintiff's interest in diamond property by insisting plaintiff comply with contractual provision for notice with which

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defendant also not complying; plaintiff correspondingly deprived of part of interest; enrichment not occurring in accordance with joint venture agreement; contract not allowing either party to take over whole program without proper notice but not providing remedy should this occur; no juristic reason for enrichment).

16 *BMF Trading, A Partnership v. Abraxis Holdings Ltd.* (2002), 219 D.L.R. (4th) 533 (B.C. S.C.); reversed on other grounds (2003), 2003 CarswellBC 2560 (B.C. C.A.).

17 *Union of India v. Bumper Development Corp.* (1995), [1995] 7 W.W.R. 80 (Alta. Q.B.); affirmed (December 4, 1995), Foisy J.A., Harradence J.A., Hetherington J.A. (Alta. C.A.); leave to appeal refused (1996), [1996] 9 W.W.R. xlvii (note) (S.C.C.) (English court ordering return of sculpture without compensation and awarding damages against defendant; final judgment of foreign court recognized by domestic court providing juristic reason for enrichment of plaintiffs).

18 *S. (L.) v. P. (E.)* (1999), 126 B.C.A.C. 28 (B.C. C.A.); leave to appeal refused (1999), 135 B.C.A.C. 160 (note) (S.C.C.) (juristic reason for enrichment existing when both parties contemplating benefit and court condoning it); *Keneber Inc. v. Midland (Town)* (1994), 16 O.R. (3d) 753 (Ont. Gen. Div.) (plaintiff subdivider agreeing with municipality to pay total cost of new road and municipality agreeing to collect pro rata share from neighbouring landowner when neighbour applying for building permit in future; municipality failing to follow proper procedure when neighbour applying and court decision holding neighbour not liable to pay for share of road; court decision dismissing municipality's claim was juristic reason for enrichment; plaintiff's claim against municipality dismissed).

19 *Ryan (In Trust) v. Kaukab* (2011), 2011 CarswellOnt 12853 (Ont. S.C.J.); affirmed (2014), 2014 CarswellOnt 4080 (Ont. Div. Ct.).

20 *Royal Bank v. Harowitz* (1994), 17 O.R. (3d) 671 (Ont. Gen. Div.); affirmed (1997), 33 O.R. (3d) 704 (Ont. C.A.) (customer fraudulently obtaining credit from bank and using funds to repay loan from defendant); *Toronto Dominion Bank v. Bank of Montreal* (1995), 22 O.R. (3d) 362 (Ont. Gen. Div.) (substantial debt that company owing to recipient bank providing juristic reason for bank to retain mistaken payment); *Ierullo v. Rovan* (2000), 3 B.L.R. (3d) 163 (Ont. S.C.J.); affirmed (2001), 2001 CarswellOnt 9827 (Ont. Div. Ct.) (wrongdoer obtaining cheque from landowner with payee's name left blank, ostensibly for equipment purchase; wrongdoer inserting lawyer's name as payee; pre-existing debt to lawyer providing juristic reason; lawyer lacking actual knowledge of breach of trust and not reckless or wilfully blind to events that constituting breach of trust).

21 *Mack v. Canada (Attorney General)* (2002), 60 O.R. (3d) 737 (Ont. C.A.); leave to appeal refused (2003), 2003 CarswellOnt 1455 (S.C.C.) (statute imposing tax on immigrants based on race repealed over 50 years ago; statute valid in its time; statute not rendered retroactively invalid by present day *Charter* or international laws; statute constituting juristic reason for past enrichment of government and deprivation of immigrants); *R. v. 1431633 Ontario Inc.* (2010), 2010 CarswellOnt 161 (Ont. S.C.J.) (forfeiture provision of *Criminal Code* treated differently than formerly valid statutes).

22 *Hamm v. Metz* (2002), 209 D.L.R. (4th) 385 (Sask. C.A.) (transferees under transactions void under legislation governing fraudulent conveyances retaining properties and receiving rents for many years; rents to be accounted for to plaintiffs as unjust enrichment; no juristic reason for transferees to retain benefits as transferees parties to fraudulent property transaction voided by court); *Verlaan v. Lang Estate* (2005), 2005 CarswellSask 708 (Sask. Q.B.) (example given with regard to Saskatchewan's *Homesteads Act*).

23 *Garland v. Consumers' Gas Co.* (2004), 2004 CarswellOnt 1558 (S.C.C.) (unfair to defendant gas company to require it to repay late payment charges approved by regulatory body as part of overall rate structure as company ordered to impose charges to reduce collection costs and repayment of such charges for past 20 years would penalize other customers who had paid on time).

24 *Toronto Dominion Bank v. Bank of Montreal* (1995), 22 O.R. (3d) 362 (Ont. Gen. Div.) (bank claiming unjust enrichment created problem by certifying cheque by mistake and taking inordinate amount of time to correct error; cheque issued to another bank

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which used it to ensure employees paid); *Craiggs v. Owens* (2012), 2012 CarswellBC 27 (B.C. S.C.) (parties were common law spouses and partners in marijuana grow operation; claimant sought to recover interest in house; claimant established benefit and deprivation but denied recovery as equity in house derived from profits of illegal operation which claimant willingly participated in; not relevant that defendant experienced windfall due to decision of Crown not to seize property as proceeds of crime); *Juzumas v. Baron* (2012), 2012 CarswellOnt 16785 (Ont. S.C.J.) (woman provided domestic services to elderly man; also orchestrated scheme to transfer man's property to her son; court held man was unjustly enriched by woman's services but that she was disentitled to equitable remedy due to unconscionable conduct and undue influence).

[25] *Kerr v. Baranow* (2011), 2011 CarswellBC 240 (S.C.C.); *Cloutier v. Francis* (2011), 2011 CarswellOnt 15427 (Ont. S.C.J.) (man argued clear intention was not to share his pension; woman admitted to recalling a single discussion about not sharing pension; couple held themselves out to be married and pooled all resources; declared intention must be considered in light of actions; legitimate expectation was that parties would share pensions in retirement).

[26] *Brundage v. Campbell* (1992), [1993] 2 W.W.R. 186 (B.C. C.A.) (common law wife of 17 years under no obligation to contribute money, work or services to common law husband; common law relationship leading to constructive and resulting trusts over residence and RRSP in favour of common law wife).

[27] *Lavigne v. Templeton* (2000), 151 Man. R. (2d) 69 (Man. Q.B.) (man's physical labour in maintaining yard and household chores balanced by woman's household chores; mutual home maintenance not resulting in unjust enrichment).

[28] *Orobko v. Orobko* (1992), 39 R.F.L. (3d) 203 (Man. C.A.) (court deciding if unjust enrichment occurring, and if so appropriate remedy, which should be in proportion to unjust enrichment).

[29] *Naiker v. Naiker Estate* (1995), 1995 CarswellBC 119 (B.C. S.C.); affirmed (1997), 1997 CarswellBC 2522 (B.C. C.A.); *Kerr v. Baranow* (2011), 2011 CarswellBC 240 (S.C.C.).

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Most Negative Treatment: Distinguished
Most Recent Distinguished: Hope v. Parkdale No. 498 (Rural Municipality) | 2016 SKCA 19, 2016 CarswellSask 78, 476 Sask. R. 10, 666 W.A.C. 10, 263 A.C.W.S. (3d) 229, 396 D.L.R. (4th) 84, 48 M.P.L.R. (5th) 91 | (Sask. C.A., Feb 10, 2016)

2004 SCC 25, 2004 CSC 25
Supreme Court of Canada

Garland v. Consumers' Gas Co.

2004 CarswellOnt 1558, 2004 CarswellOnt 1559, 2004 SCC 25, 2004 CSC 25, [2004] 1 S.C.R. 629, [2004] A.C.S. No. 21, [2004] S.C.J. No. 21, 130 A.C.W.S. (3d) 32, 186 O.A.C. 128, 237 D.L.R. (4th) 385, 319 N.R. 38, 43 B.L.R. (3d) 163, 72 O.R. (3d) 80 (note), 72 O.R. (3d) 80, 9 E.T.R. (3d) 163, J.E. 2004-931, REJB 2004-60672

Gordon Garland, Appellant v. Enbridge Gas Distribution Inc., previously known as Consumers' Gas Company Limited, Respondent and Attorney General of Canada, Attorney General for Saskatchewan, Toronto Hydro-Electric System Limited, Law Foundation of Ontario and Union Gas Limited, Interveners

Iacobucci, Major, Bastarache, Binnie, LeBel, Deschamps, Fish JJ.

Heard: October 9, 2003
Judgment: April 22, 2004*
Docket: 29052

Proceedings: reversing (2001), 19 B.L.R. (3d) 10 (Ont. C.A.); affirming (2000), 185 D.L.R. (4th) 536 (Ont. S.C.J.); and reversing (2000), 2000 CarswellOnt 1673 (Ont. S.C.J.); additional reasons to (2000), 185 D.L.R. (4th) 536 (Ont. S.C.J.)

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Mark M. Orkin, Q.C., for intervener Law Foundation of Ontario
Patricia D.S. Jackson and M. Paul Michell for intervener Union Gas Limited

Subject: Criminal; Public; Restitution

Related Abridgment Classifications

Public law
IV Public utilities
IV.2 Operation of utility
IV.2.e Collection of utility charges
IV.2.e.iii Miscellaneous

Public law
IV Public utilities
IV.3 Actions by and against public utilities
IV.3.d Practice and procedure
IV.3.d.iii Miscellaneous

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Restitution and unjust enrichment
I General principles
I.4 Bars to recovery
I.4.e Miscellaneous

Headnote

Public utilities --- Operation of utility — Collection of utility charges — General
Receipt of late payment penalties by gas company constitutes unjust enrichment giving rise to restitutionary claim — Gas company ordered to repay late payment penalties in excess of interest limit set out in s. 347 of Criminal Code from 1994 forward.

Restitution --- General principles — Bars to recovery — Miscellaneous issues
Receipt of late payment penalties by gas company constitutes unjust enrichment giving rise to restitutionary claim — Gas company ordered to repay late payment penalties in excess of interest limit set out in s. 347 of Criminal Code from 1994 forward.

Public utilities --- Actions by and against public utilities — Practice and procedure — General
Plaintiff in action against gas company for restitution of late payment penalties entitled to his costs throughout.

Services publics --- Exploitation d'un service public — Recouvrement des redevances aux services publics — En général
Perception par la compagnie de gaz de pénalités pour paiement en retard constituait un enrichissement sans cause et donnait ouverture à une réclamation de restitution — Compagnie de gaz s'est vu ordonner de rembourser les pénalités pour paiement en retard excédant le taux d'intérêt maximal énoncé à l'art. 347 du Code criminel, et ce, à partir de l'année 1994.

Restitution --- Principes généraux — Motifs empêchant le recouvrement — Questions diverses
Perception par la compagnie de gaz de pénalités pour paiement en retard constituait un enrichissement sans cause et donnait ouverture à une réclamation de restitution — Compagnie du gaz s'est vu ordonner de rembourser les pénalités pour paiement en retard excédant le taux d'intérêt maximal énoncé à l'art. 347 du Code criminel, et ce, à partir de l'année 1994.

Services publics --- Actions intentées par ou contre les services publics — Procédure — En général
Demandeur dans le cadre de l'action qu'il avait intentée contre la compagnie de gaz afin d'obtenir la restitution des pénalités pour paiement en retard avait droit aux dépens devant toutes les cours.

The plaintiff brought a class action on behalf of more than 500,000 customers of a gas company. He claimed that the late payment penalties charged by the gas company on overdue payments violated s. 347 of the Criminal Code. The case reached the Supreme Court of Canada, which held that the penalties constituted the charging of a criminal rate of interest contrary to s. 347 of the Code. The plaintiff brought a second action claiming restitution for unjust enrichment of charges received by the gas company in violation of s. 347. The gas company moved for summary judgment dismissing this action. The motions judge granted the gas company's motion, finding that the action was a collateral attack on the order of the Ontario Energy Board, which had approved the creation of the late payment penalties. The plaintiff appealed. The appeal was dismissed. A majority of the Ontario Court of Appeal disagreed with the motions judge's reasons but held that the plaintiff's unjust enrichment claim could not be made out. The plaintiff appealed.

Held: The appeal was allowed.

The receipt of late payment penalties by the gas company constituted unjust enrichment giving rise to a restitutionary claim. The gas company was ordered to repay those penalties, collected from 1994 forward, that were in excess of the interest limit set out in s. 347 of the Criminal Code.

When money is transferred from plaintiff to defendant, there is an enrichment. Without doubt, the gas company received the money from the late payment penalties and the money was available to it to carry on its business. The availability of that money constituted a benefit to the gas company and there was no juristic reason for the enrichment.

The proper approach to the juristic reason analysis has two parts. First, the plaintiff must show that there is no juristic reason

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from an established category, such as a contract or a disposition of law, to deny recovery. If there is no juristic reason, then the plaintiff has made out a prima facie case. The prima facie case can be rebutted if the defendant demonstrates another reason to deny recovery. A de facto burden of proof is placed on the defendant to show why the enrichment should be retained.

In this case, the only possible juristic reason from an established category (disposition of law) that could be used to justify the enrichment was the existence of Ontario Energy Board orders creating the late payment penalties. The orders were not a juristic reason for the enrichment, however, because they were rendered inoperative to the extent of their conflict with s. 347 of the Criminal Code. The plaintiff had made out a prima facie case for unjust enrichment and it fell to the gas company to show a juristic reason for the enrichment outside the established categories.

From 1981 to 1994 the gas company's reliance on the inoperative orders of the Ontario Energy Board provided a juristic reason for the enrichment. Section 347 of the Criminal Code was enacted in 1981 and the action was commenced in 1994. Between 1981 and 1994 no suggestion could be made that the gas company knew that the late payment penalties violated s. 347 of the Code. The gas company's reliance on the board's orders in the absence of actual or constructive notice that the orders were inoperative was sufficient to provide a juristic reason for the enrichment during this period. When the plaintiff commenced the first action in 1994, however, the gas company was put on notice that it might be violating the Code. This possibility became a reality in 1998, when the Supreme Court of Canada held, in the first action, that the late payment penalties were in excess of the s. 347 limits. After the gas company was put on notice of a serious possibility of a Criminal Code violation, the gas company could no longer reasonably rely on the board's orders to authorize the penalties. After the commencement of the action in 1994, there was no longer a juristic reason for the enrichment of the gas company. After 1994 the plaintiff was entitled to restitution of the portion of the penalties paid that exceeded the 60 per cent rate of interest set out in s. 347 of the Criminal Code.

The gas company could not rely on the defence of change of position. The penalties were obtained in contravention of the Criminal Code and, as a result, it could not be unjust for the gas company to have to return them.

Neither could the gas company rely on the defence set out in s. 25 of the Ontario Energy Board Act. This defence must be read down to exclude protection from civil liability that arises out of Criminal Code violations.

The doctrines of exclusive jurisdiction and collateral attack were likewise not defences on which the gas company could rely. The Ontario Energy Board did not have exclusive jurisdiction over this dispute. Although the dispute involved rate orders, at its heart it was a private law matter within the competence of the civil courts and the board had jurisdiction to order the remedy sought by the plaintiff. Furthermore, the action did not constitute an impermissible collateral attack on the board's orders. The object of the plaintiff's action was not to invalidate or render inoperable the board's orders but rather to recover money that had been illegally collected by the gas company as a result of the board orders. The plaintiff was not the object of the orders, and he was not seeking to avoid the orders by bringing the action.

The regulated industries defence was unavailable to the gas company. The language in s. 347 of the Criminal Code does not support the notion that a valid provincial regulatory scheme cannot be contrary to the public interest or an offence against the state.

Because the gas company was not a government official acting under colour of authority, it could not rely on the de facto doctrine to exempt it from liability. The underlying purpose of the de facto doctrine is to preserve law and order and the authority of the government. Those interests were not at stake in this litigation.

A preservation order was not appropriate. The gas company had ceased to collect the late payment penalties at a criminal rate and, if a preservation order was made, there were no future late payment penalties to which it could attach. For those late payment penalties paid between 1994 and 2004, a preservation order would serve no practical purpose. The plaintiff did not allege that the gas company was impecunious or that there was any reason to believe that it would not satisfy a judgment against it. Furthermore, the plaintiff did not satisfy the criteria set out in R. 45.02 of the Rules of Civil Procedure.

The plaintiff was entitled to his costs of all the proceedings throughout, regardless of the outcome of any future litigation.

Le demandeur a exercé un recours collectif au nom de plus de 500 000 clients d'une compagnie de gaz. Il a soutenu que les pénalités pour paiement en retard imposées par la compagnie à l'égard des paiements dus contrevenaient à l'art. 347 du Code

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criminel. L'affaire s'est rendue jusqu'en Cour suprême du Canada, qui a statué que les pénalités pour paiement en retard constituaient un taux d'intérêt criminel contrevenant à l'art. 347 du Code. Le demandeur a intenté une deuxième action, cette fois en restitution pour enrichissement sans cause des pénalités pour paiement en retard perçues par la compagnie en contravention de l'art. 347. La compagnie a présenté une requête en jugement sommaire afin d'obtenir le rejet de la deuxième action. Le juge saisi de la requête de la compagnie l'a accueillie au motif qu'il s'agissait d'une contestation indirecte de l'ordonnance de la Commission de l'énergie de l'Ontario approuvant la création des pénalités pour paiement en retard. Le demandeur a interjeté appel. Le pourvoi a été rejeté. Les juges majoritaires de la Cour d'appel étaient en désaccord avec les motifs du premier juge, mais ils ont quand même estimé que l'enrichissement sans cause n'avait pas été établi. Le demandeur a interjeté appel.

Arrêt: Le pourvoi a été accueilli.

La perception par la compagnie des pénalités pour paiement en retard constituait un enrichissement sans cause donnant ouverture à une demande de restitution. La compagnie s'est vu ordonner de rembourser les pénalités payées à partir de 1994, lesquelles excédaient le taux d'intérêt maximal prévu par l'art. 347 du Code criminel.

Le transfert d'un montant d'argent du demandeur au défendeur constitue un enrichissement. Il n'y avait aucun doute que la compagnie avait perçu l'argent provenant des pénalités et qu'elle aurait pu l'utiliser dans l'exploitation de son entreprise. La disponibilité de l'argent constituait un avantage pour la compagnie et il n'existait aucun motif juridique pouvant justifier un tel enrichissement.

Il convient de scinder en deux l'étape de l'analyse du motif juridique. Premièrement, le demandeur doit démontrer qu'il n'existe aucun motif juridique appartenant à une catégorie établie permettant de refuser le recouvrement. S'il n'existe aucun motif juridique appartenant à une catégorie établie, alors le demandeur a prouvé sa cause de façon prima facie. Le défendeur peut réfuter la preuve prima facie en démontrant qu'il existe une autre raison justifiant de refuser le recouvrement. Le défendeur a l'obligation de facto de démontrer pourquoi il devrait conserver ce dont il s'est enrichi.

En l'espèce, le motif juridique appartenant à une catégorie établie (disposition légale) qui pouvait servir à justifier l'enrichissement était l'existence des ordonnances de la Commission de l'énergie de l'Ontario ayant créé les pénalités pour paiement en retard. Ces ordonnances ne constituaient cependant pas un motif juridique justifiant l'enrichissement puisqu'elles étaient inopérantes dans la mesure où elles entraient en conflit avec l'art. 347 du Code criminel. Le demandeur avait prouvé l'enrichissement sans cause de façon prima facie et c'était alors à la compagnie qu'il revenait de démontrer l'existence d'un motif juridique n'appartenant pas aux catégories qui puisse justifier l'enrichissement.

Le fait que, à partir de 1981 jusqu'en 1994, la compagnie se soit fondée sur les ordonnances inopérantes de la CEO était un motif juridique justifiant l'enrichissement. L'article 347 du Code criminel a été adopté en 1981 et cette action a été intentée en 1994. Rien ne prouvait que la compagnie savait, entre 1981 et 1994, que les pénalités contrevenaient à l'art. 347 du Code. Le fait que la compagnie se soit fondée sur les ordonnances de la Commission, sans savoir véritablement ou vraisemblablement qu'elles étaient inopérantes, suffisait pour fournir un motif juridique justifiant l'enrichissement pendant cette période. La compagnie a par ailleurs été avisée de la possibilité qu'elle puisse contrevenir au Code lorsque le demandeur a intenté son action en 1994. Cette possibilité est devenue réalité lorsque la Cour suprême du Canada a statué, dans le cadre de la première action, que les pénalités excédaient les limites de l'art. 347. Dès que la compagnie a été avisée qu'il existait une réelle possibilité que les pénalités puissent violer le Code, elle ne pouvait alors plus raisonnablement se fonder sur les ordonnances de la Commission pour autoriser les pénalités. Elle n'avait donc plus de motif juridique justifiant l'enrichissement dès après l'institution de l'action en 1994. Le demandeur avait donc droit, à partir de 1994, à la restitution de la portion des pénalités payées qui excédaient le taux d'intérêt de 60 pour cent prévu par l'art. 347 du Code criminel.

La compagnie ne pouvait invoquer le moyen de défense fondé sur le changement de situation. Les pénalités ont été obtenues en contravention du Code criminel et, par conséquent, il ne pouvait être injuste pour la compagnie d'avoir à les rembourser.

La compagnie ne pouvait non plus invoquer le moyen de défense prévu par l'art. 25 de la Loi sur la Commission de l'énergie de l'Ontario. Ce moyen de défense doit recevoir une interprétation stricte afin de pouvoir exclure la protection contre la responsabilité civile pouvant découler de contraventions au Code criminel.

La compagnie ne pouvait pas non plus invoquer les théories de la compétence exclusive et de la contestation indirecte. La Commission de l'énergie de l'Ontario n'avait pas compétence exclusive à l'égard du litige. Même si ce dernier impliquait des

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ordonnances en matière de taux, il portait principalement sur une question de droit privée relevant de la compétence des tribunaux civils, et la Commission n'avait pas compétence pour ordonner la réparation demandée par le demandeur. De plus, l'action ne constituait pas une contestation indirecte inacceptable des ordonnances de la Commission. L'action du demandeur ne visait pas à obtenir que les ordonnances de la Commission soient invalidées ou déclarées inopérantes, mais plutôt à obtenir le recouvrement de l'argent illégalement perçu par la compagnie en raison des ordonnances de la Commission. Le demandeur n'était pas régi par les ordonnances et il n'y avait aucune crainte qu'il ait cherché à éviter les ordonnances en intentant l'action.

Le moyen de défense fondé sur la réglementation de l'industrie ne pouvait non plus être invoqué par la compagnie. Rien dans l'art. 347 du Code criminel ne pouvait appuyer la théorie qu'un régime de réglementation provincial ne pouvait être contraire à l'intérêt public ni constituer une infraction contre l'État.

La compagnie n'était pas un fonctionnaire qui agissait avec une apparence d'autorité et ne pouvait donc se fonder sur le principe de la validité de facto pouvant l'exonérer de toute responsabilité. L'objectif sous-jacent du principe de la validité de facto était d'assurer le respect de la loi et l'ordre ainsi que de l'autorité du gouvernement. De tels intérêts n'étaient pas en jeu dans ce litige.

Il n'était pas approprié d'accorder une ordonnance de conservation. La compagnie avait cessé de percevoir les pénalités pour paiement en retard qui étaient à un taux criminel; une telle ordonnance ne pouvait se rattacher à aucune pénalité à venir. Quant aux pénalités payées de 1994 à 2004, une ordonnance de conservation ne serait d'aucune utilité pratique. Le demandeur n'a pas allégué que la compagnie était démunie ou qu'il existait des raisons de croire qu'elle n'exécuterait pas un jugement rendu contre elle. De plus, le demandeur n'a pas satisfait au critère énoncé dans la règle 45.02 des Règles de procédure civile.

Le demandeur avait droit aux dépens devant toutes les cours, quelle que soit l'issue de tout autre litige ultérieur.

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APPEAL by plaintiff from judgment reported at 2001 CarswellOnt 4244, 19 B.L.R. (3d) 10, 152 O.A.C. 244, 57 O.R. (3d) 127, 208 D.L.R. (4th) 494 (Ont. C.A.), dismissing plaintiff's appeal from judgment granting gas company's motion to dismiss action against it.

POURVOI du demandeur à l'encontre de l'arrêt publié à 2001 CarswellOnt 4244, 19 B.L.R. (3d) 10, 152 O.A.C. 244, 57 O.R. (3d) 127, 208 D.L.R. (4th) 494 (Ont. C.A.), qui a rejeté son pourvoi à l'encontre du jugement ayant accueilli la requête

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de la compagnie de gaz en rejet de l'action intentée contre elle.

***Iacobucci J.*:**

1 At issue in this appeal is a claim by customers of a regulated utility for restitution for unjust enrichment arising from late payment penalties levied by the utility in excess of the interest limit prescribed by s. 347 of the *Criminal Code*, R.S.C. 1985, c. C-46. More specifically, the issues raised include the necessary ingredients to a claim for unjust enrichment, the defences that can be mounted to resist the claim, and whether other ancillary orders are necessary.

2 For the reasons that follow, I am of the view to uphold the appellant's claim for unjust enrichment and therefore would allow the appeal.

I. Facts

3 The respondent Consumers' Gas Company Limited, now known as Enbridge Gas Distribution Inc., is a regulated utility which provides natural gas to commercial and residential customers throughout Ontario. Its rates and payment policies are governed by the Ontario Energy Board ("OEB" or "Board") pursuant to the *Ontario Energy Board Act*, R.S.O. 1990, c. O.13 ("OEBA"), and the *Municipal Franchises Act*, R.S.O. 1990, c. M.55. The respondent cannot sell gas or charge for gas-related services except in accordance with rate orders issued by the Board.

4 Consumers' Gas bills its customers on a monthly basis, and each bill includes a due date for the payment of current charges. Customers who do not pay by the due date incur a late payment penalty ("LPP") calculated at 5 per cent of the unpaid charges for that month. The LPP is a one-time penalty and does not compound or increase over time.

5 The LPP was implemented in 1975 following a series of rate hearings conducted by the OEB. In granting Consumers' Gas's application to impose the penalty, the Board noted that the primary purpose of the LPP is to encourage customers to pay their bills promptly, thereby reducing the cost to Consumers' Gas of carrying accounts receivable. The Board also held that such costs, along with any special collection costs arising from late payments, should be borne by the customers who cause them to be incurred, rather than by the customer base as a whole. In approving a flat penalty of 5 per cent, the OEB rejected the alternative course of imposing a daily interest charge on overdue accounts. The Board reasoned that an interest charge would not provide sufficient incentive to pay by a named date, would give little weight to collection costs, and might seem overly complicated. The Board recognized that if a bill is paid very soon after the due date, the penalty would, if calculated as an interest charge, be a very high rate of interest. However, it noted that customers could avoid such a charge by paying their bills on time, and that, in any event, in the case of the average bill the dollar amount of the penalty would not be very large.

6 The appellant Gordon Garland is a resident of Ontario and has been a Consumers' Gas customer since 1983. He and his wife paid approximately $75 in LPP charges between 1983 and 1995. In a class action on behalf of over 500,000 Consumers' Gas customers, Garland asserted that the LPPs violate s. 347 of the *Criminal Code*. That case also reached the Supreme Court of Canada, which held that charging the LPPs amounted to charging a criminal rate of interest under s. 347 and remitted the matter back to the trial court for further consideration (*Garland v. Consumers' Gas Co.*, [1998] 3 S.C.R. 112 (S.C.C.) ("*Garland #1*")). Both parties have now brought cross-motions for summary judgment.

7 The appellant now seeks restitution for unjust enrichment of LPP charges received by the respondent in violation of s. 347 of the Code. He also seeks a preservation order requiring Consumers' Gas to hold LPPs paid during the pendency of the litigation subject to possible repayment.

8 The motions judge granted the respondent's motion for summary judgment, finding that the action was a collateral attack on the OEB order. He dismissed the application for a preservation order. A majority of the Court of Appeal disagreed with the motions judge's reasons, but dismissed the appeal on the grounds that the appellant's unjust enrichment claim could not be made out.

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II. Relevant Statutory Provisions

9 *Ontario Energy Board Act*, R.S.O. 1990, c. O.13

18. An order of the Board is a good and sufficient defence to any proceeding brought or taken against any person in so far as the act or omission that is the subject of the proceeding is in accordance with the order.

Ontario Energy Board Act, 1998, S.O. 1998, c. 15, Sched. B

25. An order of the Board is a good and sufficient defence to any proceeding brought or taken against any person in so far as the act or omission that is the subject of the proceeding is in accordance with the order.

Criminal Code, R.S.C. 1985, c. C-46

15. No person shall be convicted of an offence in respect of an act or omission in obedience to the laws for the time being made and enforced by persons in *de facto* possession of the sovereign power in and over the place where the act or omission occurs.

. . . . .

347.(1) Notwithstanding any Act of Parliament, every one who

(a) enters into an agreement or arrangement to receive interest at a criminal rate, or

(b) receives a payment or partial payment of interest at a criminal rate,

is guilty of

(c) an indictable offence and is liable to imprisonment for a term not exceeding five years, or

(d) an offence punishable on summary conviction and is liable to a fine not exceeding twenty-five thousand dollars or to imprisonment for a term not exceeding six months or to both.

III. Judicial History

A. Ontario Superior Court (2000), 185 D.L.R. (4th) 536

10 As this case raised no factual disputes, all parties agreed that summary judgment was the proper procedure on the motion. Winkler J. found that the appellant's claim could not succeed in law and that there was no serious issue to be tried. In so finding, he held that the "regulated industries defence" was not a complete defence to the claim. On his reading of the relevant case law, the dominant consideration was whether the express statutory language affords a degree of flexibility to provincial regulators. Section 347 affords no such flexibility, so the defence is not available.

11 Nor, in Winkler J.'s view, did s. 15 of the *Criminal Code* act as a defence. Section 15 was a provision of very limited application, originally enacted to ensure that persons serving the Monarch *de facto* could not be tried for treason for remaining faithful to the unsuccessful claimant to the throne. While it could have a more contemporary application, it was limited on its face to actions or omissions occurring pursuant to the authority of a sovereign power. As the OEB was not a sovereign power, it did not apply.

12 Winkler J. found that the proposed action was a collateral attack on the OEB's orders. The OEBA indicated repeatedly that the OEB has exclusive control over matters within its jurisdiction. In addition, interested parties were welcome to participate in OEB hearings, and OEB orders were reviewable. The appellant did not avail himself of any of these opportunities, choosing instead to challenge the validity of the OEB orders in the courts. Winkler J. found that, unless

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attacked directly, OEB orders are valid and binding upon the respondent and its consumers. The OEB was not a party to the instant proceeding and its orders were not before the court. Winkler J. noted that the setting of rates is a balancing exercise, with LPPs being one factor under consideration. Applying *Sprint Canada Inc. v. Bell Canada* (1997), 79 C.P.R. (3d) 31 (Ont. Gen. Div.), *Ontario Hydro v. Kelly* (1998), 39 O.R. (3d) 107 (Ont. Gen. Div.), and *Mahar v. Rogers Cablesystems Ltd.* (1995), 25 O.R. (3d) 690 (Ont. Gen. Div.), Winkler J. found that the instant action, although framed as a private dispute between two contractual parties, was in reality an impermissible collateral attack on the validity of OEB orders. It would be inappropriate for the court to determine matters that fall squarely within the OEB's jurisdiction. Moreover, this Court's decision in *Garland #1* with respect to s. 347 provided the OEB with ample legal guidance to deal with the matter.

13 In case he was incorrect in that finding, Winkler J. went on to find that s. 18 of the OEBA provided a complete defence to the proposed action. He held that s. 18 was constitutionally valid because it did not interfere with Parliament's jurisdiction over interest and the criminal law or, to the extent that it did, the interference was incidental. Although the respondent did not strictly comply with the OEB order in that it waived LPPs for some customers, this did not preclude the respondent from relying on s. 18.

14 In case that finding was also mistaken, Winkler J. went on to consider whether the appellant's claim for restitution was valid. The parties had conceded that the appellant had suffered a deprivation, and Winkler J. was satisfied that the respondent had received a benefit. However, he found that the OEB's rate order constituted a valid juristic reason for the respondent's enrichment.

15 Having reached those conclusions, Winkler J. declined to make a preservation order, as requested by the appellant, allowed the respondent's motion for summary judgment and dismissed the appellant's action. By endorsement, he ordered costs against the appellant.

B. Ontario Court of Appeal (2001), 208 D.L.R. (4th) 494

16 McMurtry C.J.O., for the majority, found that Winkler J. was incorrect in finding that there had been an impermissible collateral attack on a decision of the OEB because the appellant was not challenging the merits or legality of the OEB order or attempting to raise a matter already dealt with by the OEB. Rather, the proposed class action was based on the principles of unjust enrichment and raised issues over which the OEB had no jurisdiction. As such, the courts had jurisdiction over the proposed class action.

17 McMurtry C.J.O. further found that s. 25 of the 1998 OEBA (the equivalent provision to s. 18 of the 1990 OEBA) did not provide grounds to dismiss the appellant's action. He did not agree that the respondent's failure to comply strictly with the OEB orders made s. 25 inapplicable. Instead, he found that, while s. 25 provides a defence to any proceedings insofar as the act or omission at issue is in accordance with the OEB order, legislative provisions restricting citizen's rights of action attract strict construction (*Berardinelli v. Ontario Housing Corp.* (1978), [1979] 1 S.C.R. 275 (S.C.C.)). The legislature could not reasonably be believed to have contemplated that an OEB order could mandate criminal conduct, and even wording as broad as that found in s. 25 could not provide a defence to an action for restitution arising from an OEB order authorizing criminal conduct. He noted that this decision was based on the principles of statutory interpretation, not on the federal paramountcy doctrine.

18 Section 15 of the *Criminal Code* did not provide the respondent with a defence either. It was of limited application and is largely irrelevant in modern times. As for the "regulated industries defence," it did not apply because the case law did not indicate that a company operating in a regulatory industry could act directly contrary to the *Criminal Code*.

19 Nonetheless, McMurty C.J.O. held that the appellant's unjust enrichment claim could not be made out. It had been conceded that the appellant suffered a deprivation, but McMurtry C.J.O. held that the appellant failed to establish the other two elements of the claim for unjust enrichment. While payment of money will normally be a benefit, McMurtry C.J.O. found that the payment of the late penalties in this case did not confer a benefit on the respondent. Taking the "straightforward economic approach" to the first two elements of unjust enrichment, as recommended in *Peter v. Beblow*, [1993] 1 S.C.R. 980 (S.C.C.), McMurtry C.J.O. noted that the OEB sets rates with a view to meeting the respondent's overall revenue requirements. If the revenue available from LPPs had been set lower, the other rates would have been set higher. Therefore, the receipt of the LPPs was not an enrichment capable of giving rise to a restitutionary claim.

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20 In case that conclusion was wrong, McMurtry C.J.O. went on to find that there was a juristic reason for any presumed enrichment. Under this aspect of the test, moral and policy questions were open for consideration, and it was necessary to consider what was fair to both the plaintiff and the defendant. It was therefore necessary to consider the statutory regime within which the respondent operated. McMurtry C.J.O. noted that the respondent was required by statute to apply the LPPs; it had been ordered to collect them and they were taken into account when the OEB made its rate orders. He found that it would be contrary to the equities in this case to require the respondent to repay all the LPP charges collected since 1981. Such an order would affect all of the respondent's customers, including the vast majority who consistently pay on time.

21 The appellant argued that a preservation order was required even if his arguments on restitution were not successful because he could still be successful in arguing that the respondent could not enforce payment of the late penalties. As he had found no basis for ordering restitution, McMurtry C.J.O. saw no reason to make a preservation order. Moreover, the order requested would serve no practical purpose because it gave the respondent the right to spend the monies at stake. He dismissed the appeal and the appellant's action. In so doing, he agreed with the motions judge that the appellant's claims for declaratory and injunctive relief should not be granted.

22 As to costs, McMurtry C.J.O. found that there were several considerations that warranted overturning the order that the appellant pay the respondent's costs. First, the order required him to pay the costs of his successful appeal to the Supreme Court of Canada. Second, even though the respondent was ultimately successful, it failed on two of the defences it raised at the motions stage and three of the defences it raised at the Court of Appeal. Third, the proceedings raised novel issues. McMurtry C.J.O. found that each party should bear its own costs.

23 Borins J.A., writing in dissent, was of the opinion that the appeal should be allowed. He agreed with most of McMurtry C.J.O.'s reasons, but found that the plaintiff class was entitled to restitution. In his opinion, the motions judge's finding that the LPPs had enriched the respondent by causing it to have more money than it had before was supported by the evidence and the authorities. Absent material error, he held, it was not properly reviewable.

24 However, Borins J.A. found that the motions judge had erred in law in finding that there was a juristic reason for the enrichment. The motions judge had failed to consider the effect of the Supreme Court of Canada decision that the charges amount to interests at a criminal rate and that s. 347 of the *Criminal Code* prohibits the receipt of such interest. As a result of this decision, Borins J.A. felt that the rate orders ceased to have any legal effect and could not provide a juristic reason for the enrichment. A finding that the rate orders constituted a juristic reason for contravening s. 347 also allowed orders of a provincial regulatory authority to override federal criminal law and removed a substantial reason for compliance with s. 347. Thus, he held that allowing the respondent to retain the LPPs was contrary to the federal paramountcy doctrine.

25 According to Borins J.A., finding the OEB orders to constitute a juristic reason would also be contrary to the authorities which have applied s. 347 in the context of commercial obligations. This line of cases required consideration of when restitution should have been ordered and for what portion of the amount paid. Finally, it would allow the respondent to profit from its own wrongdoing.

26 Borins J.A. was not sympathetic to the respondent's claims that its change of position should allow it to keep the money it had collected in contravention of s. 347, even if it could have recovered the same amount of money on an altered rate structure. He also noted that, in his opinion, the issue of recoverability should have been considered in the context of the class action, not on the basis of the representative plaintiff's claim for $75. Borins J.A. would have allowed the appeal, set aside the judgment dismissing the appellant's claim, granted partial summary judgment, and dismissed the respondent's motion for summary judgment. The appellant would have been required to proceed to trial with respect to damages. He would also have declared that the charging and receipt of LPPs by the respondent violates s. 347(1)(b) of the *Criminal Code* and that the LPPs need not be paid by the appellant, and would have ordered that the respondent repay the LPPs received from the appellant, as determined by the trial judge. He would also have ordered costs against the respondent.

27 It should be noted that on January 9, 2003, the Chief Justice stated the following constitutional question:

> Are s. 18 of the *Ontario Energy Board Act*, R.S.O. 1990, c. O-13, and s. 25 of the *Ontario Energy Board Act, 1998*, S.O. 1998, c. 15, Sched. B, constitutionally inoperative by reason of the paramountcy of s. 347 of the *Criminal Code*, R.S.C. 1985, c. C-46?

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As will be clear from the reasons below, I have found it unnecessary to answer the constitutional question.

IV. Issues

28

1. Does the appellant have a claim for restitution?

    (a) Was the respondent enriched?

    (b) Is there a juristic reason for the enrichment?

2. Can the respondent avail itself of any defence?

    (a) Does the change of position defence apply?

    (b) Does s. 18 (now s. 25) of the OEBA ("s. 18/25") shield the respondent from liability?

    (c) Is the appellant engaging in a collateral attack on the orders of the Board?

    (d) Does the "regulated industries" defence exonerate the respondent?

    (e) Does the *de facto* doctrine exonerate the respondent?

3. Other orders sought by the appellant

    (a) Should this Court make a preservation order?

    (b) Should this Court make a declaration that the LLPs need not be paid?

    (c) What order should this Court make as to costs?

V. Analysis

29 My analysis will proceed as follows. First, I will assess the appellant's claim in unjust enrichment. Second, I will determine whether the respondent can avail itself of any defences to the appellant's claim. Finally, I will address the other orders sought by the appellant.

A. Unjust Enrichment

30 As a general matter, the test for unjust enrichment is well established in Canada. The cause of action has three elements: (1) an enrichment of the defendant, (2) a corresponding deprivation of the plaintiff, and (3) an absence of juristic reason for the enrichment (*Becker v. Pettkus*, [1980] 2 S.C.R. 834 (S.C.C.), at p. 848; *Peel (Regional Municipality) v. Canada*, [1992] 3 S.C.R. 762 (S.C.C.), at p. 784). In this case, the parties are agreed that the second prong of the test has been satisfied. I will thus address the first and third prongs of the test in turn.

(a) Enrichment of the Defendant

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31 In *Peel*, *supra*, at p. 790, McLachlin J. (as she then was) noted that the word "enrichment" connotes a tangible benefit which has been conferred on the defendant. This benefit, she writes, can be either a positive benefit, such as the payment of money, or a negative benefit, for example, sparing the defendant an expense which he or she would otherwise have incurred. In general, moral and policy arguments have not been considered under this head of the test. Rather, as McLachlin J. wrote in *Peter*, *supra*, at p. 990, "[t]his Court has consistently taken a straightforward economic approach to the first two elements of the test for unjust enrichment." Other considerations, she held, belong more appropriately under the third element - absence of juristic reason.

32 In this case, the transactions at issue are payments of money by late payers to the respondent. It seems to me that, as such, under the "straightforward economic approach" to the benefit analysis, this element is satisfied. Winkler J. followed this approach and was satisfied that the respondent had received a benefit. "Simply stated," he wrote at para. 95, "as a result of each LPP received by Consumers' Gas, the company has more money than it had previously and accordingly is enriched."

33 The majority of the Court of Appeal for Ontario disagreed. McMurtry C.J.O. found that while payment of money would normally be a benefit, it was not in this case. He claimed to be applying the "straightforward economic approach" as recommended in *Peter*, *supra*, but accepted the respondent's argument that because of the rate structure of the OEB, the respondent had not actually been enriched. Because LPPs were part of a scheme designed to recover the respondent's overall revenue, any increase in LPPs was offset by a corresponding decrease in regular rates. Thus, McMurty C.J.O. concluded, "[t]he enrichment that follows from the receipt of LPPs is passed on to all [Consumers' Gas] customers in the form of lower gas delivery rates" (para. 65). As a result, the real beneficiary of the scheme is not the respondent but is rather all of the respondent's customers.

34 In his dissent, Borins J.A. disagreed with this analysis. He would have held that, where there is payment of money, there is little controversy over whether or not a benefit was received and since a payment of money was received in this case, a benefit was conferred on the respondent.

35 The respondent submits that it is not enough that the plaintiff has made a payment; rather, it must also be shown that the defendant is "in possession of a benefit." It argues that McMurtry C.J.O. had correctly held that the benefit had effectively been passed on to the respondent's customers, so the respondent could not be said to have retained the benefit. The appellant, on the other hand, maintains that the "straightforward economic analysis" from *Peter*, *supra*, should be applied and any other moral or policy considerations should be considered at the juristic reason stage of the analysis.

36 I agree with the analysis of Borins J.A. on this point. The law on this question is relatively clear. Where money is transferred from plaintiff to defendant, there is an enrichment. Transfer of money so clearly confers a benefit that it is the main example used in the case law and by commentators of a transaction that meets the threshold for a benefit (see *Peel*, *supra*, at p. 790; *Sharwood & Co. v. Municipal Financial Corp.* (2001), 53 O.R. (3d) 470 (Ont. C.A.), at p. 478; Peter D. Maddaugh and John D. McCamus, *The Law of Restitution* (Aurora, Ont.: Butterworths, 1990), at p. 38; Lord Goff and Gareth Jones, *The Law of Restitution*, 6th ed. (London: Sweet & Maxwell, 2002), at p. 18). There simply is no doubt that Consumers' Gas received the monies represented by the LPPs and had that money available for use in the carrying on of its business. The availability of those funds constitutes a benefit to Consumers' Gas. We are not, at this stage, concerned with what happened to this benefit in the ongoing operation of the regulatory scheme.

37 While the respondent rightly points out that the language of "received and retained" has been used with respect to the benefit requirement (see, for example, *Peel*, *supra*, at p. 788), it does not make sense that it is a requirement that the benefit be retained permanently. The case law does, in fact, recognize that it might be unfair to award restitution in cases where the benefit was not retained, but it does so after the three steps for a claim in unjust enrichment have been made out by recognizing a "change of position" defence (see, for example, *Storthoaks (Rural Municipality) v. Mobil Oil Canada Ltd.* (1975), [1976] 2 S.C.R. 147 (S.C.C.); *RBC Dominion Securities Inc. v. Dawson* (1994), 111 D.L.R. (4th) 230 (Nfld. C.A.)). Professor Jacob S. Ziegel, in his comment on the Ontario Court of Appeal decision in this case, "Criminal Usury, Class Actions and Unjust Enrichment in Canada" (2002), 18 *Journal of Contract Law* 121, at p. 126, suggests that McMurtry C.J.O.'s reliance on the regulatory framework of the LPP in finding that a benefit was not conferred "was really a change of position defence." I agree with this assessment. Whether recovery should be barred because the benefit was passed on to the respondent's other customers ought to be considered under the change of position defence.

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(b) Absence of Juristic Reason

(i) General Principles

38 In his original formulation of the test for unjust enrichment in *Rathwell v. Rathwell*, [1978] 2 S.C.R. 436 (S.C.C.), at p. 455 (adopted in *Pettkus*, *supra*, at p. 844), Dickson J. (as he then was) held in his minority reasons that for an action in unjust enrichment to succeed:

> . . . the facts must display an enrichment, a corresponding deprivation, and the absence of any juristic reason - such as a contract or disposition of law - for the enrichment.

39 Later formulations of the test by this Court have broadened the types of factors that can be considered in the context of the juristic reason analysis. In *Peter*, *supra*, at p. 990, McLachlin J. held that:

> It is at this stage that the court must consider whether the enrichment and detriment, morally neutral in themselves, are "unjust".
>
> . . . The test is flexible, and the factors to be considered may vary with the situation before the court.

40 The "juristic reason" aspect of the test for unjust enrichment has been the subject of much academic commentary and criticism. Much of the discussion arises out of the difference between the ways in which the cause of action of unjust enrichment is conceptualized in Canada and in England. While both Canadian and English causes of action require an enrichment of the defendant and a corresponding deprivation of the plaintiff, the Canadian cause of action requires that there be "an absence of juristic reason for the enrichment" while English courts require "that the enrichment be unjust" (see discussion in L.D. Smith, "The Mystery of 'Juristic Reason' " (2000), 12 S.C.L.R. (2d) 211, at pp. 212-213). It is not of great use to speculate on why Dickson J. in *Rathwell*, *supra*, expressed the third condition as absence of juristic reason but I believe that he may have wanted to ensure that the test for unjust enrichment was not purely subjective in order to be responsive to Martland J.'s criticism in his reasons that application of the doctrine of unjust enrichment contemplated by Dickson J. would require "immeasurable judicial discretion" (p. 473). The importance of avoiding a purely subjective standard was also stressed by McLachlin J. in her reasons in *Peel*, *supra*, at p. 802, in which she wrote that the application of the test for unjust enrichment should not be "case by case 'palm tree' justice."

41 Perhaps as a result of these two formulations of this aspect of the test, Canadian courts and commentators are divided in their approach to juristic reason. As Borins J.A. notes in his dissent (at para. 105), while "some judges have taken the *Pettkus* formulation literally and have attempted to decide cases by finding a 'juristic reason' for a defendant's enrichment, others have decided cases by asking whether the plaintiff has a positive reason for demanding restitution." In his article, "The Mystery of 'Juristic Reason,' " *supra*, which was cited at length by Borins J.A., Professor Smith suggests that it is not clear whether the requirement of "absence of juristic reason" should be interpreted literally to require that plaintiffs show the absence of a reason for the defendant to keep the enrichment or, as in the English model, the plaintiff must show a reason for reversing the transfer of wealth. Other commentators have argued that in fact there is no difference beyond semantics between the Canadian and English tests (see, for example, M. McInnes, "Unjust Enrichment - Restitution - Absence of Juristic Reason: *Campbell v. Campbell*" (2000), 79 Can. Bar Rev. 459).

42 Professor Smith argues that, if there is in fact a distinct Canadian approach to juristic reason, it is problematic because it requires the plaintiff to prove a negative, namely, the absence of a juristic reason. Because it is nearly impossible to do this, he suggests that Canada would be better off adopting the British model, where the plaintiff must show a positive reason that it would be unjust for the defendant to retain the enrichment. In my view, however, there is a distinctive Canadian approach to juristic reason which should be retained but can be construed in a manner that is responsive to Smith's criticism.

43 It should be recalled that the test for unjust enrichment is relatively new to Canadian jurisprudence. It requires flexibility for courts to expand the categories of juristic reasons as circumstances require and to deny recovery where to allow it would be inequitable. As McLachlin J. wrote in *Peel*, *supra*, at p. 788, the Court's approach to unjust enrichment, while

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informed by traditional categories of recovery, "is capable, however, of going beyond them, allowing the law to develop in a flexible way as required to meet changing perceptions of justice." But, at the same time, there must also be guidelines that offer trial judges and others some indication of what the boundaries of the cause of action are. The goal is to avoid guidelines that are so general and subjective that uniformity becomes unattainable.

44 The parties and commentators have pointed out that there is no specific authority that settles this question. But recalling that this is an equitable remedy that will necessarily involve discretion and questions of fairness, I believe that some redefinition and reformulation is required. Consequently, in my view, the proper approach to the juristic reason analysis is in two parts. First, the plaintiff must show that no juristic reason from an established category exists to deny recovery. By closing the list of categories that the plaintiff must canvass in order to show an absence of juristic reason, Smith's objection to the Canadian formulation of the test that it required proof of a negative is answered. The established categories that can constitute juristic reasons include a contract (*Pettkus*, *supra*), a disposition of law (*Pettkus*, *supra*), a donative intent (*Peter*, *supra*), and other valid common law, equitable or statutory obligations (*Peter*, *supra*). If there is no juristic reason from an established category, then the plaintiff has made out a *prima facie* case under the juristic reason component of the analysis.

45 The *prima facie* case is rebuttable, however, where the defendant can show that there is another reason to deny recovery. As a result, there is a de facto burden of proof placed on the defendant to show the reason why the enrichment should be retained. This stage of the analysis thus provides for a category of residual defence in which courts can look to all of the circumstances of the transaction in order to determine whether there is another reason to deny recovery.

46 As part of the defendant's attempt to rebut, courts should have regard to two factors: the reasonable expectations of the parties and public policy considerations. It may be that when these factors are considered, the court will find that a new category of juristic reason is established. In other cases, a consideration of these factors will suggest that there was a juristic reason in the particular circumstance of a case but which does not give rise to a new category of juristic reason that should be applied in other factual circumstances. In a third group of cases, a consideration of these factors will yield a determination that there was no juristic reason for the enrichment. In the latter cases, recovery should be allowed. The point here is that this area is an evolving one and that further cases will add additional refinements and developments.

47 In my view, this approach to the juristic reason analysis is consistent with the general approach to unjust enrichment endorsed by McLachlin J. in *Peel*, *supra*, where she stated that courts must effect a balance between the traditional "category" approach, according to which a claim for restitution will succeed only if it falls within an established head of recovery, and the modern "principled" approach, according to which relief is determined with reference to broad principles. It is also, as discussed by Professor Smith, *supra*, generally consistent with the approach to unjust enrichment found in the civil law of Quebec (see, for example, arts. 1493 and 1494 of the *Civil Code of Quebec*, S.Q. 1991, c. 64).

(ii) Application

48 In this case, the only possible juristic reason from an established category that could be used to justify the enrichment is the existence of the OEB orders creating the LPPs under the "disposition of law" category. The OEB orders, however, do not constitute a juristic reason for the enrichment because they are rendered inoperative to the extent of their conflict with s. 347 of the *Criminal Code*. The plaintiff has thus made out a *prima facie* case for unjust enrichment.

49 Disposition of law is well established as a category of juristic reason. In *Rathwell*, *supra*, Dickson J. gave as examples of juristic reasons "a contract or disposition of law" (p. 455). In *Reference re Excise Tax Act (Canada)*, [1992] 2 S.C.R. 445 (S.C.C.) ("*GST Reference*"), Lamer C.J. held that a valid statute is a juristic reason barring recovery in unjust enrichment. This was affirmed in *Peter*, *supra*, at p. 1018. Most recently, in *Mack v. Canada (Attorney General)* (2002), 60 O.R. (3d) 737 (Ont. C.A.), the Ontario Court of Appeal held that the legislation which created the Chinese head tax provided a juristic reason which prevented recovery of the head tax in unjust enrichment. In the leading Canadian text, *The Law of Restitution*, *supra*, McCamus and Maddaugh discuss the phrase "disposition of law" from *Rathwell*, *supra*, stating, at p. 46:

> . . . it is perhaps self-evident that an unjust enrichment will not be established in any case where enrichment of the defendant at the plaintiff's expense is required by law.

It seems clear, then, that valid legislation can provide a juristic reason which bars recovery in restitution.

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50 Consumers' Gas submits that the LPPs were authorized by the Board's rate orders, which qualify as a disposition of law. It seems to me that this submission is predicated on the validity and operability of this scheme. The scheme has been challenged by the appellant on the basis that it conflicts with s. 347 of the *Criminal Code* and, as a result of the doctrine of paramountcy, is consequently inoperative. In the *GST Reference*, *supra*, Lamer C.J. held that legislation provides a juristic reason "unless the statute itself is *ultra vires*" (p. 477). Given that legislation that would have been *ultra vires* the province cannot provide a juristic reason, the same principle should apply if the provincial legislation is inoperative by virtue of the paramountcy doctrine. This position is contemplated by Borins J.A. in his dissent when he writes, at para. 149:

> In my view, it would be wrong to say that the rate orders do not provide [Consumers' Gas] with a defence under s. 18 of the OEBA because they have been rendered inoperative by the doctrine of federal paramountcy, and then to breathe life into them for the purpose of finding that they constitute a juristic reason for [Consumers' Gas's] enrichment.

51 As a result, the question of whether the statutory framework can serve as a juristic reason depends on whether the provision is held to be inoperative. If the OEB orders are constitutionally valid and operative, they provide a juristic reason which bars recovery. Conversely, if the scheme is inoperative by virtue of a conflict with s. 347 of the *Criminal Code*, then a juristic reason is not present. In my view, the OEB rate orders are constitutionally inoperative to the extent of their conflict with s. 347 of the *Criminal Code*.

52 The OEB rate orders require the receipt of LPPs at what is often a criminal rate of interest. Such receipt is prohibited by s. 347 of the *Criminal Code*. Both the OEB rate orders and s. 347 of the *Criminal Code* are *intra vires* the level of government that enacted them. The rate orders are *intra vires* the province by virtue of s. 92(13) (property and civil rights) of the *Constitution Act, 1867*. Section 347 of the *Criminal Code is intra vires* the federal government by virtue of s. 91(19) (interest) and s. 91(27) (criminal law power).

53 It should be noted that the Board orders at issue did not require Consumers' Gas to collect the LPPs within a period of 38 days. One could then make the argument that this was not an express operational conflict. But to my mind this is somewhat artificial. I say this because at bottom it is a necessary implication of the OEB orders to require payment within this period. In that respect it should be treated as an express order for purposes of paramountcy analysis. Consequently, there is an express operational conflict between the rate orders and s. 347 of the *Criminal Code* in that it is impossible for Consumers' Gas to comply with both provisions. Where there is an actual operational conflict, it is well settled that the provincial law is inoperative to the extent of the conflict (*Multiple Access Ltd. v. McCutcheon*, [1982] 2 S.C.R. 161 (S.C.C.), at p. 191; *M & D Farm Ltd. v. Manitoba Agricultural Credit Corp.*, [1999] 2 S.C.R. 961 (S.C.C.)). As a result, the Board orders are constitutionally inoperative. Because the Board orders are constitutionally inoperative, they do not provide a juristic reason. It therefore falls to Consumers' Gas to show that there was a juristic reason for the enrichment outside the established categories in order to rebut the *prima facie* case made out by the appellant.

54 The second stage of juristic reason analysis requires a consideration of reasonable expectations of the parties and public policy considerations.

55 When the reasonable expectations of the parties are considered, Consumers' Gas's submissions are at first blush compelling. Consumers' Gas submits, on the one hand, that late payers cannot have reasonably expected that there would be no penalty for failing to pay their bills on time and, on the other hand, that Consumers' Gas could reasonably have expected that the OEB would not authorize an LPP scheme that violated the *Criminal Code*. Because Consumers' Gas is operating in a regulated environment, their reliance on OEB orders should be given some weight. An inability to rely on such orders would make it very difficult, if not impossible, to operate in this environment. At this point, it should be pointed out that the reasonable expectation of the parties regarding LPPs is achieved by restricting the LPPs to the limit prescribed by s. 347 of the *Criminal Code* and also would be consistent with this Court's decision in *Transport North American Express Inc. v. New Solutions Financial Corp.*, [2004] 1 S.C.R. 249, 2004 SCC 7 (S.C.C.).

56 Consumers' Gas's reliance on the orders would not provide a defence if it was charged under s. 347 of the *Criminal Code* because they are inoperative to the extent of their conflict with s. 347. However, its reliance on the orders is relevant in the context of determining the reasonable expectations of the parties in this second stage of the juristic reason analysis.

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57 Finally, the overriding public policy consideration in this case is the fact that the LPPs were collected in contravention of the *Criminal Code*. As a matter of public policy, a criminal should not be permitted to keep the proceeds of their crime (*Oldfield v. Transamerica Life Insurance Co. of Canada*, [2002] 1 S.C.R. 742, 2002 SCC 22 (S.C.C.), at para. 11; *New Solutions*, *supra*). Borins J.A. focused on this public policy consideration in his dissent. He held that, in light of this Court's decision in *Garland #1*, allowing Consumers' Gas to retain the LPPs collected in violation of s. 347 would let Consumers' Gas profit from a crime and benefit from its own wrongdoing.

58 In weighing these considerations, from 1981-1994, Consumers' Gas's reliance on the inoperative OEB orders provides a juristic reason for the enrichment. As the parties have argued, there are three possible dates from which to measure the unjust enrichment: 1981, when s. 347 of the *Criminal Code* was enacted, 1994, when this action was commenced, and 1998, when this Court held in *Garland #1* that the LPPs were limited by s. 347 of the *Criminal Code*. For the period between 1981 and 1994, when the current action was commenced, there is no suggestion that Consumers' Gas was aware that the LPPs violated s. 347 of the *Criminal Code*. This mitigates in favour of Consumers' Gas during this period. The reliance of Consumers' Gas on the OEB orders, in the absence of actual or constructive notice that the orders were inoperative is sufficient to provide a juristic reason for Consumers' Gas's enrichment during this first period.

59 However, in 1994 when this action was commenced, Consumers' Gas was put on notice of the serious possibility that it was violating the *Criminal Code* in charging the LPPs. This possibility became a reality when this Court held that the LLPs were in excess of the s. 347 limit. Consumers' Gas could have requested that the OEB alter its rate structure until the matter was adjudicated in order to ensure that it was not in violation of the *Criminal Code* or asked for contingency arrangements to be made. Its decision not to do this, as counsel for the appellant pointed out in oral submissions, was a "gamble." After the action was commenced and Consumers' Gas was put on notice that there was a serious possibility the LPPs violated the *Criminal Code*, it was no longer reasonable for Consumers' Gas to rely on the OEB rate orders to authorize the LPPs.

60 Moreover, once this Court held that LPPs were offside, for purposes of unjust enrichment, it is logical and fair to choose the date on which the action for redress commenced. Awarding restitution from 1981 would be unfair to the respondent since it was entitled to reasonably rely on the OEB orders until the commencement of this action in 1994. Awarding restitution from 1998 would be unfair to the appellant. This is because it would permit the respondent to retain LPPs collected in violation of s. 347 after 1994 when it was no longer reasonable for the respondent to have relied on the OEB orders and the respondent should be presumed to have known the LPPs violated the *Criminal Code*. Further, awarding restitution from 1998 would deviate from the general rule that monetary remedies like damages and interest are awarded as of the date of occurrence of the breach or as of the date of action rather than the date of judgment.

61 Awarding restitution from 1994 appropriately balances the respondent's reliance on the OEB orders from 1981-1994 with the appellant's expectation of recovery of monies that were charged in violation of the *Criminal Code* once the serious possibility that the OEB orders were inoperative had been raised. As a result, as of the date this action was commenced in 1994, it was no longer reasonable for Consumers' Gas to rely on the OEB orders to insulate them from liability in a civil action of this type for collecting LPPs in contravention of the *Criminal Code*. Thus, after the action was commenced in 1994, there was no longer a juristic reason for the enrichment of the respondent, so the appellant is entitled to restitution of the portion of monies paid to satisfy LPPs that exceeded an interest rate of 60 per cent, as defined in s. 347 of the *Criminal Code*.

B. Defences

62 Having held that the appellant's claim for unjust enrichment is made out for LPPs paid after 1994, it remains to be determined whether the respondent can avail itself of any defences raised. It is only necessary to consider the defences for the period after 1994, when the elements of unjust enrichment are made out, and thus I will not consider whether the defences would have applied if there had been unjust enrichment before 1994. I will address each defence in turn.

(a) Change of Position Defence

63 Even where the elements of unjust enrichment are made out, the remedy of restitution will be denied where an innocent defendant demonstrates that it has materially changed its position as a result of an enrichment such that it would be inequitable to require the benefit to be returned (*Storthoaks*, *supra*). In this case, the respondent says that any "benefit" it

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received from the unlawful charges was passed on to other customers in the form of lower gas delivery rates. Having "passed on" the benefit, it says, it should not be required to disgorge the amount of the benefit (a second time) to overcharged customers, such as the appellant. The issue here, however, is not the ultimate destination within the regulatory system of an amount of money equivalent to the unlawful overcharges, nor is this case concerned with the net impact of these overcharges on the respondent's financial position. The issue is whether, as between the overcharging respondent and the overcharged appellant, the passing of the benefit on to other customers excuses the respondent of having overcharged the appellant.

64 The appellant submits that the defence of change of position is not available to a defendant who is a wrongdoer and that, since the respondent in this case was enriched by its own criminal misconduct, it should not be permitted to avail itself of the defence. I agree. The rationale for the change of position defence appears to flow from considerations of equity. G.H.L. Fridman writes that "[o]ne situation which would appear to render it inequitable for the defendant to be required to disgorge a benefit received from the plaintiff in the absence of any wrongdoing on the part of the defendant would be if he has changed his position for the worse as a result of the receipt of the money in question" (*Restitution*, 2nd ed. (Toronto: Carswell, 1992), at p. 458). In the leading British case on the defence, *Gorman v. Karpnale Ltd.* (1991), [1992] 4 All E.R. 512 (U.K. H.L.), Lord Goff stated (at p. 533):

> [I]t is right that we should ask ourselves: why do we feel that it would be unjust to allow restitution in cases such as these [where the defendant has changed his or her position]? The answer must be that, where an innocent defendant's position is so changed that he will suffer an injustice if called upon to repay or to repay in full, the injustice of requiring him so to repay outweighs the injustice of denying the plaintiff restitution.

65 If the change of position defence is intended to prevent injustice from occurring, the whole of the plaintiff's and defendant's conduct during the course of the transaction should be open to scrutiny in order to determine which party has a better claim. Where a defendant has obtained the enrichment through some wrongdoing of his own, he cannot then assert that it would be unjust to return the enrichment to the plaintiff. In this case, the respondent cannot avail itself of this defence because the LPPs were obtained in contravention of the *Criminal Code* and, as a result, it cannot be unjust for the respondent to have to return them.

66 Thus, the change of position defence does not help the respondent in this case. Even assuming that the respondent would have met the other requirements set out in *Storthoaks*, *supra*, the respondent cannot avail itself of the defence because it is not an "innocent" defendant given that the benefit was received as a result of a *Criminal Code* violation. It is not necessary, as a result, to discuss change of position in a comprehensive manner and I leave a fuller development of the other elements of this defence to future cases.

(b) Section 18/25 of the Ontario Energy Board Act

67 The respondent raises a statutory defence found formerly in s. 18 and presently in s. 25 of the 1998 OEBA. The former and the present sections are identical and read:

> An order of the Board is a good and sufficient defence to any proceeding brought or taken against any person in so far as the act or omission that is the subject of the proceeding is in accordance with the order.

I agree with McMurty C.J.O. that this defence should be read down so as to exclude protection from civil liability damage arising out of *Criminal Code* violations. As a result, the defence does not apply in this case and we do not have to consider the constitutionality of the section.

68 McMurtry C.J.O. was correct in his holding that legislative provisions purporting to restrict a citizen's rights of action should attract strict construction (*Berardinelli*, *supra*). In this case, I again agree with McMurtry C.J.O. that the legislature could not reasonably be believed to have contemplated that an OEB order could mandate criminal conduct, despite the broad wording of the section. Section 18/25 thus cannot provide a defence to an action for restitution arising from an OEB order authorizing criminal conduct. As a consequence, like McMurtry C.J.O., I find the argument on s. 18/25 to be unpersuasive.

69 Because I find that it could not have been the intention of the legislature to bar civil claims stemming from acts that

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offend the *Criminal Code*, on a strict construction, s. 18/25 cannot protect Consumers' Gas from these types of claims. If the provincial legislature had wanted to eliminate the possibility of such actions, it should have done so explicitly in the provision. In the absence of such explicit provision, s. 18/25 must be read so as to exclude from its protection civil actions arising from violations of the *Criminal Code* and thus does not provide a defence for the respondent in this case.

(c) Exclusive Jurisdiction and Collateral Attack

70 McMurtry C.J.O. was also correct in his holding that the OEB does not have exclusive jurisdiction over this dispute. While the dispute does involve rate orders, at its heart it is a private law matter under the competence of civil courts and, consequently, the Board does not have jurisdiction to order the remedy sought by the appellant.

71 In addition, McMurtry C.J.O. is correct in holding that this action does not constitute an impermissible collateral attack on the OEB's order. The doctrine of collateral attack prevents a party from undermining previous orders issued by a court or administrative tribunal (see *Toronto (City) v. C.U.P.E., Local 79*, [2003] 3 S.C.R. 77, 2003 SCC 63 (S.C.C.); Donald J. Lange, *The Doctrine of Res Judicata in Canada* (Markham, Ont.: Butterworths, 2000), at pp. 369-370). Generally, it is invoked where the party is attempting to challenge the validity of a binding order in the wrong forum, in the sense that the validity of the order comes into question in separate proceedings when that party has not used the direct attack procedures that were open to it (i.e., appeal or judicial review). In *R. v. Wilson*, [1983] 2 S.C.R. 594 (S.C.C.), at p. 599, this Court described the rule against collateral attack as follows:

> It has long been a fundamental rule that a court order, made by a court having jurisdiction to make it, stands and is binding and conclusive unless it is set aside on appeal or lawfully quashed. It is also well settled in the authorities that such an order may not be attacked collaterally - and a collateral attack may be described as an attack made in proceedings other than those whose specific object is the reversal, variation, or nullification of the order or judgment.

Based on a plain reading of this rule, the doctrine of collateral attack does not apply in this case because here the specific object of the appellant's action is not to invalidate or render inoperative the Board's orders, but rather to recover money that was illegally collected by the respondent as a result of Board orders. Consequently, the collateral attack doctrine does not apply.

72 Moreover, the appellant's case lacks other hallmarks of collateral attack. As McMurtry C.J.O. points out at para. 30 of his reasons, the collateral attack cases all involve a party, bound by an order, seeking to avoid the effect of that order by challenging its validity in the wrong forum. In this case, the appellant is not bound by the Board's orders; therefore, the rationale behind the rule is not invoked. The fundamental policy behind the rule against collateral attack is to "maintain the rule of law and to preserve the repute of the administration of justice" (*R. v. Litchfield*, [1993] 4 S.C.R. 333 (S.C.C.), at p. 349). The idea is that if a party could avoid the consequences of an order issued against it by going to another forum, this would undermine the integrity of the justice system. Consequently, the doctrine is intended to prevent a party from circumventing the effect of a decision rendered against it.

73 In this case, the appellant is not the object of the orders and thus there can be no concern that he is seeking to avoid the orders by bringing this action. As a result, a threat to the integrity of the system does not exist because the appellant is not legally bound to follow the orders. Thus, this action does not appear, in fact, to be a collateral attack on the Board's orders.

(d) The Regulated Industries Defence

74 The respondent submits that it can avail itself of the "regulated industries defence" to bar recovery in restitution because an act authorized by a valid provincial regulatory scheme cannot be contrary to the public interest or an offence against the state and, as a result, the collection of LPPs pursuant to orders issued by the OEB cannot be considered to be contrary to the public interest and thus cannot be contrary to s. 347 of the *Criminal Code*.

75 Winkler J. held that the underlying purpose of the defence, regulation of monopolistic industries in order to ensure "just and reasonable" rates for consumers, would be served in the circumstances and, as a result, the defence would normally apply. However, because of the statutory language of s. 347, Winkler J. determined that the defence was not permitted in this

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case. He wrote, at para. 34, "[t]he defendant can point to no case which allows the defence unless the federal statute in question uses the word 'unduly' or the phrase 'in the public interest.' " Absent such recognition in the statute of "public interest," he held, no leeway for provincial exceptions exist.

76 I agree with the approach of Winkler J. The principle underlying the application of the defence is delineated in *Canada (Attorney General) v. Law Society (British Columbia)*, [1982] 2 S.C.R. 307 (S.C.C.), at p. 356:

> When a federal statute can be properly interpreted so as not to interfere with a provincial statute, such an interpretation is to be applied in preference to another applicable construction which would bring about a conflict between the two statutes.

Estey J. reached this conclusion after canvassing the cases in which the regulated industries defence had been applied. Those cases all involved conflict between federal competition law and a provincial regulatory scheme, but the application of the defence in those cases had to do with the particular wording of the statutes in question. While I cannot see a principled reason why the defence should not be broadened to apply to cases outside the area of competition law, its application should flow from the above enunciated principle.

77 Winkler J. was correct in concluding that, in order for the regulated industries defence to be available to the respondent, Parliament needed to have indicated, either expressly or by necessary implication, that s. 347 of the *Criminal Code* granted leeway to those acting pursuant to a valid provincial regulatory scheme. If there were any such indication, I would say that it should be interpreted, in keeping with the above principle, not to interfere with the provincial regulatory scheme. But s. 347 does not contain the required indication for exempting a provincial scheme.

78 This view is further supported by this Court's decision in *R. v. Jorgensen*, [1995] 4 S.C.R. 55 (S.C.C.). In that case, the accused was charged with "'knowingly' selling obscene material 'without lawful justification or excuse' " (para. 44). The accused argued that the Ontario Film Review Board had approved the videotapes; therefore, it had a lawful justification or excuse. This Court considered whether approval by a provincial body could displace a criminal charge. Sopinka J., for the majority, held that in order to exempt acts taken pursuant to a provincial regulatory body from the reach of the criminal law, Parliament must unequivocally express this intention in the legislative provision in issue (at para. 118):

> While Parliament has the authority to introduce dispensation or exemption from criminal law in determining what is and what is not criminal, and may do so by authorizing a provincial body or official acting under provincial legislation to issue licences and the like, an intent to do so must be made plain.

79 The question of whether the regulated industries defence can apply to the respondent is actually a question of whether s. 347 of the *Criminal Code* can support the notion that a valid provincial regulatory scheme cannot be contrary to the public interest or an offence against the state. In the previous cases involving the regulated industries defence, the language of "the public interest" and "unduly" limiting competition has always been present. The absence of such language from s. 347 of the *Criminal Code* precludes the application of this defence in this case.

(e) De Facto Doctrine

80 Consumers' Gas submits that because it was acting pursuant to a disposition of law that was valid at the time - the Board orders - they should be exempt from liability by virtue of the *de facto* doctrine. This argument cannot succeed. Consumers' Gas is not a government official acting under colour of authority. While the respondent points to the Board orders as justification for its actions, this does not bring the respondent into the purview of the *de facto* doctrine because the case law does not support extending the doctrine's application beyond the acts of government officials. The underlying purpose of the doctrine is to preserve law and order and the authority of the government. These interests are not at stake in the instant litigation. As a result, Consumers' Gas cannot rely on the *de facto* doctrine to resist the plaintiff's claim.

81 Furthermore, the *de facto* doctrine attaches to government and its officials in order to protect and maintain the rule of law and the authority of government. An extension of the doctrine to a private corporation that is simply regulated by a government authority is not supported by the case law and, in my view, does not further the underlying purpose of the

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doctrine. In *Reference re Language Rights Under s. 23 of Manitoba Act, 1870 & s. 133 of Constitution Act, 1867*, [1985] 1 S.C.R. 721 (S.C.C.), this Court held, at p. 756, that:

> There is only one true condition precedent to the application of the doctrine: the *de facto* officer must occupy his or her office under colour of authority.

It cannot be said that Consumers' Gas was a *de facto* officer acting under colour of authority when it charged LPPs to customers. Consumers' Gas is a private corporation acting in a regulatory context, not an officer vested with some sort of authority. When charging LPPs, Consumers' Gas is engaging in commerce, not issuing a permit or passing a by-law.

82 In rejecting the application of the *de facto* doctrine here, I am cognizant of the passage in *Reference re Language Rights*, at p. 757, cited by the intervener Toronto Hydro and which, at first glance, appears to imply that the *de facto* doctrine might apply to private corporations:

> . . . the *de facto* doctrine will save those rights, obligations and other effects which have arisen out of actions performed pursuant to invalid Acts of the Manitoba Legislature by public *and private bodies corporate*, courts, judges, persons exercising statutory powers and public officials. [Emphasis added.]

83 While this passage appears to indicate that "private bodies corporate" are protected by the doctrine, it must be read in the context of the entire judgment. Earlier, at p. 755, the Court referred to the writings of Judge A. Constantineau in *The De Facto Doctrine* (1910), at pp. 3-4. The following excerpt from that passage is relevant:

> The de facto doctrine is a rule or principle of law which . . . *recognizes the existence of*, and protects from collateral attack, public or *private bodies corporate*, which, *though irregularly or illegally organized*, yet, under color of law, openly exercise the powers and functions of regularly created bodies . . . [Emphasis added.]

In this passage, I think it is clear that the Court's reference to "private bodies corporate" is limited to issues affecting the creation of the corporation, for example, where a corporation was incorporated under an invalid statute. It does not suggest that the acts of the corporation are shielded from liability by virtue of the *de facto* doctrine.

84 This view finds further support in the following passage from the judgment (at p. 755):

> That the foundation of the principle is the more fundamental principle of the rule of law is clearly stated by Constantineau in the following passage (at pp. 5-6):
>
> > Again, the doctrine is necessary to maintain the supremacy of the law and to preserve peace and order in the community at large, since any other rule would lead to such uncertainty and confusion, as to break up the order and quiet of all civil administration. Indeed, if any individual or body of individuals were permitted, at his or their pleasure, to challenge the authority of and refuse obedience to the government of the state and the numerous functionaries through whom it exercises its various powers, or refuse to recognize municipal bodies and their officers, on the ground of irregular existence or defective titles insubordination and disorder of the worst kind would be encouraged, which might at any time culminate in anarchy.

The underlying purpose of the doctrine is to preserve law and order and the authority of the government. These interests are not at stake in the instant litigation. In sum, I find no merit in Consumers' Gas's argument that the *de facto* doctrine shields it from liability and, as a result, this doctrine should not be a bar to the appellant's recovery.

C. Other Orders Requested

(a) Preservation Order

85 The appellant, Garland, requests an "*Amax-type*" preservation order on the basis that the LPPs continue to be collected at a criminal rate during the pendency of this action, and these payments would never have been made but for the delays

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inherent in litigation (*Amax Potash Ltd. v. Saskatchewan* (1976), [1977] 2 S.C.R. 576 (S.C.C.)). In my view, however, a preservation order is not appropriate in this case. Consumers' Gas has now ceased to collect the LPPs at a criminal rate. As a result, if a preservation order were made, there would be no future LPPs to which it could attach. Even with respect to the LPPs paid between 1994 and the present, to which such an order could attach, a preservation order should not be granted for three further reasons: (1) such an order would serve no practical purpose, (2) the appellant has not satisfied the criteria in the Ontario *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194, and (3) *Amax Potash Ltd.* can be distinguished from this case.

86 First, the appellant has not alleged that Consumers' Gas is an impecunious defendant or that there is any other reason to believe that Consumers' Gas would not satisfy a judgment against it. Even if there were some reason to believe that Consumers' Gas would not satisfy such a judgment, an *Amax Potash Ltd.*-type order allows the defendant to spend the monies being held in the ordinary course of business - no actual fund would be created. So the only thing that a preservation order would achieve would be to prevent Consumers' Gas from spending the money earned from the LPPs in a non-ordinary manner (for example, such as moving it off-shore), which the appellant has not alleged is likely to occur absent the order.

87 Second, the respondent submits that by seeking a preservation order the appellant is attempting to avoid R. 45.02 of the Ontario *Rules of Civil Procedure*, the only source of jurisdiction in Ontario to make a preservation order. The *Rules of Civil Procedure* apply to class proceedings and do not permit such an order in these circumstances. Rule 45.02 provides that, "Where the right of a party to a *specific fund* is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just" (emphasis added). The respondent submits that the appellant is not in fact claiming a specific fund here. In the absence of submissions by the appellant on this issue, I am of the view that the appellant has not satisfied the criteria set out in the Ontario *Rules of Civil Procedure* and that this Court could refuse to grant the order requested on this basis.

88 Finally, the appellant's use of *Amax Potash Ltd.*, *supra*, as authority for the type of order sought is without merit. The appellant has cited the judgment very selectively. The portion of the judgment the appellant cites in his written submissions reads in full (at p. 598):

> Apart from the Rules this Court has the discretion to make an order as requested by appellants directing the Province of Saskatchewan to hold, as stakeholder, such sums as are paid by the appellants pursuant to the impugned legislation but with the right to use such sums in the interim for Provincial purposes, and with the obligation to repay them with interest in the event the legislation is ultimately held to be *ultra vires*. *Such an order, however, would be novel, in giving the stakeholder the right to spend the moneys at stake, and I cannot see that it would serve any practical purpose*. [Emphasis added.]

The Court in *Amax* went on to refuse to make the order. So while the appellant is right that the Court in *Amax* failed to reject the hypothetical possibility of making such an order in the future, it seems to me that in this case, as in *Amax*, such an order would serve no practical purpose. For these reasons, I find there is no basis for making a preservation order in this case.

(b) Declaration that the LPPs Need Not Be Paid

89 The appellant also seeks a declaration that the LPPs need not be paid. Given that the respondent asserts that the LPP is no longer charged at a criminal rate, issuing such a declaration would serve no practical purpose and, as a result, such a declaration should not be made.

(c) Costs

90 The appellant is entitled to his costs throughout. This should be understood to mean that, regardless of the outcome of any future litigation, the appellant is entitled to his costs in the proceedings leading up to and including *Garland #1* and this appeal. In addition, in oral submissions counsel for the Law Foundation of Ontario made the point that in order to reduce costs in future class actions, "litigation by instalments," as occurred in this case, should be avoided. I agree. On this issue, I endorse the comments of McMurty C.J.O., at para. 76 of his reasons:

> In this context, I note the protracted history of these proceedings cast some doubt on the wisdom of hearing a case in

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instalments, as was done here. Before employing an instalment approach, it should be considered whether there is potential for such a procedure to result in multiple rounds of proceedings through various levels of court. Such an eventuality is to be avoided where possible, as it does little service to the parties or to the efficient administration of justice.

VI. Disposition

91 For the foregoing reasons, I would allow the appeal with costs throughout, set aside the judgment of the Ontario Court of Appeal, and substitute therefor an order that Consumers' Gas repay LPPs collected from the appellant in excess of the interest limit stipulated in s. 347 after the action was commenced in 1994 in an amount to be determined by the trial judge.

Appeal allowed.
Pourvoi accueilli.

Footnotes

* On June 2, 2004, the court issued a corrigendum correcting text; the change has been incorporated herein.

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TAB 3

1995 CarswellOnt 326
Ontario Court of Justice (General Division)

Toronto Dominion Bank v. Bank of Montreal

1995 CarswellOnt 326, [1995] O.J. No. 176, 18 B.L.R. (2d) 248, 22 O.R. (3d) 362, 53 A.C.W.S. (3d) 209, 6 E.T.R. (2d) 202

TORONTO-DOMINION BANK v. BANK OF MONTREAL, RICHARD BAIN, LOUIS REZNICK, ANTHONY F. GRIFFITHS, ALLAN D. HORN and W. DAVID WILSON

MacPherson J.

Heard: January 9-10, 1995
Judgment: February 2, 1995
Docket: Doc. 67305/91Q

Counsel: *Joel Goldenberg*, for plaintiff.
Burton Tait, Q.C., for defendant Bank of Montreal.
Bruce Thomas, for defendant Richard Bain.
D.N. Plumley, Q.C., and *J.C. D'Angelo*, for defendants *Anthony F. Griffiths*, *Allan D. Horn* and *W. David Wilson*.
Defendant *Louis Reznick*, in person.

Subject: Corporate and Commercial; Estates and Trusts; Restitution

Related Abridgment Classifications

Restitution and unjust enrichment
II Benefits conferred under mistake
II.1 Mistake of fact

Headnote

Restitution --- Benefits conferred under mistake — Mistake of fact

Banking and banks — Cheques — Accepted or certified cheques — Bank error in entering amount of deposit — Incorrect amount ultimately drawn on by cheque that was certified by bank which made error — Cheque deposited in payee's account at second bank and funds withdrawn — No unjust enrichment — Bank in error not entitled to equitable relief — Reliance on mistake.

The plaintiff bank, TD, commenced an action to recover $425,003.07 from the defendant bank, BMo, and from RB, LR, AG, AH and DW, former directors of C Corp., a bankrupt company. Prior to its bankruptcy on June 29, 1990, C Corp. was a retailer of carpet and related products in Canada and the U.S. BMo was C Corp.'s principal banker and had extended to C Corp. secured lines of credit totalling $10,000,000. C Corp. also maintained an account at a Toronto TD branch for the purposes of receiving credit card deposits from across Canada. C Corp.'s practice was to transfer the money from this TD account every two or three days to its main account at BMo.

C Corp.'s board of directors determined on June 20 and 21, 1990 that C Corp. was in serious financial difficulty and meetings were arranged for June 25 with representatives of BMo to discuss the situation.

On June 21, a teller at a TD branch in LaSalle, Quebec, posted a wire transfer deposit to the TD account of C Corp. in Toronto but made a mistake while typing the entry on the computer and $450,000.50 was deposited to the C Corp. account

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instead of the correct amount of $450.50. The error was not detected at the LaSalle TD branch until the morning of June 22, and the LaSalle TD branch did not notify the Toronto TD branch of the error by telephone until later that day. A Toronto TD branch ledger clerk reported the error to her supervisor, who had the authority to make correcting entries in the C Corp. account. The supervisor failed to make the correction. C Corp. employees detected the increased balance in C Corp.'s TD branch account and after making inquiries to verify the balance, were advised by TD that there had been no unusual postings.

A C Corp. employee shortly thereafter attended at the Toronto TD branch and presented for certification a cheque in the amount of $585,000 which was duly certified by TD and deposited by C Corp. to the credit of its current account at BMo. TD contacted no one at C Corp. to notify it that the cheque had been certified in error and BMo had no notice of any problem with respect to the cheque. The cheque was honoured by TD when presented to TD by BMo on June 25.

During that same week, C Corp. exceeded its $10,000,000 line of credit with BMo. On both occasions, a representative of BMo immediately called C Corp. to insist on coverage of such excess and C Corp. complied. On June 25, C Corp. met with BMo and BMo was told that C Corp. was insolvent. On June 26, BMo notified C Corp. that unless the amount in excess of the line of credit was covered, BMo would return all cheques drawn on C Corp.'s account received on June 22 which would include two payroll cheques for C Corp.'s employees. C Corp. instructed BMo to stop payment on all cheques issued by C Corp., commencing with those received on June 22, except for the two payroll cheques. BMo wanted the C Corp. directors to remain in office and the C Corp. directors notified BMo that they would be prepared to stay on as directors of C Corp. if BMo would indemnify them against personal liability for the payment of employee wages and other benefits after June 25. BMo was not willing to permit the line of credit to exceed $10,000,000 which at that time was drawn down to $9,968,315.

The next day, BMo and C Corp. discovered the $450,500.50 deposit to the credit of C Corp. in the BMo account. Neither C Corp. nor BMo knew that this cheque resulted from TD's errors. On June 27, BMo certified a C Corp. cheque payable to FR, a law firm, in trust, in the amount of $586,835 which was deposited into an FR trust fund for the payment of wages of C Corp. employees. The amount of the cheque represented the difference between C Corp.'s outstanding loans balance on June 26 and its line of credit. Absent the certification and delivery of the cheque, the C Corp. directors would have resigned on June 26.

On June 29, C Corp. made an assignment in bankruptcy. On the same day, a debit memo sent from the LaSalle TD branch arrived at the Toronto TD branch. It had been delayed in transit for a week because it had originally been misdirected to a non-existing Toronto TD branch. The debit memo resulted in an overdraft in excess of $400,000 in the C Corp. TD account. Late in the afternoon on July 3, TD notified BMo of the mistake that had occurred and requested the return of the amount of the original certified cheque. TD advised C Corp. of the mistake on July 5 and on the same day made a written demand on FR for reimbursement out of the trust fund. TD sued for recovery of money from the trust account, less recoveries received from C Corp. from time to time in the intervening years. TD's statement of claim was framed in terms of allegations of breach of trust, negligence, conversion and unjust enrichment against all defendants. At trial, TD proceeded against the defendants only on the basis of unjust enrichment.

Held:

The action was dismissed against all defendants.

Certification of a cheque by a bank is irrevocable and there is no distinction between certification obtained by the payer or by the payee. Certification creates a status in the cheque which is the equivalent of acceptance of such certified cheque regardless of who is responsible for certification. TD could not resile from the certified cheque that it gave to BMo.

TD did not establish the elements of unjust enrichment at trial. There are three requirements to be satisfied before an unjust enrichment can be said to exist: an enrichment; a corresponding deprivation; and an absence of any juristic reason for the enrichment. BMo conceded the first two elements; however, there was a juristic reason for BMo to receive and retain the funds transferred to it by TD. C Corp. owed a very substantial debt to BMo and the existence of this debt and BMo's instant use of the cheque to reduce the debt was a juristic reason for BMo's retention of the money. Money paid under a mistake of fact that is used to discharge a debt owed to the payee by the payer is an exception to the general principle that a person who pays money under a mistake of fact should be able to recover it.

Unjust enrichment is an equitable remedy and the party claiming it must establish that its conduct leading to its deprivation was untainted. Given the conduct of the TD employees in this matter and the delay of TD in seeking recovery of the money

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paid under the mistake, it would have been against commercial conscience to have allowed TD to recover on unjust enrichment grounds. In contrast, BMo and the C Corp. directors acted in good faith and made efforts to permit C Corp. to remain in business and to pay the C Corp. employees the wages that they were entitled to receive.

BMo was entitled to rely on the reliance exception to recovery of money paid under a mistake of fact. BMo and the C Corp. directors made fundamental decisions concerning the management of C Corp.'s bank account and its indebtedness to BMo in reliance on the day-by-day state of the bank accounts, including the proceeds of the mistaken cheque. Without the mistaken funds, BMo might have made different decisions during that week, including an attempt to realize sooner on its security against C Corp. and with better results. Absent the mistaken funds, BMo's vigilant policing of the excess in C Corp.'s line of credit would almost certainly have led BMo to make decisions different from those it in fact made at the time.

TD failed to establish its claim against the directors because it could not be said that they received an incontrovertible benefit. A claim for unjust enrichment can succeed only if the benefit received by the person enriched is "incontrovertible" or "demonstrable" or "unquestionable." The fact that a portion of the money paid by TD to C Corp. under the mistake was used to establish a fund to pay the wages to the C Corp. employees was insufficient to establish the required benefit. No employee of C Corp. ever made a claim under s. 131 of the *Business Corporations Act* (Ont.) for payment of wages by a director of C Corp., nor did any of the directors receive any of the money in the FR trust fund. Accordingly, the directors received no direct benefit, and, as for indirect benefit, no one initiated an action against the directors under the statute.

In addition, the directors' receipt and use of the money received through TD's mistake was completely innocent. The directors served C Corp. faithfully and took important steps to protect their employees and manage C Corp. during a period of financial hardship. During that same period, TD was slow and inept in its attempts to recover the money. Unjust enrichment is an equitable doctrine; the equities favoured the directors and TD did not succeed in its attempt to invoke it.

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Cases considered:

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A.E. LePage Real Estate Services Ltd. v. Rattray Publications Ltd. (1994), 21 O.R. (3d) 164, 120 D.L.R. (4th) 499, (sub nom. *LePage (A.E.) Investments Ltd. v. Canadian Imperial Bank of Commerce)* 77 O.A.C. 280 (C.A.) — *followed*

Atlas Cabinets & Furniture Ltd. v. National Trust Co. (1990), 38 C.L.R. 106, 45 B.C.L.R. (2d) 99, 37 E.T.R. 16, 68 D.L.R. (4th) 161 (C.A.) — *applied*

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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 v. Harowitz (1994), 17 O.R. (3d) 671 (Gen. Div.) — *referred to*

Sorochan v. Sorochan, [1986] 2 S.C.R. 38, [1986] 5 W.W.R. 289, 46 Alta. L.R. (2d) 97, 2 R.F.L. (3d) 225, 29 D.L.R. (4th) 1, 69 N.R. 81, 23 E.T.R. 143, [1986] R.D.I. 448, [1986] R.D.F. 501, 74 A.R. 67 — *referred to*

Storthoaks (Rural Municipality) v. Mobil Oil Canada Ltd., [1976] 2 S.C.R. 147, [1975] 4 W.W.R. 591, 5 N.R. 23, 55 D.L.R. (3d) 1 — *referred to*

Statutes considered:

Bills of Exchange Act, R.S.C. 1985, c. B-4 —

s. 2 "acceptance"

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s. 131

Action to recover moneys paid by mistake on basis of unjust enrichment.

MacPherson J.:

Introduction

1 This case presents an unusual mix of high comedy and financial tragedy in the normally bland worlds of banking and retail sales. The story unfolds in a two-week period in the summer of 1990.

2 The comedy is all on a major national bank's side. In a milliseconda teller in a small Quebec branch made a mistake and gave away almost half a million dollars. Then, for the next two weeks, bank personnel in Quebec and Ontario stumbled around, almost in Keystone Kops fashion, trying to retrieve the money.

3 The financial tragedy is on the side of a retail carpet chain which received the money by mistake just as it was tumbling into bankruptcy.

4 From the perspective of the actors involved, the events on the bank's comedy stage and the carpet company's tragedy stage unfolded, they thought, in splendid isolation from each other. They were wrong. In fact, unbeknownst to the actors, the comedy and the tragedy intersected. And five years later they intersect again in this trial because the bank, which lost the large sum of money entirely through its own errors, believes that it is entitled to recover the money from another bank and from the former directors of the corporation, both of whom used the money without realizing that they had obtained it by mistake.

A. Factual Background

5 The trial proceeded on the basis of an Agreed Statement of Facts. The parties and their counsel are to be complimented for converting what could have been a long trial involving many witnesses into a one-and-a-half-day trial devoted entirely to

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legal argument.

6 The plaintiff, Toronto-Dominion Bank ("TD"), sues to recover $425,003.07 from either the Bank of Montreal ("B of M"), or the former directors of Carpita Corporation ("Carpita"), Messrs. Bain, Reznick, Griffiths, Horn and Wilson.

7 Prior to its bankruptcy on June29, 1990, Carpita carried on business across Canada and in the United States as a retailer of carpet and related products under the business name Factory Carpet.

8 B of M was the principal banker of Carpita and, at the relevant time in 1990, had extended to Carpita lines of credit aggregating $10,000,000. B of M had valid security over Carpita's assets, including its receivables.

9 Carpita also maintained an account at the College and Spadina branch of TD. It used this account for the receipt of Visa deposits from across Canada. Every two or three days the money was transferred from this account to Carpita's main account at the B of M.

10 On June 20 and 21, 1990, the Board of Directors of Carpita met to discuss the precarious financial position of the corporation. There was a discrepancy of $2,500,000 between the company's own financial records and its bank statements. It also appeared that the corporation might have lost $20,000,000 in the previous fiscal year. One director, Mr.Beutel, scrambled for cover and resigned on the morning of June 21. The other directors decided to notify B of M, the company's principal banker, with a view to discussing the situation. A meeting was set for Monday, June 25, the earliest date on which representatives of B of M were available.

11 Meanwhile, on June 21 as well, a completely different set of events was set in motion. A teller at a TD branch in LaSalle, Quebec made two keying errors. She kept her finger on a key too long, thus shifting decimals in two entries by three spaces. The result was a wire transfer deposit into the TD College and Spadina branch to the credit of Carpita in the amount of $450,500.50 instead of the correct amount of $450.50.

12 The teller did not detect her error. At the close of business on June 21 she would have known that her records were out of balance. However, as a matter of risk management it is not worth it to TD to find the error that day. Reports are produced overnight by TD's data centre and such errors are usually found before the branch opens for business the next day.

13 In this instance the posting error was detected at the LaSalle branch at about 10:00 a.m. on June 22, 1990. It was discussed among employees and a Mr. Laberge was instructed to call the Toronto branch. He began by first preparing a written interbranch debit and then turned to other branch business. At noon he attempted to telephone the Toronto branch. He didn't get through then. However, at about 2:30 p.m. someone in the Quebec branch spoke by telephone to a ledger clerk at the TD Toronto branch advising her of the error. The clerk reported the error to her supervisor. The supervisor had the authority to make, and should have made, correcting entries in the Carpita account. She did not do so.

14 Meanwhile, on the same day, Friday, June 22, Ms Friedrichs, a clerk at Carpita, telephoned the TD branch to inquire about the balance in the Carpita Visa account. The same TD supervisor informed her that the balance was $595,000. MsFriedrichs said "wow" and immediately informed the company's accountant, Mr.Grilo. He told her to call the bank again to verify the balance and ensure that no unusual postings had occurred. MsFriedrichs made a second call to the TD supervisor who checked the records and confirmed that there was nothing unusual in them. Shortly thereafter, a Carpita representative attended at the Toronto TD branch and presented for certification a cheque payable to Factory Carpet for $585,000. The TD supervisor authorized the certification. On the same day, Carpita deposited the cheque to the credit of its current account at B of M.

15 No one at TD contacted Carpita to advise it that the $585,000 cheque had been certified in error. No notice was given to B of M of any problem with respect to the cheque, even though it was Carpita's pattern to transfer its funds quite regularly to B of M. The TD supervisor does not recall telling anyone else of the error. Thus, when the cheque was received by the TD Toronto branch on Monday, June 25, it was honoured. B of M now had the $585,000 in its accounts.

16 I turn now to the events of the second week, the week of June 25. It will be recalled that a meeting of representatives of Carpita and B of M was scheduled for Monday, June 25. Twice during the previous week Carpita had appeared to exceed

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its $10,000,000 line of credit. On both occasions Mr.Stratton of B of M called Carpita to insist on coverage of the excess. Carpita complied.

17 On the morning of June 25, B of M saw that the loan balance in Carpita's account had risen to $10,471,936. Mr.S tratton called Mr. Grilo at Carpita on Monday morning and asked that the company have a solution to be discussed at the meeting scheduled for that afternoon.

18 At approximately 2:00p.m. on Monday, June 25, several representatives of Carpita and B of M met. The Carpita people informed B of M of Carpita's huge losses in the previous fiscal year and that there was no longer any equity in the company. No solution to the line of credit excess problem was achieved, presumably because it paled almost into insignificance against the $20,000,000 loss being discussed.

19 On Tuesday, June 26 another meeting was held. Mr. Stratton advised the Carpita representatives that unless the excess beyond the line of credit was covered, B of M would return all cheques drawn on Carpita's account received on June 22. This would include two cheques payable to Comcheq Corporation for payroll purposes. At about 2:30 p.m., Carpita instructed B of M to stop payment of all cheques issued by Carpita, commencing with those received on June 22. However, Carpita's instruction exempted the two cheques payable to Comcheq to reimburse it for payroll amounts totalling $515,785.68 which had previously been remitted to Carpita employees.

20 Following the stop payment order given on June 26, B of M returned cheques totalling $573,299.15 before the final closing of accounts for the previous day. This was in accordance with standard banking practice. However, B of M did not return the payroll cheques to Comcheq. The result was that at the close of business on June 25, Carpita had borrowed $9,968,315 on its $10,000,000 line of credit.

21 Also at the meeting on June 26, the Carpita and B of M representatives discussed the ongoing management of Carpita. The Carpita directors were prepared to stay on if B of M would indemnify them against personal liability for the payment of employee wages and other benefits after June 25. In other words, the decision not to dishonour the two previous payroll cheques covered liability to June 25. Now attention was being focussed on possible future liability for employee claims.

22 B of M wanted the directors to stay in office, at least until it decided to commence to realize on its security. But B of M was not willing to permit the line of credit to exceed $10,000,000. The directors were prepared to continue to serve, provided they were immunized from personal liability for employee claims. When the representatives met on June 26 this combination of positions presented an intractable problem because Carpita was so close to the limit of its line of credit.

23 By the next day the problem was solved by the incredible irony of the accidental $450,000 finding its way into B of M's records. Overnight Carpita went from being almost at the ceiling of its line of credit to having about $600,000 of breathing space. Neither Carpita nor B of M knew that this change was the result of TD's errors. In any case, on Wednesday, June 27, B of M certified a Carpita cheque payable to the law firm Fogler Rubinoff in trust in the amount of $586,835 which was deposited into the Fogler Rubinoff trust fund for the benefit of Carpita employees. The amount of the cheque equalled the difference between Carpita's outstanding loans balance on June 26 and its line of credit limit of $10,000,000. Without the certification and delivery of that cheque, the Carpita directors would have resigned.

24 On Friday, June 29, Carpita made an assignment in bankruptcy with the knowledge of B of M. Still no one at B of M or Carpita had any inkling of the $450,000 windfall. But the TD comedy of errors was about to catch up to the Carpita tragedy. On this same day, the debit memo sent from the Quebec TD branch arrived at the College and Spadina branch. It had been delayed in transit for a week because it had originally been misdirected to a non-existent Toronto branch. The debit memo resulted in an overdraft in excess of $400,000 in Carpita's TD account. Even though the account had no overdraft privilege, nobody at TD reacted to the situation on June 29.

25 The long holiday weekend ensued. Finally, in the late afternoon of July 3, TD notified B of M of the mistake that had been made and requested a return of the amount of the original certified cheque. TD didn't get around to advising Carpita of the mistake until July 5. Also on July 5, TD made a written demand on Fogler Rubinoff for reimbursement out of the trust fund.

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26 By agreement of counsel, the balance in the Fogler Rubinoff trust account, namely $585,887.61, has been paid into a special accountof Ernst and Young, Carpita's trustee in bankruptcy, to abide the outcome of this litigation. In the intervening years TD has recovered about $25,000 from Carpita through other avenues. Hence its claim now is for the recovery of $425,003.07 from this special account.

B. Legal Issues

27 TD's Statement of Claim was framed in terms of allegations of breach of trust, negligence, conversion and unjust enrichment against all the defendants. Most of these allegations have been abandoned. At trial the argument proceeded on only two bases, which I would frame in the form of questions:

(1) Can TD recover $425,003.07 from B of M because the latter has been unjustly enriched?

(2) In the alternative, can TD recover $425,003.07 from the former directors of Carpita because they have been unjustly enriched?

28 I will address these questions in turn.

(1) Unjust Enrichment — Bank of Montreal

29 TD claims that B of M has been unjustly enriched by mistakenly receiving and improperly retaining $425,003.07 of TD's money. TD says that at the close of business on June26 Carpita had available to it on its line of credit about $585,000. However, says TD, just over $450,000 of this amount was there by mistake. TD's submission is that this amount was impressed with a trust in its favour. The money has not disappeared; it is in a trust account abiding the result of this trial. It is, therefore, available to be returned to TD and, says TD, it would be against commercial conscience if it were not returned.

30 TD grounds its argument in a passage from the judgment of GoffJ. (the highly regarded English academic in the domain of equity before his appointment to the bench) in *Barclays Bank Ltd. v. W.J. Simms, Son & Cooke (Southern) Ltd.*, [1979] 3 All E.R. 522 (Q.B.). After an extensive review of centuries of jurisprudence relating to the recovery of money obtained by mistake of fact, GoffJ. said, at p. 535:

> From this formidable line of authority certain simple principles can, in my judgment, be deduced.
>
> 1. If a person pays money to another under a mistake of fact which causes him to make the payment, he is prima facie entitled to recover it as money paid under a mistake of fact.

31 The applicability of this principle in Ontario, and its legal basis, have recently been articulated by OsborneJ. in *Morgan Guaranty Trust Co. of New York v. Outerbridge* (1990), 72 O.R. (2d) 161 (H.C.), at p. 188:

> The obligation to return money paid by mistake (of fact) is rooted in the law of restitution, responsive as it is to what the law views as unjust enrichment. Notions of an implied contract to repay have been discarded. The claim is equitable.
>
> As a statement of general principle I refer to Goff and Jones' text *The Law of Restitution*, 3rd ed., at pp. 12-13 where the following appears:
>
> > Most mature systems of law have found it necessary to provide, outside the fields of contract and civil wrongs, for the restoration of benefits on grounds of unjust enrichment. There are many circumstances in which a defendant may find himself in possession of a benefit which, in justice, he should restore to the plaintiff. Obvious examples are where the plaintiff has himself conferred the benefit on the defendant through mistake or compulsion. To allow the defendant to retain such a benefit would result in his being unjustly enriched at the plaintiff's expense and this, subject to certain defined limits, the law will not allow.

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32 TD supplements its argument anchored in unjust enrichment by asserting that the money it mistakenly transferred to B of M is still recoverable. Because $585,000 has been placed in a trust account and not spent, there is more than enough money available, says TD, for its recovery of just over $425,000. TD points to an old Privy Council decision, *Colonial Bank v. Exchange Bank of Yarmouth* (1885), 11 App. Cas. 84, and especially to this passage at p. 89:

> Now it was not true that the sum had been used and could not be recalled. The defendants had only got to run a pen through some private entries in their own books and the matter then would have stood in precisely the same position as it stood in before the mistake was made.

A century later the same result could and should prevail, says TD, with the punching of a key (one hopes that the B of M employee would do this more successfully than the TD teller in LaSalle, Quebec!) replacing the stroke of a pen.

33 I do not agree with TD's claim and analysis. In my view, there are at least three compelling reasons, each sufficient in its own right, for denying TD's claim grounded in unjust enrichment.

(a) Legal effect of certifying a cheque

34 The first reason is the legal effect of cashing a certified cheque. In a decision released about a month ago, *A.E. LePage Real Estate Services Ltd. v. Rattray Publications Ltd.*, [1994] O.J. No. 2950 [reported at 120 D.L.R. (4th) 499], the Court of Appeal stated clearly that a certified cheque is irrevocable. The principal issue in this case was whether there was a distinction between certification obtained by the payer and certification obtained by the payee. Finlayson J.A., in approving of the decision made at trial by MontgomeryJ., (1991), 5 O.R. (3d) 216 (Gen. Div.), was not prepared to make such a distinction. His reasons are, I believe, animated by a desire to enunciate general principles of value to the commercial community. One consequenceis non-acceptance of the payer-payee distinction. He said, at p. 6 [p. 504, D.L.R.]:

> ... certification creates a status in the cheque which is the equivalent of acceptance regardless of who is responsible for the certification.
>
> The great advantage of treating certification as acceptance, whether at the instance of the payee or the drawer, is that it brings a certified cheque squarely within the framework of the *Bills of Exchange Act* and *codifies the consequences of certification.*[1]

(My emphasis.) [Footnote added by MacPherson J.]

35 In reaching this conclusion, Finlayson J.A. relied on a law review article by Professor Benjamin Geva, Canada's foremost academic authority on the law of banking and negotiable instruments. The article is "Irrevocability of Bank Drafts, Certified Cheques and Money Orders" (1986), 65 Can. Bar Rev. 107. Finlayson J.A. said this about it in his judgment in *LePage*, at pp. 6-7 [p. 505, D.L.R.]:

> Professor Geva argues persuasively that acceptance is the proper theoretical basis underlying certification. After undertaking a detailed examination of certified cheques in his article, *supra*, he identifies three premises for this theory in his examination at pp. 110-11:
>
> > First of all, the irrevocability of the banker's obligation facilitates the acceptability of banker's instruments as cash substitutes. Secondly, prevailing mercantile perceptions as to irrevocability attached to any type of instrument should be reflected in existing law. Thirdly, it is preferable to explain the irrevocability of the banker's obligation in the framework of the law of negotiable instruments rather than under general principles of law. Indeed, fitting irrevocability into a known category of statutory engagement under the Act is bound to produce a greater certainty than the application of broad and often open-ended general principles.

36 I make one final point about *LePage*. Not only is FinlaysonJ.A.'s judgment for the court written very much at the level of broad legal and commercial principles; in addition, the fact situation in *LePage* is very similar to the situation in this case, namely a mistakenly certified cheque cashed by a second financial institution. My conclusion, therefore, is that the reasoning

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and result in *LePage* govern this case. TD cannot resile from the certified cheque that it gave to B of M.

(b) The 'juristic reason' component of unjust enrichment

37 My second reason for not agreeing with TD's argument is that I do not believe that the elements of an unjust enrichment are made out in this case. These elements are now well-known in the Canadian legal context because of a series of major decisions by the Supreme Court of Canada: see, for example, *Rathwell v. Rathwell*, [1978] 2 S.C.R. 436; *Becker v. Pettkus*, [1980] 2 S.C.R. 834; *Sorochan v. Sorochan*, [1986] 2 S.C.R. 38; and *Peter v. Beblow*, [1993] 1 S.C.R. 980. In *Pettkus*, DicksonJ. put it thus, at p. 848:

> ... 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.

38 B of M concedes that the first two of these elements are met in this case — TD has been deprived of money and B of M has received it.

39 However, in my view, the third element for unjust enrichment is missing. There is a juristic reason for B of M receiving and retaining the funds. When B of M cashed the certified cheque for about $585,000 it had granted a line of credit of $10,000,000 to Carpita and Carpita in fact owed it almost that amount. In other words, Carpita owed a very substantial debt to B of M. The existence of this debt, and B of M's instant use of the cheque to reduce the debt, is a juristic reason for B of M's retention of the money. In *Barclays Bank*, supra, Goff J., after setting out the general principle that a person who pays money under a mistake of fact should be able to recover it, articulated three exceptions to the rule. The second one he expressed as follows, at p. 535:

> His claim may however fail if ... (b) the payment is made for good consideration, *in particular if the money is paid to discharge, and does discharge, a debt owed to the payee ... by the payer ...*

(My emphasis.) See also: *Royal Bank v. Harowitz* (1994), 17 O.R. (3d) 671 (Gen. Div.), and *McDiarmid Lumber Ltd. v. Canadian Imperial Bank of Commerce* (1992), 94 D.L.R. (4th) 227 (B.C. S.C.); contra, in obiter, *Morgan Guaranty Trust*, supra.

40 I make one other point about TD's unjust enrichment argument. Unjust enrichment is an equitable remedy. The party claiming it must establish that its conduct leading to its deprivation was untainted. In a commercial context I like the formulation of Lambert J.A. of the British Columbia Court of Appeal in *Atlas Cabinets & Furniture Ltd. v. National Trust Co.* (1990), 68 D.L.R. (4th) 161, at p. 172:

> In my opinion the concept of the injustice of the enrichment as being against sound commercial conscience must continue to guide the application of the three tests in *Pettkus v. Becker* when they are applied to a commercial relationship.

41 In the present case, it would be against commercial conscience to allow TD to recover on unjust enrichment grounds. While B of M and Carpita were struggling to try to keep Factory Carpet afloat and pay its employees, TD employees in two provinces displayed remarkable lassitude and ineptitude as they tried to correct the original mistake. The litany of errors and omissions is set out earlier in these reasons. I agree with Mr. Tait, B of M's counsel, who described TD's conduct in an apt and colourful sentence "In short, the TD system permitted an error to be made at the speed of light which could only be corrected by the equivalent of the Pony Express."

(c) The reliance exception to recovery for mistake of fact

42 In *Barclays Bank*, supra, GoffJ. enunciated three exceptions to the general principle that a person has a prima facie right to recover money paid under a mistake of fact. He expressed the third exception in this fashion, at p. 535:

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His claim may however fail if ... (c) the payee has changed his position in good faith, or is deemed in law to have done so.

See also: *Storthoaks (Rural Municipality) v. Mobil Oil Canada Ltd.*, [1976] 2 S.C.R. 147, and *Morgan Guaranty*, supra.

43 In my view, B of M is entitled to rely on this exception in this case. In the week before it became aware of the seriousness of Carpita's situation, B of M, on two occasions, immediately notified Carpita when Carpita went over its line of credit. Adherence to the line of credit was important to B of M. It did not wink at excesses, even small ones or even for a day. The next week saw Carpita tumble into financial ruin. During that week B of M and the Carpita directors made fundamental decisions about the management of Carpita's bank account and its indebtedness to B of M in reliance on the day-by-day state of the bank accounts, including the proceeds of the mistaken cheque. Without the mistaken funds, B of M might have made different decisions during the last week of June 1990. It might not have permitted a trust fund to be created for the benefit of employees or it might have attempted to realize sooner, and with better results, on its security. We will never know for certain because a different course of conduct was pursued in reliance on the known state of Carpita's accounts. What we do know is that B of M was vigilant about policing the excess in Carpita's line of credit, and that without the mistaken funds, the policing in the last week of June would almost certainly have led B of M to make decisions different from those they in fact made at the time.

(2) Unjust Enrichment — Former Directors of Carpita

44 If TD is unsuccessful in what it candidly admits is its main claim, the one against B of M, then it advances an alternative claim against the former directors of Carpita. TD sets out succinctly this claim at para. 39 of its factum:

> 39. If for any reason, the Toronto-Dominion Bank is not entitled to the relief claimed against the Bank of Montreal, then clearly Carpita and its Directors will have been unjustly enriched. The Directors will have benefited in that they have been relieved of the obligation to make substantial wage payments.

45 The last sentence in para. 39 is a reference to s. 131 of the Ontario *Business Corporations Act*, R.S.O. 1990, c. B.16, which provides inter alia:

> 131. — (1) [*Directors' liability to employees for wages*] The directors of a corporation are jointly and severally liable to the employees of the corporation for all debts not exceeding six months' wages that become payable while they are directors for services performed for the corporation and for the vacation pay accrued while they are directors for not more than twelve months under the *Employment Standards Act*, and the regulations thereunder, or under any collective agreement made by the corporation.
>
> (2) [*Limitation*] A director is liable under subsection (1) only if,
>
> (*a*) the director is sued while he or she is a director or within six months after ceasing to be a director; and
>
> (*b*) the action against the director is commenced within six months after the debts became payable ...

46 TD's argument is that the trust fund for employee salaries was established only because of the money that was deposited by mistake into B of M's account. Without the trust fund, TD says, there might not have been sufficient money to pay the employees which might have provoked them to sue the directors under this provision. By avoiding this potential liability the directors have received a benefit — unjustly, asserts TD.

47 I do not agree with this argument. In a recent case, *Peel (Regional Municipality) v. Ontario*, (sub nom. *Peel (Regional Municipality) v. Canada)* [1992] 3 S.C.R. 762, McLachlin J., for a unanimouscourt, discussed in some detail the concept of benefit in the context of juristic reason, the third component of the test for unjust enrichment. She reviewed many cases and the two leading texts, Goff and Jones, *The Law of Restitution*, 3rd ed. (1986), and Maddaugh and McCamus, *The Law of Restitution* (1990), and concluded that a claim for unjust enrichment can succeed only if, inter alia, the benefit received by the

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person enriched is "incontrovertible" or "demonstrable" or "unquestionable" (p. 797).

48 None of these words comes anywhere close to describing the benefit that TD alleges the directors of Carpita received in this case. No employee ever made a claim under s. 131 of the Ontario *Business Corporations Act*. Nor did any of the directors receive one penny of the money in the trust fund. Accordingly, the directors received no direct benefit. As for indirect benefit, it was remote and speculative in 1990 and it disappeared entirely when no one initiated the s. 131 process. In short, the situation in this case is, in my view, completely divorced from any realistic notion of "incontrovertible" benefit.

49 I note as well that the directors had no idea throughout the difficult days of late June 1990 that Carpita had received a windfall through TD's mistake. Their receipt and use of the windfall was completely innocent. Moreover, they served faithfully at a difficult time. Unlike one director, the defendant directors did not resign when the financial storm clouds blew in; rather they stayed, took important steps to protect their employees, and generally tried to manage the company in turbulent waters. During the same days, TD was slow and inept in its attempts to recover the money. In other words, the equities are with the directors, not TD. Since unjust enrichment is an equitable doctrine, it follows that TD should not succeed in its attempt to invoke it.

Conclusion and Disposition

50 In *LePage*, supra, Finlayson J.A. said, at p. 7 [p. 505, 120 D.L.R. (4th)]:

> The problem on appeal, is not that the bank does not have a remedy, but that its customer, the party against whom it has the remedy, is insolvent.

This passage is, in my view, a perfect description of TD's problem in this case.

51 The action is dismissed against all defendants. Costs may be spoken to, if necessary.

Action dismissed.

Footnotes

1 The provisions of the *Bills of Exchange Act*, R.S.C. 1985, c. B-4, to which Finlayson J.A. referred are:

2. ...
"acceptance" means an acceptance completed by delivery or notification;

. . . . .

38. Every contract on a bill, whether it is the drawer's, the acceptor's or an endorser's, is incomplete and revocable, until delivery of the instrument in order to give effect thereto, but where an acceptance is written on a bill and the drawee gives notice to, or according to the directions of, the person entitled to the bill that he has accepted it, the acceptance then becomes complete and irrevocable.

127. The acceptor of a bill by accepting it engages that he will pay it according to the tenor of his acceptance.

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TAB 4

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

1994 CarswellOnt 836
Ontario General Division

Royal Bank v. Harowitz

1994 CarswellOnt 836, [1994] O.J. No. 619, 17 O.R. (3d) 671, 46 A.C.W.S. (3d) 1194

Royal Bank of Canada Plaintiff v. Sharon Harowitz Defendant

Killeen J.

Judgment: March 15, 1994
Docket: Doc. 10611

Counsel: *M.J. Neirinck*, for the plaintiff, Royal Bank of Canada.
S.M. Tick and *K. Malhotra*, for the defendant, Sharon Harowitz.

Subject: Corporate and Commercial; Restitution; Insolvency

Related Abridgment Classifications

Bills of exchange and negotiable instruments
III Cheques
III.11 Forged or unauthorized cheques
III.11.e Cheque obtained by fraud or theft

Restitution and unjust enrichment
I General principles
I.2 Requirements for unjust enrichment
I.2.c No juristic reason for enrichment

Headnote

Banking and Banks --- Cheques — Forged or unauthorized cheques — Cheque obtained by fraud or theft

Bank customer fraudulently obtaining credit with bank — Cheque written on account — Bank claiming unjust enrichment to payee of cheque.

Defendant lent M. $250,000 with a promissory note as security. When defendant asked for the loan to be repaid, M. forwarded to her a cheque drawn on his personal account with plaintiff bank. Unknown to both defendant and bank, M. had fraudulently obtained credit with bank by using forged documents and security instruments. Another bank discovered that it also had been defrauded and obtained an order freezing M.'s assets. M. became bankrupt. Bank brought an action against defendant for a declaration that defendant held $250,000 as a constructive trustee for bank. Held, the action was dismissed. Even assuming that the first two elements of the test for unjust enrichment had been met, the third element, the absence of a juristic reason for defendant's enrichment, was not proven. The juristic reason lay in the loan between defendant and M. The juristic reason did not have to be connected to party which made the claim of unjust enrichment.

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Restitution

Bank customer of bank fraudulently obtaining credit -- Cheque written on account — Bank claiming unjust enrichment to payee of cheque.

Defendant lent M. $250,000 with a promissory note as security. When defendant asked for the loan to be repaid, M. forwarded to her a cheque drawn on his personal account with plaintiff bank. Unknown to both defendant and bank, M. had fraudulently obtained credit with bank by using forged documents and security instruments. Another bank discovered that it also had been defrauded and obtained an order freezing M.'s assets. M. became bankrupt. Bank brought an action against defendant for a declaration that defendant held $250,000 as a constructive trustee for bank. Held, the action was dismissed. Even assuming that the first two elements of the test for unjust enrichment had been met, the third element, the absence of a juristic reason for defendant's enrichment, was not proven. The juristic reason lay in the loan between defendant and M. The juristic reason did not have to be connected to party which made the claim of unjust enrichment.

***Killeen. J.*:**

1 This is another trial of an issue in the bankruptcy proceedings of Julius Melnitzer. In this case, the plaintiff, Royal Bank, seeks a declaration against the defendant, Sharon Harowitz, that she holds the sum of $250,000., paid to her by Melnitzer shortly before his bankruptcy, as constructive trustee for the plaintiff.

The Background Facts

2 I propose, first, to deal with the business relationship of Mrs. Harowitz with Melnitzer which led to the $250,000. payment to her and then I will deal with the business relationship between the plaintiff and Melnitzer out of which the plaintiff claims its relief under the equitable principles of unjust enrichment and constructive trust.

3 Mrs. Harowitz, who lives in Vancouver, British Columbia, is the sister of one Allan Richman who, in turn, was a long-time friend and business associate of Melnitzer in London, Ontario.

4 In 1986, Mrs. Harowitz's husband died suddenly, leaving her, amongst other assets, the $250,000. proceeds of a life insurance policy. She wished to invest this sum in some sort of investment which would provide her with a good rate of return and was put in touch with Melnitzer through her brother. The result was that she loaned the money to Melnitzer under a promissory note.

5 On June 6, 1986, she issued a cheque in favour of Melnitzer and this cheque cleared her account on June 9. The promissory note (ex. 1, tab 60) was signed by Melnitzer on June 6; it includes a guarantee executed by Melfan Investments Ltd., a Melnitzer family investment company of which Melnitzer was an apparent officer and principal. The terms of the note were as follows: it called for payments of interest monthly, calculated at the higher of fourteen and one-half per cent or the prime rate of the Chase Manhatten Bank, plus five and one-half per cent, both before and after maturity; the note's maturity date was June 1, 1987.

6 Mrs. Harowitz set up a special account into which the interest payments were to be paid and, over the years, Melnitzer usually provided her with an annual set of post-dated cheques to cover the interest payments.

7 This investment-loan arrangement went on uneventfully until early 1991 when Mrs. Harowitz decided to call in the loan, as she had a right to do, because she wished to use the principal for other purposes in British Columbia.

8 On March 22, she wrote to Melnitzer and suggested that the money be paid back in June because she held an annual series of post-dated cheques for interest from him which ran out in that month. Mr. Melnitzer responded with a letter to Mrs. Harowitz's Vancouver business adviser on April 12 indicating that he would forward a cheque for the $250,000. loan amount on July 1 and also stating that appropriate interest adjustments would be made. Then, in early July, he forwarded a personal

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cheque to cover the $250,000. This cheque, dated July 2, 1991, which was drawn on Melnitzer's personal account with the Royal Bank in London, was debited to this account on July 10.

9 It should be added, here, that Keenan J., on August 3, issued an *ex parte* freezing order against Melnitzer's assets on the application of the National Bank. This order appointed Coopers & Lybrand as receiver-manager of Melnitzer's assets. Then, on September 3, a petition to put Melnitzer in bankruptcy was filed in the Bankruptcy Court. At a hearing on September 26 a Receiving Order in Bankruptcy was granted by me and Peat Marwick Thorne Inc. was appointed Trustee of Melnitzer's estate.

10 There was not a whisper of a suggestion in the evidence that Mrs. Harowitz had any inkling in 1991 or earlier that Melnitzer was a fraudster or that she had called in the investment because she had some suspicions and concerns about his true financial condition in 1991. In other words, from her perspective in 1991, she made a good-faith business decision to ask for the return of her money and Melnitzer complied as he was obligated to do under his agreement with her.

11 Mr. Melnitzer's business relationship with the Royal Bank was, needless to say, more complex than that which he had with Mrs. Harowitz and calls for fuller treatment.

12 The Royal Bank relationship was explained by its sole witness, Colin Liptrot, as amplified by the documentary evidence included in exs. 1-2. Mr. Liptrot had worked for the Royal Bank since 1970 in a variety of responsible posts and positions. In 1988 he came to London and set up a private banking centre for the bank. He remained in London as the manager of this banking centre until 1992 when he was transferred to another job as manager of an export-import office of the bank in British Columbia.

13 Mr. Liptrot testified that he first heard of Melnitzer in the fall of 1988. He was made aware of the fact that Melnitzer was a highly successful lawyer and was, as well, prominent in the London business community. It would seem that Liptrot met Melnitzer in about mid 1989 and that they had discussions about the possibility of Melnitzer becoming both a customer of and borrower from the bank. They met on June 7, 1989, and, on that date, Melnitzer signed a "Personal Statement of Affairs" document as a prelude to negotiating a loan from the bank. This document has 2 pages and has multiple boxes for the inclusion of detailed information on the assets and liabilities as well as the income and expenses of the signatory. In this instance, the form contains only two bits of information, namely, that Melnitzer had a residence worth $550,000. and a $200,000. liability to the Bank of Montreal.

14 Two days later, on June 9, another copy of this statement was filled out by Liptrot and, on this occasion, the form is fully filled out with the information called for in the boxes. As I understood Liptrot's evidence, he himself wrote in the required information based on notes of their meeting on June 7 but Melnitzer, for some unexplained reason, did not sign the second statement at the bottom; rather, Liptrot wrote Melnitzer's name at the bottom.

15 In any event, this statement contains some startling figures. It shows Melnitzer's assets at $18,965,000. and his liabilities at $1,500,000., with a net annual cash flow of $221,760. It is interesting to note the array of assets listed: 770,000 shares of Prenor Financial worth $5,390,000.; silver certificates apparently held by the family company, Melfan Investments, worth $3,500.000.; a 45% interest in Melfan Investments itself worth $4,205,700; real estate worth $3,050,000.; an art collection worth $1,000,000.; a 50% interest in an investment company, Grand Canyon, worth $600,000.; an interest in the Cohen, Melnitzer law firm worth $500,000. and so on.

16 Mr. Liptrot acknowledged, when pressed, that little was done by him or others in the Royal Bank to check the value and authenticity of these assets or the corresponding liabilities and encumbrances related to them. Later investigations in the bankruptcy showed that many of these listed assets were spurious or grossly inflated and that, in many instances, the encumbrances were seriously understated. Mr. Liptrot's investigations seem to have been perfunctory at best. He identified a financial statement for Melfan Investments for the year ending April 30, 1988, (ex.1, tab 2) which was purportedly prepared by the London accounting firm of Marcus & Associates. This statement showed that Melfan had net assets of $10,630,592. in 1988, including term deposits held by the Bank of Montreal worth $5,610,110. and "commodities" investments totalling $3,331,541.

17 Mr. Liptrot appears to have accepted this statement on blind faith and nothing more. He made no independent check

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with the Marcus firm to ascertain its authenticity and he made no checks with the Melfan company to confirm Melnitzer's alleged 45% ownership interest in it. If he had done so he would have found that the Marcus statement was a forgery, that Melnitzer had no significant interest in this company and, finally, that the net worth of the company was around $250,000.

18 It would seem that the only check he made on the many real estate holdings was a casual check on Melnitzer's Tallwood Road property. There is nothing in Liptrot's evidence to suggest that the bank did a careful and reasonable check of Melnitzer's real estate by requiring him to produce, property by property, registered title documents and back-up statements from encumbrancers to establish values and equity interests accurately. These would have shown that Melnitzer's equity was dramatically less than the almost $2,000,000. figure he claimed.

19 Similarly, there were no independent checks on Melnitzer's claims that he held Prenor Financial shares worth $5,390,000. or silver certificates worth $3.5 million. During Liptrot's evidence, he was referred to an internal bank document entitled "Lending To The Upscale (or Financially Active) Market" prepared in mid-1990. While this guideline document was not in existence when Melnitzer's first dealings with the bank were established in 1989, Liptrot conceded that this document was a compendium of "past practice" within the bank in its dealings with so-called "upscale" clients and that Melnitzer's loans fell within the parameters of that upscale market. This document identifies several criteria and red flags for the bank staff in their dealings with potential upscale clients. Several of these criteria are worth mentioning:

> (1) *at p.4*:
>
> A personal financial statement should not be accepted at face value....
>
> . . . . .
>
> an Applicant's income/cash flow level should be confirmed....
>
> . . . . .
>
> A tax return, with all the schedules is becoming a commonly accepted method of assembling components of the income/cash flow.
>
> (2) *at p.8*:
>
> Credit analysis should closely identify specific primary and secondary sources of payment, as well as eligible collateral....
>
> . . . . .
>
> There should be a direct relationship between an upscale borrower's cash flow and financial statement.

20 Mr. Liptrot acknowledged that with a new and upscale customer like Melnitzer, it was incumbent on a credit officer to satisfy himself through "due diligence" checks that the customer should be granted the credit sought. Yet, as noted, the initial checks here seem barren and perfunctory.

21 In his original negotiations with Liptrot, extending over the summer of 1989, Melnitzer apparently sought a credit facility of over $4 million but the loan was finally fixed at the $3 million level, as reflected in Liptrot's offer letter to Melnitzer of August 9 (ex.1, tab 6). This letter was countersigned by Melnitzer on September 21.

22 The Liptrot commitment letter contains a number of conditions to be satisfied by Melnitzer: (1) the hypothecation of $1.5 million in cash in an interest-bearing account; (2) a guarantee of the loan by Melfan Investments together with the hypothecation of all issued Melfan shares and collateral undertakings of the Melfan company; (3) the other usual commitments and covenants by Melnitzer himself.

23 Mr. Liptrot described the Melfan guarantee and undertakings as the "linchpin" for the grant of the credit. There was an apparent substantial cash flow in this company and the hypothecation of its shares gave a large comfort zone to the bank.

24 Overall, the commitment was expected to be a profitable one for the bank. The monthly interest payments would approach $38,000. and, while the term of the loan was 3 years, it would be renewable in one year from draw-down. By March of 1990 Melnitzer was pressing Liptrot for an expansion of the loan by $1 million. Liptrot sent an approved internal credit application to the regional credit office in Burlington on March 13 (ex. 1, tab 21). This document and a revised

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personal financial statement for Melnitzer (ex.1, tab 20), also prepared and signed by Liptrot on behalf of Melnitzer, show some sharp upward changes in Melnitzer's income and assets. Now, Melnitzer's gross annual income has risen from $475,000. to a startling figure of $4,750,800. This change is largely attributed to “dividend and interest” income which has increased from $110,000 to $4 million: see ex.1, tab 21, p.4. Also, one finds that his assets increased from $18,965,000. to $66,925,000. This increase was largely accounted for by Melnitzer's disclosure that he had a $36 million U.S. cash deposit with the Hongkong-Shanghai Banking Corporation in the Far East.

25 This request (and its attendant financial statement) led P.G. Lonergan, Liptrot's senior manager in Burlington, to raise some alarm bells in a letter to Liptrot of March 23. Mr. Lonergan had serious concerns about Melnitzer's “unexplained 45 mm increase in net worth in less than one year”. He found it hard to understand why Melnitzer was prepared “to go to so much trouble to negotiate an additional $1 mm from ourselves”, given his substantial net worth and long, ongoing relationship with the Canadian Imperial Bank of Commerce.

26 Mr. Liptrot responded to Lonergan's concerns in a memorandum which simply restates with some embellishment the new assets and income picture but it is clear that, once again, he did little to investigate further into the merits of Melnitzer's financial position.

27 During this same period, Melnitzer must have given Liptrot another document purportedly issued by his accountants, Marcus & Associates. This was a letter, dated March 8, 1990, written by Mr. Kohn of the Marcus firm to Melnitzer. In it, Kohn reviews all of Melnitzer's assets and liabilities, including the Hong Kong deposit holding. It seems clear that Liptrot swallowed this document in a quick gulp as he did two earlier Marcus missives provided by Melnitzer (ex. 1, tabs 2, 18 and 19). All of these supposedly confirmatory documents were, of course, forged by Melnitzer. In this period Liptrot made no concerted effort to confirm the accuracy or authenticity of the Marcus letter either with Mr. Kohn (its alleged author) or by establishing direct contact with first-hand sources at the companies or institutions where reliable information was undoubtedly available. There is not even evidence from Liptrot that he ever obtained copies of Melnitzer's income tax returns for, say, the 1988 and 1989 years, something which the bank's upscale - market discussion paper and accepted internal bank practice considered to be essential to due diligence with upscale customers.

28 Following upon Lonergan's negative assessment of the March 13 request for an increase of $1 million in the credit facility further negotiations continued which, in fact, led to the conversion of the original loan agreement to a revolving demand loan as reflected in an agreement signed on April 23 (ex.1, tab 24). This agreement shows that, as of April 20, Melnitzer was now indebted to the bank for $2,700,296.

29 The relationship of Melnitzer and the bank for the balance of 1990 was relatively uneventful. Mr. Liptrot's memorandum of March 27 to his senior manager shows, however, that Liptrot is trying to develop “a wider relationship” with Melnitzer embracing such matters as (1) the business of the Cohen, Melnitzer law firm and the Grand Canyon company, (2) an opportunity to bid on Melnitzer's U.S. dollar deposits in Hong Kong along with the 6.5 million in deposits held by Melfan Investments and, finally, using Melnitzer as a “bridge” to more business with the Jewish Community in London.

30 In the fall of 1990, it is obvious that Melnitzer has continued to out-manoeuvre and even dazzle Liptrot with his chess-plays as to his wealth and credit-worthiness.

31 By late September Liptrot has prepared another personal financial statement and unquestioningly accepts Melnitzer's information. Not only that, once again Liptrot signs this statement for Melnitzer and implies that he has an original of it signed by Melnitzer. In fact, he does not. At this point, Liptrot is putting Melnitzer's net worth at the huge figure of $68,605,000 (ex.1, tab 30).

32 Mr. Liptrot then submitted, on November 22, another application for an increased credit line for Melnitzer up to $6,020,000. to the regional office. Mr. Liptrot was again recommending approval and noted that Melnitzer had promised the Royal Bank some new business in 1991. Melnitzer's actual indebtedness to the bank in November was around $1,773,000. This application was turned down by the regional office, presumably because the bank was seeking additional security on $3,000,000. in term deposits then allegedly held by Scotia McLeod on behalf of Melnitzer and Melfan: see ex.1, tab 32-33. It may be added, parenthetically, that the bank and Liptrot appear to have been one very short step here from discovering one significant aspect of Melnitzer's fraudulent misrepresentations but failed to take it.

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33 Liptrot met with Melnitzer in Toronto on January 31, 1991, and, not surprisingly, Melnitzer, like Oliver Twist, was still asking for more. This discussion eventually led to a new credit application on April 18, 1991, in which Melnitzer was asking that his credit line be increased by $5 million to $8,020,000. (ex.1, tab 41). His actual indebtedness at this point was $2,260,000. The credit application explains that Melnitzer's purpose in increasing the credit line is to buy a larger interest in Champion Chemtech, a private company in which he had already acquired a 25% interest. He was proposing fresh substituted collateral security in the form of $12 million worth of shares in several public-traded companies, namely, Bell Canada, Canadian Pacific, IBM, Imperial Oil and McDonald Corporation.

34 This application was approved in Burlington on April 25 subject to Melnitzer's production of financial statements for Melfan Investments and the Cohen, Melnitzer law firm along with Melnitzer's 1990 tax return. Mr. Liptrot only provided the regional office with the Melfan and Cohen, Melnitzer statements with a letter of June 26 and, in the same letter, he promised Melnitzer's tax return shortly. He also indicated that Melnitzer was anxious to complete this new agreement by July 4 when Melnitzer wished to draw down the additional borrowing of $5 million.

35 As things turned out, the revised credit facility was not formally agreed to until 7 A.M. on the morning of July 31 when Liptrot went to Melnitzer's office and had Melnitzer counter-sign a detailed commitment letter submitted by Liptrot (ex.1, tabs 49-50). At this meeting, Melnitzer turned over to Liptrot the share certificates for the pledged shares and signed collateral security documents for them.

36 The old loan balance then stood at $2,808,590.93 but, by agreement, the Bank applied the old $1,509,430.42 savings account collateral to this balance later on July 31, reducing the old debt to $1,299,160.51. This latter sum was, of course, subsumed in the new credit facility. Melnitzer also drew down the sum of $1,185,000. on July 31, leaving him owing the bank $2,484,160.51 by the close of business on July 31.

37 Mr. Liptrot sent the $12 million in share certificates to Dominion Securities by courier later on July 31 for verification. Because of the intervening holiday weekend, no answer was received until the following Tuesday. By then, the bad news was superfluous because, in the intervening few days, the National Bank had discovered that similar share certificates were forged and had moved for a freezing order on Melnitzer's assets before Keenan J. on Saturday, August 3.

The Legal Issue and its Resolution

38 Mr. Neirinck's central position for the Royal Bank is as follows. He submits that when Mrs. Harowitz cashed Melnitzer's cheque for $250,000. on July 10, 1991, she received such funds as constructive trustee for the Royal Bank under the principle of unjust enrichment as propounded in the well-known line of cases in the Supreme Court, starting with *Rathwell v. Rathwell*, [1978] 2 S.C.R. 436 and ending with *Peter v. Beblow*, [1993] 1 S.C.R. 980.

39 Mr. Neirinck started his argument by citing a passage from the judgment of Dickson J., as he then was, in *Rathwell v. Rathwell*, *supra*, at p.455, where he provides a rationale for the unjust enrichment principle and adumbrates his now famous three-part test for its application:

> As a matter of principle, the court will not allow any man unjustly to appropriate to himself the value earned by the labours of another. That principle is not defeated by the existence of a matrimonial relationship between the parties; but, for the principle to succeed, the facts must display an enrichment, a corresponding deprivation, and the absence of any juristic reason - such as a contract or disposition of law - for the enrichment.

40 On the facts of this case, argues Mr. Neirinck, the three-part test has been satisfied: Mrs. Harowitz was "enriched" by receipt of the $250,000. on July 10, 1991; the Royal Bank suffered a "corresponding deprivation" because the $250,000. came from its funds advanced to the fraudster, Melnitzer; and, finally, there can be "no juristic reason" justifying the receipt of these funds by Mrs. Harowitz. By way of *remedy* for breach of this equitable principle, he asks for imposition of a constructive trust on these funds and an order requiring her to return these funds to the Royal Bank.

41 In my view, Mr. Neirinck's argument, based as it is on the restitutionary principle of unjust enrichment, cannot

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succeed on the facts of this case.

42 For the purposes of this case, I am prepared to accept that Mrs. Harowitz received a benefit or enrichment when she received the $250,000. on July 10 and even that the Royal Bank sustained a detriment on that date because its funds, under its credit facility agreement with Melnitzer, were used by Melnitzer to pay back Mrs. Harowitz's loan.

43 What I must reject, however, is Mr. Neirinck's submission that the third element of unjust enrichment-the absence of juristic reason- has been satisfied by his client.

44 To me, it is crystal-clear that there was a juristic reason for Mrs. Harowitz's receipt of the $250,000. and that juristic reason goes back to Mrs. Harowitz's original contract arrangement with Melnitzer himself in 1986, as reflected in the promissory note.

45 After June 1, 1987, Mrs. Harowitz was entitled to demand repayment at any time. She made an entirely innocent and good-faith demand for the return of her money in March, 1991, and received those funds, through Melnitzer's cheque, on July 10. She had no knowledge of Melnitzer's fraudulent misrepresentations to the Royal Bank and, in fact, had no idea that Melnitzer used Royal Bank loan funds to pay her back. On July 10, then, when she received repayment of her funds, she fell into the classic legal position of *a bona fide purchaser for value without notice*: see *Banque Belge v. Hambrouck*, [1921] 1 K.B. 321 and *Nelson v. Larholt*, [1948] 1 K.B. 339. Surely, her position as a bona fide purchaser, receiving repayment of her promissory note entitlement, is a "juristic reason" for receipt of the funds taking this claim out of the unjust enrichment principle. If this is not a juristic reason, then, from my perspective, nothing can be a juristic reason.

46 During argument, Mr. Neirinck attempted to raise a novel argument against the Melnitzer-Harowitz contractual commitment and payment as a justifiable juristic reason. His point under the third element was this: the juristic reason justifying the receipt of the money must arise out of an obligation between the Royal Bank and Mrs. Harowitz. In other words, since Mrs. Harowitz received her money out of a contractual commitment of Melnitzer, and not the Royal Bank, to her, she cannot show a juristic reason for its receipt.

47 Mr. Neirinck's purported authority for this startling - to me, at least - proposition comes from a passage in the lead or controlling judgment in *Peter v. Beblow*, *supra*, written by McLachlin J. I reproduce the entire passage from her judgment, at p.989, so that it is possible to appreciate the context within which her comments were made. I have also italicized the exact sentence which Mr. Neirinck specifically relies upon:

> I share the view of Cory J. that the three elements necessary to establish a claim for unjust enrichment - an enrichment, a corresponding deprivation, and the absence of any juristic reason for the enrichment - are made out in this case. The appellant's housekeeping and child-care services constituted a benefit to the respondent (1st element), in that he received household services without compensation, which in turn enhanced his ability to pay off his mortgage and other assets. These services also constituted a corresponding detriment to the appellant (2nd element), in that she provided services without compensation. *Finally, since there was no obligation existing between the parties which would justify the unjust enrichment and no other arguments under this broad heading were met, there is no juristic reason for the enrichment* (*3rd element*). Having met the three criteria, the plaintiff has established an unjust enrichment giving rise to restitution.

48 With respect, McLachlin J., in this passage, is showing how the three elements of an unjust enrichment are made out in a two-party, family-like case.

49 *Peter* was another of the many cases where a woman who lived in a common-law relationship was claiming a constructive trust remedy against personal and real property accumulated by her companion. In such a two-party case it is but self-evident that the court will scrutinize the relationship of the man and woman to see if some "obligation" undergirded the services or work which the woman contributed to the relationship and the wealth accumulation by the man.

50 It is, however, 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.

51 What Mr. Neirinck has attempted to do is to put the flexible, three-element test for identifying an unjust enrichment

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into a straight-jacket created by facts and relationships usually associated with the family class of unjust enrichment cases.

52 In the case at bar, one is presented with a factual situation quite unlike the family cases where the claim is made in a bi-polar relationship between two spouses or two cohabiters, without the involvement of third parties. Here, however, the bi-polar or two party picture is clouded by special third-party features which cannot be ignored in order to decide whether a true unjust enrichment occurred.

53 In this same judgment of McLachlin J., in *Peter*, one may find a refined analysis of the concept of unjust enrichment as a unifying doctrine of equity. She says this at p.987:

> In recent decades, *Canadian courts have adopted the equitable concept of unjust enrichment inter alia as the basis for remedying the injustice that occurs where one person makes a substantial contribution to the property of another person without compensation.* The doctrine has been applied to a variety of situations, from claims for payments made under mistake to claims arising from conjugal relationships. While courts have not been adverse to applying the concept of unjust enrichment in new circumstances, they have insisted on adhering to the fundamental principles which have long underlain the equitable doctrine of unjust enrichment. As stated by LaForest J.A. (as he then was) in *White v. Central Trust Co.* (1984), 54 N.B.R. (2d) 293, at p.309 "... the well recognized categories of unjust enrichment must be regarded as clear examples of the more general principle that transcends them". (Emphasis added)

54 Later, at p.990, she attempted to highlight the importance of the third element of the formula. In *Peter* the woman claimant was faced with a barrage of moral and policy arguments designed to show that her contributions to the household could not give rise to a legitimate claim for unjust enrichment because, it was submitted, she had voluntarily assumed the role she performed or had performed her services out of love and affection.

55 McLachlin, J. said that it was fruitless to consider such "moral and policy questions" under the first two elements - "the benefit-detriment analysis" - and held that such considerations must be considered under what she described as the "flexible" third element of the test:

> The first question is: where do these arguments belong? Are they part of the benefit - detriment analysis, or should they be considered under the third head - the absence of juristic reason for the unjust enrichment? The Court of Appeal, for example, held that there was no "detriment" on these grounds. I hold the view that these factors may most conveniently be considered under the third head of absence of juristic reason. This Court has consistently taken a straightforward economic approach to the first two elements of the test for unjust enrichment: *Pettkus v. Becker, supra; Sorochan v. Sorochan*, [1986] 2 S.C.R. 38: *Peel (Regional Municipality) v. Canada*, [1992] 3 S.C.R. 762, (hereinafter "*Peel*"). It is in connection with the third element - absence of juristic reason for the enrichment - that such considerations may more properly find their place. 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: *Pettkus v. Becker, supra*.

56 McLachlin J.'s final point about the "legitimate expectations of the parties" demonstrates to me the sheer futility of the plaintiff's argument that Mrs. Harowitz's juristic reason for the receipt of the money must arise from an obligation of the Royal Bank towards her.

57 Mrs. Harowitz always had a legitimate expectation arising out of her relationship with Melnitzer and that was that she would be repaid on demand. She was, in fact, repaid on demand and she received her money with clean hands.

58 On the other side of the coin, what were the expectations of the Royal Bank? The Royal Bank entered its credit facility

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arrangement with Melnitzer with a hard-headed business decision. It agreed to provide credit to Melnitzer up to a limit of $3,000,000. and took security for its loan as it saw fit. Amongst the security was the $1,509,430.42 sum deposited in the special savings account along with the Melfan guarantee and hypothecation of shares. Melnitzer drew down many sums from this credit facility between 1989 and the end of July, 1991, when a greatly increased credit facility of $8,000,000. was about to be put into effect. I cannot see any evidence indicating that the Bank had any expectation of making any claim against an innocent third party like Mrs. Harowitz who happened to have an *earlier* commitment from Melnitzer and saw it honoured with funds from a credit facility of which she was totally unaware.

59 It is not without value to note the contents of the claims set out in the plaintiff's statement of claim. While the plaintiff has pleaded its unjust enrichment/constructive trust claim, it also claimed the return of its money under the doctrine of equitable tracing: see paragraph 15 of the statement of claim.

60 The plaintiff plainly could not rely on the tracing claim here because of decisional limitations on that doctrine. The applicable case-law is clear that tracing is not permitted where the claim arises out of a contractual debtor-creditor relationship such as the one here between Melnitzer and the Bank: see my judgment in *C.I.B.C. v. Peat Marwick Thorne Inc., et al*, released on November 26, 1993, especially at pp.35-36.

61 In my view, the unjust enrichment claim is equally doomed to failure on the evidence because it attempts to distort the third element of the tripartite test for unjust enrichment. 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. That is the theme of McLachlin J.'s strong judgment in *Peter* and, indeed, it is the constant theme of the entire line of cases on this subject in the Supreme Court.

62 There is strong decisional authority in British Columbia for the interpretive approach I have taken to the third element of the principle at issue.

63 In the case of *Cherrington v. Mayhew's Perma-Plants* (1990), 45 B.C.L.R. (2d) 374, the British Columbia Court of Appeal was dealing with an analogous problem. There, a bookkeeper employed by a law firm fraudulently used cheques drawn on the law firm's account to pay a debt which the bookkeeper owed to a third-party company. When the law firm learned of the fraud, it sued this company under the unjust enrichment principle.

64 The trial judge had given judgment in favour of the plaintiff law firm but the Court of Appeal reversed. Hollinrake J.A. said this at pp. 377-78 in reversing the trial judge's decision and dismissing the action:

> Assuming there has been an enrichment here within this principle as the judge found, and further assuming there was a corresponding deprivation, again as the judge found, in my opinion, the learned chambers judge erred in finding there was an absence of any juristic reason for this alleged enrichment. He said the reason for this absence was that the respondents "were under no obligation, contractual or otherwise", to the appellant. This, in my opinion, is where there is error. I do not think juristic reason in the context of this case depends on any obligation or relationship as between the respondents and the appellant.
>
> What the appellant in this case must show is that there was a juristic reason for the funds coming into its hands. That juristic reason is the debt owed by Cochran and her company to the appellant. There is no suggestion that this debt was other than enforceable at the time.

65 While Mr. Neirinck attempted to distinguish this case on the basis of a later passage in the judgment where Hollinrake J.A. mentions that the defendant company had advanced further credit to the fraudulent employee after being paid, I am not satisfied that this evidentiary point controlled the outcome. In the same passage Hallinrake J.A. adopts a rubric developed by Lambert J.A. in another case, *Atlas Cabinets & Furniture Ltd. v. National Trust Company* (1990), 45 B.C.L.R. (2d) 99, namely, that, in commercial cases, the element of injustice or "commercial good conscience" should guide the application of the three-part test. Even using the "commercial good conscience" guideline, adopted by Lambert J.A., I think that Mrs. Harowitz's position is impregnable under the third part of the test. See, also, to the same effect, *Ken Lawter Holdings Ltd. v. Steen Panduro Holdings Ltd.* (1991), 55 B.C.L.R. (2d) 317 and *McDiarmid Lumber Ltd. v. Canadian Imperial Bank of Commerce* (1992), 71 B.C.L.R. (2d) 301.

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66 In the result, the plaintiff's claim under the principle of unjust enrichment must fail and the action is dismissed.

67 If counsel cannot agree on an appropriate costs' disposition, I may be spoken to in the next 30 days.

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1997 CarswellOnt 2609
Ontario Court of Appeal

Royal Bank v. Harowitz

1997 CarswellOnt 2609, [1997] O.J. No. 2599, 33 O.R. (3d) 704 (note), 33 O.R. (3d) 704, 72 A.C.W.S. (3d) 614

Royal Bank of Canada, Plaintiff/Appellant v. Sharon Harowitz, Defendant/Respondent

McMurtry C.J.O., Carthy and Goudge JJ.A.

Heard: June 24, 1997
Judgment: June 26, 1997
Docket: CA C18367

Proceedings: affirming (1994), 17 O.R. (3d) 671 (Ont. Gen. Div.)

Counsel: *Maurice J. Neirinck*, for the appellant.
Stanley M. Tick, Q.C. and *Janis P. Criger*, for the respondent.

Subject: Corporate and Commercial; Restitution

Related Abridgment Classifications

Bills of exchange and negotiable instruments
III Cheques
  III.11 Forged or unauthorized cheques
    III.11.e Cheque obtained by fraud or theft

Restitution and unjust enrichment
I General principles
  I.2 Requirements for unjust enrichment
    I.2.c No juristic reason for enrichment

Headnote

Banking and banks --- Cheques — Forged or unauthorized cheques — Cheque obtained by fraud or theft
Customer fraudulently obtained credit from bank — Customer gave defendant cheque from account to pay off loan — Customer became bankrupt — Bank brought action against defendant for declaration that defendant held funds as constructive trustee for bank — Action dismissed — Appeal dismissed — Absence of juristic reason was not proven — Juristic reason lay in loan between defendant and customer — Juristic reason not required to be connected to party which made claim — Not unjust for defendant to retain funds.

Restitution --- General principles — Bars to recovery — Juristic reason for enrichment
Customer fraudulently obtained credit from bank — Customer gave defendant cheque from account to pay off loan — Customer became bankrupt — Bank brought action against defendant for declaration that defendant held funds as constructive trustee for bank — Action dismissed — Appeal dismissed — Absence of juristic reason was not proven — Juristic reason lay in loan between defendant and customer — Juristic reason not required to be connected to party which made claim — Not unjust for defendant to retain funds.

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APPEAL by bank from judgment reported at (1994), 17 O.R. (3d) 671 (Ont. Gen. Div.) dismissing action.

McMurtry C.J.O. **(Carthy and Goudge JJ.A. concurring):**

Endorsement

1 We agree with the reasons of Killeen J. While, in our view, there is real doubt that when an innocent creditor is repaid she can be said to be enriched for the purposes of the unjust enrichment doctrine, there is a sound juristic reason on these facts for the respondent to retain the funds she was owed. The fundamental principle of the doctrine is that retention of the funds be unjust. Given the relative positions of the appellant and the respondent to Mr. Melnitzer, it cannot be said to be unjust for the respondent to retain the funds paid for the debt owed her.

2 The appeal is dismissed with costs.

Appeal dismissed.

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TAB 5

2000 CarswellOnt 109
Ontario Superior Court of Justice

Ierullo v. Rovan

2000 CarswellOnt 109, [2000] O.J. No. 108, 3 B.L.R. (3d) 163, 46 O.R. (3d) 692, 94 A.C.W.S. (3d) 166

Rae Ierullo, Plaintiff and David M. Rovan, Defendant

Nordheimer J.

Heard: January 13 and 14, 2000
Judgment: January 20, 2000
Docket: 99-CV-169177SR

Counsel: *Joy Casey*, for Plaintiff.
Ian R. Mang, for Defendant.

Subject: Corporate and Commercial

Related Abridgment Classifications

Bills of exchange and negotiable instruments
II Bills of exchange
II.6 Consideration
II.6.c Prior debt or liability

Bills of exchange and negotiable instruments
II Bills of exchange
II.10 Holders
II.10.a General principles
II.10.a.ii Presumption of due course

Bills of exchange and negotiable instruments
II Bills of exchange
II.10 Holders
II.10.b Good faith of holder

Bills of exchange and negotiable instruments
II Bills of exchange
II.10 Holders
II.10.c Equities and defects in title
II.10.c.i Fraud

Estates and trusts
II Trusts
II.3 Constructive trust
II.3.a Elements of constructive trust

Headnote

Bills of exchange --- Bills of exchange — Holders — General — Presumption of due course

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Plaintiff paid tenant to perform work on her property — Plaintiff gave tenant cheques with payee's name left blank for purchase of equipment, including cheque for $20,000 — Tenant gave $20,000 cheque to his lawyer, as payee, as payment for long-standing debt and as condition for retaining lawyer's services on new matters — Shortly before tenant was arrested for parole violations, plaintiff discovered that tenant had criminal record for fraudulent offences — Plaintiff brought action against payee for return of amount of cheque — Action dismissed — Writing cheque in blank form generally means person who appears as payee will be unconnected to payor — Payee was consequently and reasonably considered remote party to bill of exchange and was entitled to protection as holder in due course.

Bills of exchange --- Bills of exchange — Holders — Good faith of holder
Plaintiff paid tenant to perform work on her property — Plaintiff gave tenant cheques with payee's name left blank for purchase of equipment, including cheque for $20,000 — Tenant gave $20,000 cheque to his lawyer, as payee, as payment for long-standing debt and as condition for retaining lawyer's services on new matters — Shortly before tenant was arrested for parole violations, plaintiff discovered that tenant had criminal record for fraudulent offences — Plaintiff brought action against payee for return of amount of cheque — Action dismissed — Payee was holder in due course — Payee took cheque as payment for bona fide debt and no evidence indicated that payee had not taken cheque in good faith.

Bills of exchange --- Bills of exchange — Consideration — Prior debt or liability
Plaintiff paid tenant to perform work on her property — Plaintiff gave tenant cheques with payee's name left blank for purchase of equipment, including cheque for $20,000 — Tenant gave $20,000 cheque to his lawyer, as payee, as payment for long-standing debt and as condition for retaining lawyer's services on new matters — Shortly before tenant was arrested for parole violations, plaintiff discovered that tenant had criminal record for fraudulent offences — Plaintiff brought action against payee for return of amount of cheque — Action dismissed — Payee took cheque in repayment of old debt and as condition for doing new work — Payee took bill of exchange for value.

Bills of exchange --- Bills of exchange — Holders — Equities and defects in title — Fraud
Plaintiff paid tenant to perform work on her property — Plaintiff gave tenant cheques with payee's name left blank for purchase of equipment, including cheque for $20,000 — Tenant gave $20,000 cheque to his lawyer, as payee, as payment for long-standing debt and as condition for retaining lawyer's services on new matters — Shortly before tenant was arrested for parole violations, plaintiff discovered that tenant had criminal record for fraudulent offences — Plaintiff brought action against payee for return of amount of cheque — Action dismissed — Tenant negotiated cheque in circumstances that amounted to fraud — Payee took steps to inquire into circumstances of cheque by confirming legitimacy with plaintiff's other tenant and by having cheque certified — Payee had no notice of defect in title of cheque and, as holder in due course, was entitled to retain proceeds.

Trusts and trustees --- Constructive trust — General principles
Plaintiff paid tenant to perform work on her property — Plaintiff gave tenant cheques with payee's name left blank for purchase of equipment, including cheque for $20,000 — Tenant gave $20,000 cheque to his lawyer, as payee, as payment for long-standing debt and as condition for retaining lawyer's services on new matters — Shortly before tenant was arrested for parole violations, plaintiff discovered that tenant had criminal record for fraudulent offences — Plaintiff brought action against payee for return of amount of cheque on ground of constructive trust — Action dismissed — Payee was not unjustly enriched as he had obtained payment for debt that was due to him — Harm to plaintiff that corresponded with payment to payee was not sufficient to warrant constructive trust remedy — Payee took steps to inquire into circumstances of cheque by confirming legitimacy with plaintiff's other tenant and by having cheque certified — Payee had no knowledge of breach of trust and was not wilfully blind or reckless to events that constituted breach.

Table of Authorities

Cases considered by *Nordheimer J.*:

Air Canada v. M & L Travel Ltd., 50 E.T.R. 225, 108 D.L.R. (4th) 592, [1993] 3 S.C.R. 787, 67 O.A.C. 1, 159 N.R. 1, 15 O.R. (3d) 804 (note) (S.C.C.) — referred to

Bank of Nova Scotia v. Toronto Dominion Bank (1997), 34 O.R. (3d) 138 (Ont. Gen. Div.) — referred to

Dominion Bank v. Fassel & Baglier Construction Co., [1955] O.W.N. 709, [1955] 4 D.L.R. 161 (Ont. C.A.) — referred

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to

Lee v. Blake, 55 O.L.R. 310, [1924] 4 D.L.R. 369 (Ont. C.A.) — referred to

Marshall v. Rogers, [1924] 1 D.L.R. 888 (Alta. S.C.) — referred to

Marvco Color Research Ltd. v. Harris, [1982] 2 S.C.R. 774, 141 D.L.R. (3d) 577, 45 N.R. 302, 20 B.L.R. 143, 26 R.P.R. 48 (S.C.C.) — considered

R.E. Jones Ltd. v. Waring & Gillow Ltd., [1926] A.C. 670, [1926] All E.R. Rep. 36 (U.K. H.L.) — not followed

Soulos v. Korkontzilas, 212 N.R. 1, 9 R.P.R. (3d) 1, 46 C.B.R. (3d) 1, 32 O.R. (3d) 716 (headnote only), 146 D.L.R. (4th) 214, 100 O.A.C. 241, 17 E.T.R. (2d) 89, [1997] 2 S.C.R. 217 (S.C.C.) — considered

Statutes considered:

Bills of Exchange Act, R.S.C. 1985, c. B-4
s. 55 — considered

s. 55(1)(b) — considered

s. 55(2) — considered

s. 165 — referred to

ACTION by plaintiff payor against payee for reimbursement of amount of cheque.

***Nordheimer J.*:**

1 The plaintiff claims on a cheque dated October 21, 1997 for $20,000.00 written by her but made payable to the defendant without her knowledge or consent. The issue is whether the plaintiff is entitled in the unusual circumstances that I will describe below to recover the face amount of the cheque from the defendant.

Background

2 The plaintiff and her husband own a large piece of property in the Township of Stouffville ("the property"). On one portion of the property there is a small bungalow which was rented when the plaintiff and her husband bought the property. Subsequently, that tenant left the bungalow and the plaintiff and her husband rented the property to a new tenant who I shall simply refer to by her first name, Bridget. The plaintiff considered Bridget to be a very reliable and trustworthy individual and she was therefore quite comfortable renting the bungalow to her. Sometime after Bridget moved into the bungalow she advised the plaintiff that her boyfriend would be moving in with her. Her boyfriend was Ric Nicholls. At the time, the plaintiff knew nothing else about Mr. Nicholls.

3 The property was a former Christmas tree farm and there were a large number of trees on it which had not been looked after for some time. Mr. Nicholls suggested to the plaintiff that he could clean up the property by removing dead trees and thinning out other trees. He offered to do this work for $65.00 per hour. After checking with other possible sources for this type of work, the plaintiff determined that the proposal from Mr. Nicholls was a fair one and agreed to it. Mr. Nicholls then prepared an independent contractor agreement handwritten on a standard form. The agreement was drawn between the plaintiff and B&R Holdings which was a trade name adopted by Mr. Nicholls — the "B" standing for Bridget and the "R" standing for Ric. The agreement was signed on August 6, 1997.

4 Mr. Nicholls proceeded with the work which included bringing onto the property a number of pieces of equipment,

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including trucks, chain saws and the like. Mr. Nicholls also told the plaintiff about other work that he was doing for other parties. It appeared to the plaintiff therefore that Mr. Nicholls had an active and successful business.

5 Sometime in September, Mr. Nicholls suggested to the plaintiff that a large swamp that was on the property could be turned into a nice pond. Again, he quoted a price to the plaintiff for doing this work and again, after checking with other possible suppliers, the plaintiff agreed to have Mr. Nicholls undertake this work. Shortly after Mr. Nicholls started the work on the swamp, he advised the plaintiff that a great deal of the material that was going to have to be removed from the swamp was peat. He suggested to the plaintiff that the peat could be sold commercially if it was properly screened and that the proceeds of the sale of the peat could be used to defray the costs of building the pond. This sounded like a good idea to the plaintiff so she agreed. While the plaintiff did not know anything about the peat business, she did have someone come and do an analysis of the peat and it was confirmed to the plaintiff that the peat was good quality peat.

6 In order to properly set up this new business, on the advice of her accountant, the plaintiff incorporated a company. The arrangements for the business were that the plaintiff and her husband would own the company, the company would operate the peat processing business and Mr. Nicholls would be hired to be the general manager of the company. As part of the start-up of the business, Mr. Nicholls told the plaintiff that he would have to buy additional equipment to process the peat including a screening plant. He said he would need funds from the plaintiff to buy this equipment. Consequently, the plaintiff started to give cheques to Mr. Nicholls, drawn on her joint account with her husband, to buy equipment.

7 Some short time later, Mr. Nicholls advised the plaintiff that the cost to purchase a screening plant would be quite high. He suggested to the plaintiff that he could put a screening plant together by buying the necessary parts from different sources at a much cheaper price and the plaintiff agreed. As part of this endeavour, Mr. Nicholls advised the plaintiff that he would, on occasion, need cheques with the payee's name left blank because he did not know the exact legal entity from whom he would be buying certain parts. The plaintiff therefore gave some cheques (the exact number is not clear) to Mr. Nicholls with the payee's name left blank. One of those cheques is the subject of this action. It was in the amount of $20,000.00 and it was subsequently made payable to, and negotiated by, the defendant.

8 In mid-December, the police contacted the plaintiff through the plaintiff's lawyer. The police advised the plaintiff that Mr. Nicholls was on parole for certain criminal offences and was a dangerous person. The plaintiff says that she was frightened by this information, both for herself and for her children, because Mr. Nicholls is a physically large person. The plaintiff also says that she did not know what to do with this information because Mr. Nicholls was still living in the bungalow and working on the property. As it happens, the very next day Mr. Nicholls came to visit the plaintiff. It was obvious to the plaintiff that Mr. Nicholls was aware of the fact that the plaintiff had been contacted by the police because Mr. Nicholls advised her that she did not have anything to fear from him. Further, Mr. Nicholls called his lawyer and asked his lawyer to tell the plaintiff on the phone that she was not in any danger from Mr. Nicholls. Mr. Nicholls' lawyer advised the plaintiff that there were no instances of violent conduct in Mr. Nicholls' background. Mr. Nicholls' lawyer was the defendant, David Rovan.

9 A couple of days later, Mr. Nicholls was arrested for parole violations. Around this time, various municipal and provincial officials visited the property to examine the work that was being done. These officials advised the plaintiff that the work was being undertaken without proper permits and was also being undertaken in an environmentally sensitive area. I gather there was some considerable fallout from those matters but I need not go into those issues for the purposes of deciding this claim.

10 Shortly before Mr. Nicholls' arrest, the plaintiff received her bank statement with the cancelled cheques including the cheque to the defendant. She asked Mr. Nicholls about the cheque and was assured by him that it was connected to the purchase of equipment. Given the circumstances, the plaintiff did not press Mr. Nicholls on this point. However, after Mr. Nicholls' arrest and the visit from the municipal and provincial officials, the plaintiff did have her lawyer write to the defendant and demand the return of the monies reflected in the cheque. It appears this happened in January, 1998. It was originally assumed that these monies had been given to the defendant on account of legal fees but in fact it turns out that they were given to the defendant to pay off a long standing debt which Mr. Nicholls owed to the defendant.

11 Notwithstanding subsequent demands by the plaintiff's lawyer, by the plaintiff's husband and by the plaintiff herself, the defendant refused to return the monies. There was a complaint made by the plaintiff to the Law Society of Upper Canada

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but the Law Society determined that there was no basis for it to conclude that there had been any misconduct by the defendant and refused to further pursue the matter. Eventually this action was commenced.

12 I now turn to the connection between the defendant and Mr. Nicholls. The defendant is a lawyer who first met Mr. Nicholls in 1983. The defendant incorporated a company for Mr. Nicholls. Subsequently, Mr. Nicholls asked the defendant to represent him on an impaired driving charge. During the course of this representation, the defendant learned of Mr. Nicholl's criminal record which, I gather, was significant and which included a number of convictions for fraud.

13 In May, 1983, Mr. Nicholls asked the defendant to loan him $10,000 to assist him in buying equipment for his company. Unwisely, as the defendant himself admits, he agreed to provide the loan. The defendant had Mr. Nicholls sign a promissory note on behalf of himself and the company. Mr. Nicholls never repaid the loan and later the defendant lost track of Mr. Nicholls.

14 In late December, 1996 or early 1997, in the course of a move of his office, the defendant discovered the file on his loan to Mr. Nicholls. Having not heard anything from Mr. Nicholls for at least three or four years, and having concluded that the loan was lost money, the defendant threw out the promissory note. However, some few months later, Mr. Nicholls suddenly contacted the defendant. Mr. Nicholls came to see the defendant in the company of Bridget. Mr. Nicholls told the defendant that he was out on parole, that he was involved in a new and legitimate business and that he never wanted to go back to prison again. Mr. Nicholls then asked the defendant to incorporate three companies for him. The defendant said that he would do the work but only if Mr. Nicholls paid him the money that he owed from 1983. After doing a calculation of interest for the past 14 years, the defendant advised Mr. Nicholls that he owed him something in the order of $30,000.00 to $35,000.00. Mr. Nicholls balked at paying that much. Consequently, the defendant and Mr. Nicholls agreed on the sum of $20,000.00 to retire the debt. The defendant did not, of course, tell Mr. Nicholls that he had recently thrown out the promissory note. Mr. Nicholls then promised to get the defendant the money and the defendant proceeded to prepare the papers necessary to incorporate the companies. One other piece of information which Mr. Nicholls gave to the defendant was that it was a term of his parole that he could not have or operate a bank account. Consequently, Bridget gave a cheque to the defendant to pay the fees for incorporating the companies. Given his history of fraud convictions, the defendant did not consider this to be an unusual or unlikely term for Mr. Nicholls' parole.

15 When the defendant had the documents for the companies ready, he contacted Mr. Nicholls who urged him to come up to the bungalow with the papers. Mr. Nicholls told the defendant that he had the $20,000.00 to give him. Mr. Nicholls took the defendant on a tour of the property and showed him all of the work that he was doing and obviously made it appear to the defendant that he did have an active and legitimate business. When they went back to the bungalow, Mr. Nicholls gave the defendant the cheque for $20,000.00 from the plaintiff on which, it is clear to me, Mr. Nicholls had written the defendant's name as the payee. The defendant noticed that the cheque had not been written by Mr. Nicholls. Mr. Nicholls told the defendant that the cheque was an advance on his salary from this new business. Mr. Nicholls had earlier mentioned to the defendant that the plaintiff was the person behind this new business. Mr. Nicholls assured the defendant that the plaintiff knew that the cheque was being given to the defendant.

16 The defendant acknowledges that he was suspicious about the cheque. Indeed, his evidence was that he had a general suspicion about Mr. Nicholls at all times. The defendant says that he did two things to ease his suspicions regarding the cheque. First, he got confirmation from Bridget as to the story that Mr. Nicholls was telling him both regarding the business and regarding the cheque. The defendant considered Bridget to be trustworthy and what he referred to as a "straight shooter". The defendant also decided to have the cheque certified. His express reason for doing so was that the cheque was drawn on an account at the Royal Bank of Canada and the defendant says that, from his personal experience, he knows that it is the policy of the Royal Bank to contact an account holder before it certifies a cheque on their account. Therefore, the defendant assumed that the plaintiff would be contacted by the bank in the course of getting the cheque certified. It is appropriate to make it clear at this juncture that the plaintiff denies that anyone from the Royal Bank ever contacted her or her husband regarding this cheque.

17 The next day, the defendant asked his wife to take the cheque to the plaintiff's bank branch and have it certified. The defendant's wife did so. Mrs. Rovan gave evidence that she went to the branch and asked for the cheque to be certified. Mrs. Rovan says that she was told that it might take some time to get the cheque certified because the branch would have to contact the account holder because of the amount of the cheque. Mrs. Rovan said that she would wait. About half an hour

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later, Mrs. Rovan was told that everything was fine and the cheque was certified and given to her. During the time she was waiting, Mrs. Rovan observed one of the bank employees, who was involved in the process of certifying the cheque, make a telephone call but she admitted, obviously, that she did not know who it was that was telephoned or what was said. Mrs. Rovan returned home and that night gave the certified cheque to the defendant who subsequently deposited it in his bank account.

Analysis

18 A cheque is a bill drawn on a bank that is payable on demand. Cheques are covered by the *Bills of Exchange Act*, R.S.C. 1985, c. B-4, specifically section 165. The first issue raised is whether the payee of a cheque can be a holder in due course of it. This issue has been one that has been one that has been controversial for more than 100 years. While the House of Lords purported to resolve the issue in 1926 in *R.E. Jones Ltd. v. Waring & Gillow Ltd.*, [1926] A.C. 670 (U.K. H.L.) wherein it was decided that a payee could not be a holder in due course, that decision was not without its detractors and, in any event, has technically not binding on Canadian courts for decades with the result that existing decisions in our courts have not always chosen to follow it.

19 The authors of Crawford and Falconbridge, *Banking and Bills of Exchange*, 8th ed. Toronto: Canada Law Book, 1986 at pp. 1476-1477, offer a strong argument that the payee of a cheque should be considered as a holder in due course of it. They contend, and I respectfully agree with them, that this is particularly so in a case such as this where the cheque is written in blank form since such circumstances will generally mean that the person whose name subsequently appears as payee on the cheque will be a person unconnected to the payor. Such a person is consequently and reasonably to be considered a remote party to the bill and thus is someone who ought to take as a holder in due course and to be entitled to the protection that such a status affords. This same conclusion appears have been reached by the Court of Appeal in *Lee v. Blake*, [1924] 4 D.L.R. 369 (Ont. C.A.) and also by Simmons, J. in *Marshall v. Rogers*, [1924] 1 D.L.R. 888 (Alta. S.C.).

20 While I recognize that both of those decisions were reached prior to the decision of the House of Lords in *R.E. Jones Ltd. v. Waring & Gillow Ltd.*, for the reasons set out in that portion of Crawford and Falconbridge to which I have referred above, I conclude that the decision in *R.E. Jones Ltd. v. Waring & Gillow Ltd.* should not be followed in the particular circumstances of this case and that the defendant should be found to be a holder in due course of the cheque in question. That such a conclusion could, in appropriate circumstances, be justified was expressly recognized in *Dominion Bank v. Fassel & Baglier Construction Co.*, [1955] 4 D.L.R. 161 (Ont. C.A.) although I note that the decision in that case does not make any reference to *R.E. Jones Ltd. v. Waring & Gillow Ltd.*

21 What follows from this finding? Section 55 of the *Bills of Exchange Act* states:

> 55.(1) A holder in due course is a holder who has taken a bill, complete and regular on the face of it, under the following conditions, namely,
>
> > (a) that he became the holder of it before it was overdue and without notice that it had been previously dishonoured, if such was the fact; and
> >
> > (b) that he took the bill in good faith and for value, and that at the time the bill was negotiated to him he had no notice of any defect in the title of the person who negotiated it.
>
> (2) In particular, the title of a person who negotiates a bill is defective within the meaning of this Act when he obtained the bill, or the acceptance thereof, by fraud, duress or force and fear, or other unlawful means, or for an illegal consideration, or when he negotiates it in breach of faith, or under such circumstances as amount to a fraud.

22 Subsection 55(1)(b) has three requirements that the defendant must satisfy. First, the defendant must take the bill in good faith. Secondly, he must take it for value. Thirdly, he must not have notice of any defect in the title of the person who negotiated it to him. The plaintiff contends that the defendant cannot satisfy any of these requirements. I do not agree. At least with respect to the first two requirements, I believe that the defendant clearly satisfies them. There is no evidence upon

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which I could conclude other than that the defendant took the cheque in good faith. There is nothing to question the *bona fides* of the defendant in attempting to get payment of the debt which Mr. Nicholls owed him. The fact that there might have been technical defences available to Mr. Nicholls had the defendant been compelled to sue him on the note does not detract from the fact that the monies were borrowed by Mr. Nicholls and never repaid. The defendant had a legitimate interest in seeking their repayment and it was fair for him to make it a condition of doing work for Mr. Nicholls that Mr. Nicholls honour this obligation. Further, it is equally clear to me that the defendant took the bill for value. He took it in repayment of this old debt; he took it as an agreed compromise on the amount that was due to him on that old debt; and, he took it as a condition of doing fresh work for Mr. Nicholls.

23 The third requirement is considerably more problematic. Subsection 55(2) of the Act expands on what is meant by a defect in title. Applying that subsection to the circumstances of this case, it is clear that Mr. Nicholls negotiated the cheque in breach of faith and also in circumstances that amount to a fraud. The issue then becomes did the defendant have notice of this defect. In considering this issue, one necessarily has to ask the corollary question — what degree of inquiry was placed on the defendant in such circumstances regarding the cheque?

24 The defendant admits that he was suspicious regarding the cheque. He took steps to deal with that suspicion by obtaining confirmation of the surrounding circumstances from Bridget who he thought was trustworthy. I note that the plaintiff also viewed Bridget as trustworthy so it does not seem that the plaintiff can legitimately criticize the defendant for placing reliance on her. The defendant also took steps to get the cheque certified believing that this would involve some ratification by the plaintiff of the use to which the cheque was being put. This latter evidence is of limited usefulness, however, because there is no direct evidence from the Royal Bank that it has a policy to contact the account holder prior to certifying a cheque and that, even if it has such a policy, the policy was followed in this particular case.

25 The real question is whether on the facts of this case there should be a finding that the defendant did not have notice of the defect in title of Mr. Nicholls to the cheque in question? While I consider it a very close call in the unusual circumstances of this case, I have concluded that the defendant did not have notice of the defect in title. The defendant, therefore, is a holder in due course of the cheque and is entitled to retain the proceeds of it.

26 In reaching this conclusion, I am mindful of the fact that there were steps available to the plaintiff which, had she taken them, would have either avoided the whole issue or would have made the onus of inquiry on the defendant greater. The former step was, of course, not to issue the cheque with the payee in blank. The plaintiff could have easily told Mr. Nicholls that she was not prepared to take such a risk and that he would simply have to arrange his purchases so that the exact payee would be known whenever the cheque had to be written. The latter step was for the plaintiff, as she had apparently done on other cheques, to write on the face of the cheque what it was to be used for. There is a line on the front of the cheque for just this purpose. Had the plaintiff written on the front of the cheque "payment for equipment" or "payment for screening plant" or the like, then the defendant would clearly have been put on further inquiry before he accepted such a cheque in the subsequent circumstances in which Mr. Nicholls gave it to him[1]. In this regard, the observation of Mr. Justice Estey in *Marvco Color Research Ltd. v. Harris* (1982), 141 D.L.R. (3d) 577 (S.C.C.) at p. 585, albeit in a different context, is applicable here:

> As between the appellant and the respondents, simple justice requires that the party, who by the application of reasonable care was in a position to avoid a loss to any of the parties, should bear any loss that results when the only alternative available to the courts would be to place the loss upon the innocent appellant.

27 The plaintiff also relies on the doctrine of constructive trust in support of her claim. In particular, reliance is placed on the decisions of the Supreme Court of Canada in *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787 (S.C.C.) and in *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217 (S.C.C.). In the *Soulos* case, Madam Justice McLachlin (as she then was) said at para. 20:

> Canadian courts have never abandoned the principles of constructive trust developed in England. They have, however, modified them. Most notably, Canadian courts in recent decades have developed the constructive trust as a remedy for unjust enrichment. It is now established that a constructive trust may be imposed in the absence of wrongful conduct like breach of fiduciary duty, where three elements are present: (1) the enrichment of the defendant; (2) the corresponding deprivation of the plaintiff; and (3) the absence of a juristic reason for the enrichment: *Pettkus v. Becker, supra*.

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28 It follows from my findings above that I do not consider this to be a case of unjust enrichment. The defendant has not been unjustly enriched; he has obtained payment of a debt that was due by Mr. Nicholls to him. Granted that payment came with a corresponding harm to the plaintiff but that fact does not, in my view, warrant the imposition of the extraordinary remedy of a constructive trust. Further, even if one imposed a constructive trust on the cheque, the defendant would only be liable for a breach of that trust if it could be shown that he had actual knowledge of the breach or was reckless or wilfully blind to the events that constituted the breach of the trust — see *Air Canada*, *supra*, at para. 38. That requirement would seem to lead right back to the same inquiry that was necessary regarding whether the defendant had notice of the defect in title to the cheque. For the same reasons I have set out above, I would conclude that the actions of the defendant do not amount to recklessness or wilful blindness regarding the activities of Mr. Nicholls.

29 In the end result, therefore, the plaintiff's claim is dismissed. The parties may make written submissions to me on the disposition of the costs of the action. The defendant shall deliver his submissions within 10 days of the date of these reasons and the plaintiff shall deliver her response within 10 days thereafter.

Action dismissed.

Footnotes

[1] Such a statement of the front of a cheque is precisely what lead to the opposite finding in favour of the plaintiff in *Bank of Nova Scotia v. Toronto Dominion Bank* (1997), 34 O.R. (3d) 138 (Ont. Gen. Div.)

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2001 CarswellOnt 9827
Ontario Superior Court of Justice (Divisional Court)

Ierullo v. Rovan

2001 CarswellOnt 9827, [2001] O.J. No. 5419

Rae Ierullo v. David Rovan

Czutrin J., Day J., Lang J.

Judgment: November 23, 2001
Docket: Toronto 114/00

Proceedings: affirming *Ierullo v. Rovan* (2000), 2000 CarswellOnt 109, 46 O.R. (3d) 692, 3 B.L.R. (3d) 163 (Ont. S.C.J.)

Counsel: Joy Casey, for Appellant

Subject: Corporate and Commercial

Related Abridgment Classifications

Bills of exchange and negotiable instruments
II Bills of exchange
II.6 Consideration
II.6.c Prior debt or liability

Bills of exchange and negotiable instruments
II Bills of exchange
II.10 Holders
II.10.a General principles
II.10.a.ii Presumption of due course

Bills of exchange and negotiable instruments
II Bills of exchange
II.10 Holders
II.10.b Good faith of holder

Bills of exchange and negotiable instruments
II Bills of exchange
II.10 Holders
II.10.c Equities and defects in title
II.10.c.i Fraud

Estates and trusts
II Trusts
II.3 Constructive trust
II.3.a Elements of constructive trust

Headnote

Bills of exchange and negotiable instruments --- Bills of exchange — Holders — General principles — Presumption of due

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course
Plaintiff paid tenant to perform work on her property — Plaintiff gave tenant cheques with payee's name left blank for purchase of equipment, including cheque for $20,000 — Tenant gave $20,000 cheque to his lawyer, as payee, as payment for long-standing debt and as condition for retaining lawyer's services on new matters — Shortly before tenant was arrested for parole violations, plaintiff discovered that tenant had criminal record for fraudulent offences — Plaintiff brought action against payee for return of amount of cheque — Action dismissed — Trial judge held that writing cheque in blank form generally means person who appears as payee will be unconnected to payor — Payee was consequently and reasonably considered remote party to bill of exchange and was entitled to protection as holder in due course — Plaintiff appealed — Appeal dismissed — Plaintiff argued that bill was payable to order rather than to bearer and accordingly required endorsement — Trial judge considered all these issues and reviewed law on both sides of argument — Trial judge made factual findings that payee satisfied three requirements of holder in due course: that he took bill in good faith, for value, and without notice of defect — There was no ground to interfere with those findings.

Bills of exchange and negotiable instruments --- Bills of exchange — Holders — Good faith of holder
Plaintiff paid tenant to perform work on her property — Plaintiff gave tenant cheques with payee's name left blank for purchase of equipment, including cheque for $20,000 — Tenant gave $20,000 cheque to his lawyer, as payee, as payment for long-standing debt and as condition for retaining lawyer's services on new matters — Shortly before tenant was arrested for parole violations, plaintiff discovered that tenant had criminal record for fraudulent offences — Plaintiff brought action against payee for return of amount of cheque — Action dismissed — Trial judge held that payee was holder in due course — Payee took cheque as payment for bona fide debt and no evidence indicated that payee had not taken cheque in good faith — Plaintiff appealed — Appeal dismissed — Plaintiff argued that bill was payable to order rather than to bearer and accordingly required endorsement — Trial judge considered all these issues and reviewed law on both sides of argument — Trial judge made factual findings that payee satisfied three requirements of holder in due course: that he took bill in good faith, for value, and without notice of defect — There was no ground to interfere with those findings.

Table of Authorities

Statutes considered:

Bills of Exchange Act, R.S.C. 1985, c. B-4
s. 55(1)(b) — referred to

s. 59 — considered

s. 59(2) — referred to

APPEAL by plaintiff from judgment reported at *Ierullo v. Rovan* (2000), 2000 CarswellOnt 109, 46 O.R. (3d) 692, 3 B.L.R. (3d) 163 (Ont. S.C.J.), finding that payee was entitled to protection as holder in due course.

***Lang J.* (endorsement):**

1 We are of the opinion that on the findings of fact made by the trial judge, which findings he was entitled to make on the evidence before him, the appeal must fail.

2 The appellant argues that applying the law to the facts as found, Mr. Rovan did not satisfy the requirements of the Bills of Exchange Act for a holder in due course (s. 55(1)(b)), because the cheque was not "negotiated" to him. S. 59 provides that while a bill payable to bearer is "negotiated" by delivery (s. 59(2)), a bill payable to order can only be "negotiated" by the endorsement of the holder.

3 The appellant argues the bill was payable to order rather than to bearer and accordingly required the s. 59 endorsement. However Nordheimer J. considered all these issues and reviewed the law on both sides of the argument. He concluded that the Re Jones decision should not be followed in the circumstances of this case, although it can also be distinguished on the

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facts. Justice Nordheimer prepared the argument in the earlier cases and referenced in Crawford and Falconbridge that, particularly where a cheque is written in blank, the eventual "payee" is often, as he is in this case, a person unconnected to the payor and can be considered to be a remote party to the bill. We see no error in the trial judge's statement of the law and indeed we agree with his analysis on the facts of this case.

4 Nordheimer J. made factual findings that Mr. Rovan satisfied the 3 requirements of a holder in due course: that he took the bill in good faith, for value, without notice of defect. The trial judge appreciated that "the defendant must satisfy" these requirements. There was evidence upon which the trial judge could base his findings. We see no grounds upon which we would interfere with those findings.

5 Accordingly the appeal is dismissed. Costs to the respondent fixed at $1500.

Appeal dismissed.

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TAB 6

1992 CarswellBC 268
British Columbia Supreme Court

McDiarmid Lumber Ltd. v. Canadian Imperial Bank of Commerce

1992 CarswellBC 268, [1992] B.C.W.L.D. 2077, [1992] B.C.J. No. 1853, [1993] 1 W.W.R. 378, 46 E.T.R. 90, 71 B.C.L.R. (2d) 301, 94 D.L.R. (4th) 227

McDIARMID LUMBER LTD. v. CANADIAN IMPERIAL BANK OF COMMERCE

Collver J.

Heard: March 6, 1992
Judgment: August 7, 1992
Docket: Doc. Vancouver C914617

Counsel: *Nicole J. Garson*, for plaintiff.
Marcel J. Peerson, for defendant.

Subject: Estates and Trusts

Related Abridgment Classifications

Estates and trusts
II Trusts
II.3 Constructive trust
II.3.c Third person as constructive trustee

Headnote

Trusts and Trustees --- Constructive trust — Third person as constructive trustee

Trusts — Constructive trusts — Plaintiff mistakenly paying lumber supply account to another of its suppliers having a similar name — Supplier receiving payment depositing funds to bank account — Bank applying funds to supplier's line of credit in accordance with established practice — Bank having juristic reason for taking funds and not liable to plaintiff as constructive trustee or in damages for unjust enrichment.

Restitution — Unjust enrichment — Plaintiff mistakenly paying lumber supply account to another of its suppliers having a similar name — Supplier receiving payment depositing funds to bank account — Bank applying funds to supplier's line of credit in accordance with established practice — Bank having juristic reason for taking funds and not liable to plaintiff as constructive trustee or in damages for unjust enrichment.

Banking — Relationship between bank and third parties — Plaintiff mistakenly paying lumber supply account to another of its suppliers having a similar name — Supplier receiving payment depositing funds to bank account — Bank applying funds to supplier's line of credit in accordance with established practice — Bank having juristic reason for taking funds and not liable to plaintiff as constructive trustee or in damages for unjust enrichment.

The plaintiff routinely purchased building supplies from two unrelated companies with similar names. It purchased $24,339 worth of lumber from one of them and paid the other that sum by mistake. The recipient of the money was indebted to the defendant bank and its accounts receivable clerk did not detect the error. The funds were deposited to its account and the bank applied them to the company's line of credit in accordance with prevailing arrangements. By the time the plaintiff discovered its error, the company which had received the money was bankrupt. The plaintiff sued the bank for the money,

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relying on constructive trust and unjust enrichment.

Held:

Action dismissed.

There was an enrichment of the bank and a corresponding deprivation of the plaintiff. However, the bank had a legally enforceable right, a juristic reason, to take the money from the company's account. It did nothing objectionable by treating that deposit like all other deposits at the time. It was not liable to the plaintiff as a constructive trustee or in damages for unjust enrichment.

Table of Authorities

Cases considered:

Atlas Cabinets & Furniture Ltd. v. National Trust Co. (1990), 45 B.C.L.R. (2d) 99, 38 C.L.R. 106, 37 E.T.R. 16, 68 D.L.R. (4th) 161 (C.A.) — *considered*

Becker v. Pettkus, [1980] 2 S.C.R. 834, 19 R.F.L. (2d) 165, 8 E.T.R. 143, 117 D.L.R. (3d) 257, 34 N.R. 384 — *referred to*

Cherrington v. Mayhew's Perma-Plants Ltd., 45 B.C.L.R. (2d) 374, [1990] 5 W.W.R. 208, 37 E.T.R. 202, 71 D.L.R. (4th) 371 (C.A.) — *applied*

Hazlewood v. West Coast Securities Ltd. (1976), 49 D.L.R. (3d) 46 (B.C.S.C.) [varied on other grounds (1977), 68 D.L.R. (3d) 172 (B.C.C.A.)] — *distinguished*

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 — *considered*

Sorochan v. Sorochan, [1986] 2 S.C.R. 38, [1986] 5 W.W.R. 289, 46 Alta. L.R. (2d) 97, 2 R.F.L. (3d) 225, 29 D.L.R. (4th) 1, 69 N.R. 81, 23 E.T.R. 143, [1986] R.D.I. 448, [1986] R.D.F. 501, 74 A.R. 67 — *considered*

Statutes considered:

Bankruptcy Act, R.S.C. 1985, c. B-3 — *referred to*

Rules considered:

British Columbia Rules of Court, 1990

R. 18A

Words and phrases considered:

UNJUST

In Fridman and McLeod's Restitution (Toronto: Carswell, 1982), the authors attempt some indication of what "unjust" [in the context of "unjust enrichment"] means, at p. 55:

That means that it should not have been merited, desired or envisioned by the party at whose expense the enrichment occurred, and might even have been contrary to that party's knowledge or intentions. These elements of unjust enrichment are redolent with the characteristics of an approach based upon morality. It is a matter of debate whether the morality that is material is that of the "reasonable man", or that of the "reasonable judge". However, on general principles it might be thought that the task of judges is to interpret everyday morality with a view to giving it content and expression in terms of legal rules. Hence the purpose of the courts in developing the modern law of restitution is to seek to achieve a standard of just and

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correct behaviour that accords with what would be generally acceptable in the society in which the law and the courts function.

Action for declaration of constructive trust and for damages for unjust enrichment.

***Collver J.*:**

1 When a borrower deposits moneys it has received by mistake, and to which it has absolutely no entitlement, is its creditor, a bank which has no notice of the mistake or the lack of entitlement, obligated to return those moneys to the paying party?

2 That is the interesting question posed in this summary trial, conducted pursuant to R. 18A of the *Rules of Court*.

Facts

3 The plaintiff, McDiarmid Lumber Ltd. ("McDiarmid"), is a Winnipeg lumber retailer. McDiarmid regularly purchases products from Westcott Supply Canada Ltd. ("Westcott Alberta"), a Calgary building products supplier. From time to time, McDiarmid has also purchased products from Westcott Sales Limited ("Westcott B.C."), a Burnaby supplier. Westcott Alberta and Westcott B.C. are not related companies.

4 In early November 1990 McDiarmid placed an order with Westcott Alberta for lumber products worth $24,339.10.

5 In purporting to deal with the Westcott Alberta invoice after delivery, the McDiarmid accounts payable clerk mistakenly issued a cheque for $24,339.10 to Westcott B.C. Aside from the fact that McDiarmid had not dealt with Westcott B.C. for many months, when the cheque was issued McDiarmid was not then indebted to Westcott B.C.

6 The accounts receivable clerk at Westcott B.C. did not catch the payment error, and on January 7, 1991 McDiarmid's cheque was deposited in the account which Westcott B.C. then had with the defendant, the Canadian Imperial Bank of Commerce ("C.I.B.C.").

7 The money Westcott B.C. owed to C.I.B.C. reflected a substantial line of credit the bank had extended to Westcott B.C. In accordance with prevailing arrangements between Westcott B.C. and C.I.B.C., the January 7, 1991 deposit was simply applied to reduce the balance owing.

8 During the next two weeks Westcott B.C. deposited and withdrew varying amounts (greater than $24,339.10) into and from its C.I.B.C. account. But on January 22, 1991 C.I.B.C. began realization of its security by appointing Peat Marwick Thorne Inc. ("Peat Marwick") as a receiver-manager.

9 On February 4, 1991 C.I.B.C. filed a petition against Westcott B.C. under the *Bankruptcy Act* [R.S.C. 1985, c. B-3], and on February 13, 1991 a receiving order was granted, adjudging Westcott B.C. bankrupt.

10 McDiarmid's solicitors wrote to Peat Marwick, and then to the bank's solicitors, hoping to recover the $24,339.10 mistakenly deposited by Westcott B.C. When those efforts failed, these proceedings were commenced.

11 McDiarmid acknowledges that C.I.B.C. will incur a significant shortfall (many times greater than $24,339.10) on recovery of moneys the bank loaned to Westcott B.C., and that C.I.B.C. had no knowledge of either McDiarmid's mistaken payment or Westcott B.C.'s error in depositing the McDiarmid cheque.

Issues

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12 1. Does C.I.B.C. hold $24,339.10 as a constructive trustee for McDiarmid?

13 2. Should C.I.B.C. be ordered to pay or deliver the alleged trust fund to McDiarmid?

14 3. Alternatively, are damages of $24,339.10 payable to McDiarmid by C.I.B.C.?

Submissions

15 McDiarmid asserts entitlement to a proprietary remedy on the basis that its payment to Westcott B.C. was made under a mistake of fact. Submitting that the bank's retention of the wrongfully deposited funds would constitute unjust enrichment, the remedy the plaintiff seeks is imposition of a constructive trust.

16 On the other hand, the bank submits that in the absence of either knowledge of the relationship between McDiarmid and Westcott B.C., or notice as to Westcott B.C.'s lack of entitlement to the cheque it deposited, C.I.B.C. cannot be found to be a trustee of the funds.

17 Furthermore, the bank submits that the existence of Westcott B.C.'s debt to the bank provides a juristic reason for finding that C.I.B.C. has not been unjustly enriched by its receipt of the funds.

Discussion

18 Even though it was the plaintiff's own mistake which gave rise to these proceedings, the deposit of funds to which Westcott B.C. had no entitlement encourages some sympathy for the plaintiff's position. That, however, does not entitle the plaintiff to the requested relief.

19 In her submission, plaintiff's counsel emphasized that in seeking an in rem remedy, through the imposition of a constructive trust, the mistakenly paid funds can be traced into the account of Westcott B.C. at the defendant's bank. In the alternative, damages are sought, also on the basis of unjust enrichment.

20 The remedy of constructive trust has been the subject of considerable comment in several recent decisions of the Supreme Court of Canada.

21 In *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, Dickson J. (as he then was) established the following test for finding a constructive trust, at S.C.R. p. 455:

> ... for the principle to succeed, the facts must display an enrichment, a corresponding deprivation, and the absence of any juristic reason — such as a contract or disposition of law — for the enrichment.

The above test was affirmed in *Becker v. Pettkus*, [1980] 2 S.C.R. 834, 19 R.F.L. (2d) 165, 8 E.T.R. 143, 117 D.L.R. (3d) 257, 34 N.R. 384, and *Sorochan v. Sorochan*, [1986] 2 S.C.R. 38, [1986] 5 W.W.R. 289, 46 Alta. L.R. (2d) 97, 2 R.F.L. (3d) 225, 29 D.L.R. (4th) 1, 69 N.R. 81, 23 E.T.R. 143, [1986] R.D.I. 448, [1986] R.D.F. 501, 74 A.R. 67. In *Sorochan*, Dickson C.J.C. said, at p. 44 [S.C.R.]:

> Before a constructive trust can be imposed in this case, the Court must find that there has been an unjust enrichment. In *Pettkus* and *Rathwell*, the Court outlined three requirements [set out above] that must be satisfied before it can be said that an unjust enrichment exists.

The effect of these cases is to establish that the Supreme Court of Canada has not made the test for a constructive trust any more onerous than for a finding of unjust enrichment which would entitle a plaintiff to damages.

22 Here, there is clearly an enrichment by C.I.B.C., and a corresponding deprivation of McDiarmid. However, I question the plaintiff's contention that there is the absence of juristic reason for the enrichment, having regard to the relationship between the defendant bank and its customer, Westcott B.C.

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23 Concentration on the mistakes of the plaintiff and Westcott B.C. (and the prospect of the plaintiff having to pay twice for its Calgary order) tends to overlook the consequences of now ordering the defendant bank to pay out moneys which, in the absence of any indication as to impropriety of the deposit, it had every right to credit to the depositor's debt. In the context of normal banking arrangements, what is unjust about the bank's reliance upon the depositor's entitlement at the time that the debt was credited?

24 In Fridman and McLeod's *Restitution* (Toronto: Carswell, 1982), the authors attempt some indication of what "unjust" means, at p. 55:

> That means that it should not have been merited, desired or envisioned by the party at whose expense the enrichment occurred, and might even have been contrary to that party's knowledge or intentions. These elements of unjust enrichment are redolent with the characteristics of an approach based upon morality. It is a matter of debate whether the morality that is material is that of the "reasonable man", or that of the "reasonable judge".However, on general principles it might be thought that the task of judges is to interpret everyday morality with a view to giving it content and expression in terms of legal rules. Hence the purpose of the courts in developing the modern law of restitution is to seek to achieve a standard of just and correct behaviour that accords with what would be generally acceptable in the society in which the law and the courts function.

25 In *Atlas Cabinets & Furniture Ltd. v. National Trust Co.* (1990), 45 B.C.L.R. (2d) 99, 38 C.L.R. 106, 37 E.T.R. 16, 68 D.L.R. (4th) 161 (C.A.), Lambert J.A. made the following point about the "unjust" part of the test in the context of commercial cases, at p. 110 [B.C.L.R.]:

> In my opinion the concept of the injustice of the enrichment as being against sound commercial conscience must continue to guide the application of the three tests in *Pettkus v. Becker* when they are applied to a commercial relationship.

26 A dilemma similar to that facing C.I.B.C. in the present case confronted a creditor in *Cherrington v. Mayhew's Perma-Plants Ltd.*, 45 B.C.L.R. (2d) 374, [1990] 5 W.W.R. 208, 37 E.T.R. 202, 71 D.L.R. (4th) 371 (C.A.). There, the court was faced with the plaintiff law firm's claim that fraudulent diversion of just under $25,000 of its funds by one of its employees (one Barbara Cochran, the firm's accountant) to pay the employee's outside business debts, unjustly enriched the defendant, the employee's creditor. The trial judge found that the defendant had been enriched, the plaintiff had been deprived, and that (at p. 377) [B.C.L.R.]:

> There is no juristic reason for the enrichment, that is to say, the plaintiffs were under no obligation, contractual or otherwise, to the defendant. It is an enrichment where the fraudswoman's use of the cheque was not the cause of loss to the defendant. The relevant loss pre-dated the cheque.
>
> When this bad debt was paid unintentionally by the plaintiffs without any obligation to do so, the recipient was enriched at a cost to the plaintiffs.

The Honourable Mr. Justice Hollinrake, after referring to the three part test in *Sorochan*, supra, rejected the ultimate finding of unjust enrichment at trial and commented, at p. 378:

> I do not think juristic reason in the context of this case depends on any obligation or relationship as between the respondents and the appellant.
>
> What the appellant in this case must show is that there was a juristic reason for the funds coming into its hands. That juristic reason is the debt owed by Cochran and her company to the appellant. There is no suggestion that this debt was other than enforceable at the time.

27 In the present case, is C.I.B.C. entitled to similar protection by reason of the debt owing to it by Westcott B.C., and the innocent manner in which it simply credited the questioned deposit to that debt?

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28 I have concluded that C.I.B.C. had a legally enforceable right, a juristic reason, to take the money from Westcott B.C.'s account. It did nothing objectionable by treating the January 7, 1991 deposit like any and all other deposits which Westcott B.C. was then making.

29 The above conclusion is, of course, also pertinent to McDiarmid's damages claim, referred to earlier in these reasons.

30 Restitutionary damages, based upon unjust enrichment, were awarded on a claim for money had and received, in *Hazlewood v. West Coast Securities Ltd.* (1976), 49 D.L.R. (3d) 46 (B.C.S.C.). Like *Cherington*, supra, *Hazlewood* is a case arising from the dishonesty of an employee. In *Hazlewood*, the employee, Hunter, who was also a director of the defendant firm of stockbrokers, misappropriated funds advanced by the plaintiff by fraudulently representing the funds as his own when he deposited them in the defendant's general account. The funds were ultimately used by the defendant to cover both Hunter's personal indebtedness to the defendant, and the defendant's obligations to others, arising from Hunter's fraud.

31 The trial judge in *Hazlewood* made a distinction between company law and the law of restitution. On an application of company law, the defendant principal was not liable on the transactions fraudulently entered into by Hunter. For the purposes of restitution law, the trial judge allowed the plaintiff to recover only the portion of moneys used to reduce Hunter's indebtedness to the defendant. He decided that as between the two innocent parties, it would be against conscience for the defendant principal to retain the benefit obtained by the wrongful actions of its agent.

32 Fridman and McLeod discuss cases in the nature of *Hazlewood* in their text at p. 439:

> ... for the purposes of the law of restitution at least, the prejudicial conduct of those persons in *de facto* managerial control of a corporation should be recognized as that of the corporation itself and a person who unofficiously renders services, because of the actions of the people in *de facto* control should not be denied recovery. As an internal management matter, the shareholders and the corporation itself will invariably have an action against the "directors" who acted outside the scope of authority.

33 There is no principal/agent or employer/employee relationship between Westcott B.C. and C.I.B.C. Accordingly, *Hazlewood* has no application in the present case.

Decision

34 Since C.I.B.C. has not been unjustly enriched by reason of either McDiarmid's mistake in issuing its cheque, or Westcott B.C.'s mistake in depositing it, the bank neither holds funds as a constructive trustee for McDiarmid, nor is liable to McDiarmid in damages. McDiarmid's claim is therefore dismissed, with scale 3 costs payable to C.I.B.C.

Action dismissed.

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TAB 7

1998 CarswellBC 23
British Columbia Court of Appeal

Toronto Dominion Bank v. Carotenuto

1998 CarswellBC 23, [1998] 9 W.W.R. 254, [1998] B.C.J. No. 10, 101 B.C.A.C. 216, 154 D.L.R. (4th) 627, 164 W.A.C. 216, 48 B.C.L.R. (3d) 284, 76 A.C.W.S. (3d) 655

The Toronto-Dominion Bank, Plaintiff (Appellant) and Tony Carotenuto, Avanti Hair Design Ltd. Bob Tom Holdings Ltd., Robert Tomljenovich, Peter Pan and Kim Loranger, Defendants (Respondents)

The Toronto-Dominion Bank, Plaintiff (Respondent) and Tony Carotenuto, Avanti Hair Design Ltd. Bob Tom Holdings Ltd., Robert Tomljenovich, Peter Pan and Kim Loranger, Defendants (Appellants)

Ryan, Donald, Newbury JJ.A.

Heard: November 21, 1997
Judgment: January 8, 1998
Docket: Vancouver CA022551, CA022559

Proceedings: reversing (October 29, 1996), Doc. Vancouver C957125 (B.C.S.C.)

Counsel: *J.D. Shields*, for the Plaintiff/Appellant, Toronto-Dominion Bank.
D.J. Barker, for the Defendants/Respondents Peter Pan and Kim Loranger.

Subject: Civil Practice and Procedure; Corporate and Commercial; Restitution; Estates and Trusts

Related Abridgment Classifications

Civil practice and procedure
XX Trials
XX.8 Summary trial
XX.8.b Evidence
XX.8.b.iv Miscellaneous

Estates and trusts
II Trusts
II.3 Constructive trust
II.3.c Third person as constructive trustee

Restitution and unjust enrichment
I General principles
I.2 Requirements for unjust enrichment
I.2.c No juristic reason for enrichment

Restitution and unjust enrichment
VI Benefits arising through wrongful acts
VI.2 Money or goods inequitably retained

Headnote

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Trials — Summary trial — Availability
Businessman presented bank with uncertified cheques to cover bank drafts to repay investors — Businessman assured bank of sufficient funds — Bank issued drafts and investors deposited drafts and received funds — Cheques did not clear and bank successfully sued businessman for fraud — Bank sued investors for unjust enrichment, money had and received, damages for conversion and constructive trust — Bank applied under R. 18A for judgment and investors applied under same rule for dismissal of action — Bank objected to admissibility of investors' evidence — Trial judge found insufficient evidence to decide issues on summary basis and dismissed both applications — Bank and investors appealed and sought determination of bank's claims without full trial — Trial judge erred in ruling that impugned evidence inadmissible because this evidence admissible as "operative words" and "words which, when spoken, effect a legal result" — Summary judgment granted — British Columbia, Rules of Court, 1990, R. 18A.

Benefits arising through wrongful acts — Money or goods inequitably retained
Businessman presented bank with uncertified cheques to cover bank drafts to repay investors — Businessman assured bank of sufficient funds — Bank issued drafts and investors deposited drafts and received funds — Cheques did not clear and bank successfully sued businessman for fraud — Bank sued investors for unjust enrichment, money had and received, damages for conversion and constructive trust — Bank applied under R. 18A for judgment and investors applied under same rule for dismissal of action — Trial judge found insufficient evidence to decide issues on summary basis and dismissed both applications — Bank and investors appealed and sought determination of bank's claims without full trial — None of required circumstances of action for money had and received existed, as all parties intended investors to receive funds as their own and bank intended to honour drafts — Tort of conversion required bank to remain "owner" either of funds or drafts to succeed — Bank did not remain owner because it paid out funds to investors — Summary judgment granted — British Columbia, Rules of Court, 1990, R. 18A.

Constructive trust — Miscellaneous issues
Businessman presented bank with uncertified cheques to cover bank drafts to repay investors — Businessman assured bank of sufficient funds — Bank issued drafts and investors deposited drafts and received funds — Cheques did not clear and bank successfully sued businessman for fraud — Bank sued investors for unjust enrichment, money had and received, damages for conversion and constructive trust — Bank applied under R. 18A for judgment and investors applied under same rule for dismissal of action — Bank objected to admissibility of investors' evidence — Trial judge found insufficient evidence to decide issues on summary basis and dismissed both applications — Bank and investors appealed and sought determination of bank's claims without full trial — Bank did not provide analysis as to why constructive trust should be imposed — No other basis for grant of such remedy shown because bank acknowledged inability to prove any fraudulent intention on part of investors — Summary judgment granted — British Columbia, Rules of Court, 1990, R. 18A.

Table of Authorities

Cases considered by *Newbury J.A.*:

Arrow Transfer Co. v. Royal Bank, [1971] 3 W.W.R. 241, 19 D.L.R. (3d) 420 (B.C. C.A.) — referred to

Bruyninckx v. Bruyninckx, 4 B.C.L.R. (3d) 341, [1995] 5 W.W.R. 683, 13 R.F.L. (4th) 199, 7 E.T.R. (2d) 1, 57 B.C.A.C. 1, 94 W.A.C. 1 (B.C. C.A.) — referred to

Cherrington v. Mayhew's Perma Plants Ltd., 45 B.C.L.R. (2d) 374, 71 D.L.R. (4th) 371, [1990] 5 W.W.R. 208, 37 E.T.R. 202 (B.C. C.A.) — considered

Gallen v. Allstate Grain Co. (1984), 25 B.L.R. 314, 9 D.L.R. (4th) 496, 53 B.C.L.R. 38 (B.C. C.A.) — referred to

Peter v. Beblow, [1993] 3 W.W.R. 337, 23 B.C.A.C. 81, 39 W.A.C. 81, 101 D.L.R. (4th) 621, [1993] 1 S.C.R. 980, 150 N.R. 1, 48 E.T.R. 1, 77 B.C.L.R. (2d) 1, 44 R.F.L. (3d) 329, [1993] R.D.F. 369 (S.C.C.) — referred to

R.E. Jones Ltd. v. Waring & Gillow Ltd., [1926] A.C. 670, [1926] All E.R. Rep. 36 (U.K. H.L.) — referred to

Royal Bank v. Harowitz (1994), 17 O.R. (3d) 671 (Ont. Gen. Div.) — considered

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Statutes considered:

Bills of Exchange Act, R.S.C. 1985, c. B-4
s. 56 — referred to

s. 59(1) — referred to

Rules considered:

Rules of Court, 1990, B.C. Reg. 221/90
R. 18A — considered

R. 18A(11)(a)(ii) — considered

R. 31(6) — referred to

APPEAL by bank and investors from trial judge's dismissal of application for summary judgment.

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

1 This appeal arises from a set of facts reminiscent of a law school examination question: they involve a rogue (the defendant Mr. Carotenuto); two apparently innocent individuals (the defendants Mr. Pan and Ms. Loranger) whom he persuaded to invest a total of $500,000 in a real estate venture that in fact never materialized; and a naive and overly enthusiastic bank manager who was duped into issuing bank drafts for $500,000 on the strength of Mr. Carotenuto's promises. As in most law school examination questions, the fraudsman is now nowhere to be found, and it falls to the court to decide on whom the loss occasioned by his dishonesty should fall. To complete the analogy, one of the two major legal issues in the case is a longstanding "chestnut" in banking law that has been debated in learned articles and treatises but not directly considered by a court in Canada since prior to 1926, the date of a controversial House of Lords' decision on the point.

Factual Background

2 The facts can be recounted from two viewpoints — that of the plaintiff Toronto-Dominion Bank (the "Bank") and that of Mr. Pan and Ms. Loranger (whom I will refer to as the "Respondents"). From the Bank's viewpoint, the narrative begins in late October 1995. Around that time Mr. Carotenuto had succeeded in impressing an acting branch manager of the Bank, Mr. Farquharson, with his apparent success in business and knowledge of international banking matters. Viewing Mr. Carotenuto as a potential source of new business for the Bank, Mr. Farquharson agreed to provide him with bank drafts totalling $725,000 payable to a company controlled by one of Mr. Carotenuto's associates. In return Mr. Carotenuto handed Mr. Farquharson a cheque for $725,000 drawn on the account of Score's Sports Café Inc., one of his companies, and assured him it would be covered the following day. In fact the account had insufficient funds to cover the cheque the next day. Eventually however, Mr. Farquharson received a draft from Mr. Carotenuto drawn on another bank in the required amount.

3 Some days later, in November 1995, Mr. Farquharson agreed to consider Mr. Carotenuto's request for another $500,000 which he said he wanted in order to repay a loan owing to two individuals who had invested in a real estate project. In due course, Mr. Farquharson agreed to provide Mr. Carotenuto with two drafts totalling $500,000 in return for cheques payable to the Bank in the same amount, drawn by another of Mr. Carotenuto's companies, Avanti Hair Design Ltd. ("Avanti"). Mr. Farquharson was aware that Avanti's accounts did not have funds sufficient to cover the cheques at the time the drafts were issued, but he accepted Mr. Carotenuto's promise that the necessary funds would be in those accounts by the next day, November 22. Accordingly, one bank draft in the amount of $350,000 payable to Peter Pan, and one in the amount of $150,000 payable to Kim Loranger, were delivered to Mr. Carotenuto, who in turn handed them to Mr. Pan and Mr. Young (Ms. Loranger's common-law husband) respectively. They deposited the drafts immediately to their accounts at their respective credit unions.

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4 From the point of view of the Respondents, the narrative begins in March 1995, when each of them was persuaded to advance funds to Mr. Carotenuto for the purpose of investing in real estate projects in which he was somehow involved. Mr. Pan advanced $350,000, much of which was provided by a friend; and Ms. Loranger advanced $150,000, most of which came from Mr. Young or his construction company. (In my view, nothing turns on the fact that the investments were made in the names of Mr. Pan and Ms. Loranger respectively.) In evidence of each investment, Mr. Carotenuto produced a one-page acknowledgment on the letterhead of "Westlynn Construction Corp.", which referred to an "end date" a year later, in March 1996. Subject to minor variations, each document said that the investment would "yield a return of initial investment plus bonus + profits on completion of projects." Each document was signed by Mr. Carotenuto and by one Bob Tomljenovich, a defendant herein, for "Bob Tom Holdings". Neither Mr. Pan, Mr. Young nor Ms. Loranger knew Mr. Tomljenovich or his company, and none knew anything about Westlynn Construction Corp. or "Westlynn Dev.", the name that was inserted as the payee of Mr. Pan's cheque.

5 On or about November 22, 1995, Mr. Carotenuto contacted Mr. Young and Mr. Pan to advise that the projects in which their money was to have been invested had 'fallen through'. According to Mr. Young's evidence:

> Tony [Mr. Carotenuto] offered to repay me my initial investment of $150,000. I asked him whether I would get any interest on this money but he said no, I would not. I was disappointed because I had let Tony use this money for several months and I was not going to receive any interest at all. Tony explained that there was this guy, whose name I think is Henry Peters, who had taken off with some money and that the projects were in jeopardy. He further said I should consider myself lucky to get my money back. Since I understood my investment to be dependent on the success of the projects, I felt that the whole purpose of my investment had been frustrated. I then told Tony that if I got my principal back I would not ask him to pay me any interest. He said that that would be alright and apologized to me that things did not work out adding that he would find new projects to invest in. Tony said he could give me a bank draft in the next couple of days and he asked me who it should be made payable to. I asked him to make the draft payable to Kim Loranger.
>
> On or about November 22, 1995, Tony handed me a bank draft for $150,000 payable to Kim Loranger. ...

Mr. Young deposited Ms. Loranger's draft to the couple's account on November 23. Mr. Pan also received a bank draft in the amount of his investment, which he deposited on November 22, 1995.

6 Needless to say, these were the drafts that had been provided by the Bank to Mr. Carotenuto on the understanding that funds would be in Avanti's account on November 23 to cover the cheques that had been handed to Mr. Farquharson. Perhaps also needless to say, the cheques failed to clear on that date or any subsequent date, due to insufficient funds. The Bank did not take any steps, however, to stop payment on the drafts that had been issued to Mr. Pan and Ms. Loranger. It was not until six weeks later that the Bank contacted their respective credit unions concerning alleged improprieties in connection with the issuance of the drafts.

Proceedings in the Court Below

7 The Bank commenced its action in Supreme Court in early 1996 against *inter alia* Mr. Pan and Ms. Loranger, against whom it advanced claims for unjust enrichment, money had and received, damages for conversion, and constructive trust. In their pleadings, Mr. Pan and Ms. Loranger denied the claims generally and sought the protection accorded to holders in due course by s. 56 of the *Bills of Exchange Act*, R.S.C. 1985, c. B-4. On May 2, both Mr. Pan and Ms. Loranger moved to have the Bank's claim dismissed under R. 18A - an application followed by the Bank's application for judgment against Mr. Pan in the amount of $350,000 and against Ms. Loranger in the amount of $150,000, pursuant to R. 31(6). By this time, the Bank had succeeded in obtaining a judgment (which is presumably a dry one) for fraud against Mr. Carotenuto and Avanti in the amount of $500,000, interest and costs.

8 The two applications for summary determination were heard in September 1996. On October 29, the Chambers judge issued reasons (Vancouver Registry No. C957125) declining to decide the action summarily and remitting it to the trial list. After noting counsels' lengthy submissions on the "holder in due course" issue, she adverted to various deficiencies in the evidence before the court:

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> For example, in an affidavit filed on May 2, 1996, in support of the defendants' motion, Peter Pan deposed, in part, at paragraph 7:
>
> > ... Mr. Carotenuto told me at the time that when the chosen project was completed I would get my money back as well as any bonus and share of profits. He told me that this would not take more than 12 months. I trusted Mr. Carotenuto to make sure that my investment was safe. While we never discussed what would happen if the project did not go ahead or was terminated, I always assumed that I would get my principal back.
>
> At paragraph 8 Mr. Pan deposed:
>
> > I was contacted by Mr. Carotenuto over the telephone in November, 1995. He left a message on my answering machine on November 22, 1995 that he had my cheque. After getting that message I drove to Scores Restaurant and he told me that he was sorry but that the deal had fallen through. ...
>
> It is clear that portions of those two passages offend the hearsay rule. Counsel for Mr. Pan argued that the statements were tendered, not for the truth of the contents of the statement, but for the purpose of determining Mr. Pan's state of mind at the time in question. That may be a legitimate reason to admit the evidence, but I was not persuaded that the foundation for admitting the evidence was properly laid.
>
> A similar objection arose with respect to the evidence of Tim Young. In Mr. Young's affidavit filed May 2, 1996, at paragraph 17, he deposed:
>
> > Sometime in November, 1995, Tony [Carotenuto] told me that there was a problem and the projects he had invested my money in were not going ahead. He never specified which projects and I never knew which projects my money was invested in. Tony offered to repay me my initial investment of $150,000. I asked him whether I would get any interest on this money but he said no, I would not. I was disappointed because I had let Tony use this money for several months and I was not going to receive any interest at all. ... I then told Tony that if I got my principal back I would not ask him to pay me any interest. He said that that would be alright and apologized to me that things did not work out adding that he would find new projects to invest in. Tony said he could give me a bank draft in the next couple of days and he asked me who it should be made payable to. I asked him to make the draft payable to Kim Loranger.
>
> Since no interest was payable under the agreement between Carotenuto and Loranger, to suggest, as is done in paragraph 17, that Loranger and/or Young agreed to forego the payment of interest in return for the repayment of principal, offends the parol evidence rule. The only useful purpose of such evidence would be to support the contention that there was consideration given for the early repayment of the loan.
>
> These passages from the evidence filed in support of the defendants' motions demonstrate a lack of care and precision which properly attracted the objections of counsel for the bank. Further, the objections, if upheld, would mean that there was insufficient evidence to establish the necessary *indicia* of good faith, value, and notice for the defendants to succeed on their motions. [paras. 18-20]

In the result, the Chambers Judge said she could not be fully confident that all relevant evidence had been put before the Court and that she was uncertain as to her ability to find the facts necessary to decide the issues of fact and law. More importantly, she concluded, it would be unjust to decide the issues before the Court on the application, as is required by R. 18A(11) (a) (ii). In the words of the Chambers judge:

> Having particular regard to the amount involved and the complexity of the matter, I conclude that it would be unjust to give judgment under Rule 18A. If there is evidence sufficient to establish good faith, value and notice, then Pan and Loranger ought to be given the opportunity to present such evidence in order to defend the claims against them. It is, of course, stating the obvious that such evidence should have been properly presented on their motion for summary trial. [para. 23]

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The Appeals

9 Notwithstanding the Chambers judge's comments regarding the disarray of the evidence, both the Bank and the Respondents have appealed the Court's ruling. Both seek a determination by this court of the Bank's claims without a full-blown trial. In particular, Mr. Shields on behalf of the Bank acknowledged on appeal that if a trial were held, he would be *unable* to prove that the Respondents had not been "innocent" of any involvement in Mr. Carotenuto's fraud; and Mr. Barker on behalf of the Respondents urged us to decide as a matter of law, on the affidavit evidence adduced before the court below, that his clients have no liability to the Bank — despite the observation of the Chambers judge that "If this were a trial, the defendants would, on the basis of the clearly admissible evidence before the court, fail." In short, none of the parties to this appeal wishes the opportunity given to them by the Chambers judge to marshall further evidence or refine the manner in which it was presented. Equally important for our purposes, they emphasize that there are no material conflicts in the affidavit evidence as to the facts of the case. In these circumstances, there seems little point in forcing the parties through the time and expense of a full trial.

10 Counsel do not agree, however, on the admissibility of the evidence that was excluded by the Chambers judge as hearsay and as offending the parol evidence rule. That evidence was adduced by the Respondents to prove the general circumstances of their deposit of the bank drafts and more particularly, what they understood was the reason for Mr. Carotenuto's return of their funds to them before the one-year investment period had expired. Counsel for the Bank argued that the evidence had been properly excluded, and that because it was incumbent on the Respondents to prove a "juristic reason" for their receipt of the funds (insofar as the claim for unjust enrichment is concerned) or to prove that they had given "value" for the drafts (insofar as the defence based on the *Bills of Exchange Act* is concerned), the Respondents had failed to make out a crucial part of their defence. (As to the onus of proof in the unjust enrichment claim, see para. 13 below.)

11 I agree that the impugned evidence is an important part of the defence, but I do not agree that it was hearsay or inadmissible on any other basis. As I understand it, the recollections of Mr. Pan and Mr. Young as to their conversations with Mr. Carotenuto on or about November 22, 1995 were not adduced for the purpose of proving the truth of Mr. Carotenuto's statements; rather, they were adduced to prove that the Respondents had been given to understand, and did understand, that because the alleged real estate projects had fallen through, they were to receive their money back early. It may well be that Mr. Carotenuto was not being truthful, but if the Defendants *understood* that the bank drafts they received represented the return of their investments, that understanding is relevant to the existence of a juristic reason for their enrichment.

12 As for the Respondents' acceptance of their original principal without interest, effectively in satisfaction of all Mr. Carotenuto's obligations to them, it seems to me that whether the parties were in a debtor-creditor relationship (as counsel assumed) or whether Mr. Carotenuto was a trustee of the Respondents' funds, the conversations are admissible as "operative words" or (to quote Sopinka, Lederman and Bryant in *The Law of Evidence in Canada* (1992), "words which, when spoken, effect a legal result." (at 236) Nor in my view is the parol evidence rule engaged with respect to Mr. Young's advice to Mr. Carotenuto that it would be "alright" if Mr. Carotenuto repaid his money without interest. This "agreement" about interest would constitute a collateral or amending agreement (see the comments of Lambert J.A. in *Gallen v. Allstate Grain Co.* (1984), 9 D.L.R. (4th) 496 (B.C. C.A.) at 506-7) rather than an oral term of an otherwise complete written agreement. Accordingly, I find that the Chambers judge erred in ruling the evidence of Mr. Young and Mr. Pan as to their conversations with Mr. Carotenuto on November 22 inadmissible, although one may share her concerns about the "lack of care and precision" that characterized the manner in which the evidence was adduced.

Unjust Enrichment

13 I turn, then, to the questions of law raised by the uncontradicted affidavit evidence previously excluded by the court below. The first issue is whether the Respondents were unjustly enriched by their receipt of the bank drafts or the funds for which they were exchanged. It is by now trite law that an action for unjust enrichment involves proof of three elements — an enrichment; a corresponding deprivation; and the absence of a juristic reason for the enrichment: see *Peter v. Beblow*, [1993] 1 S.C.R. 980 (S.C.C.). (Contrary to Mr. Shields' argument described above at para. 10 above, the onus of proof of all three elements lies on the Bank.) There is no doubt in this case that the Respondents were "enriched" by the return of their funds, nor that the Bank was "deprived" of $500,000 by the transactions that occurred on November 22, 1995. Was there a juristic

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reason for the enrichment? Mr. Shields argued that there was not for many reasons — the fact that Mr. Carotenuto had obtained the funds (or more precisely the drafts) by a fraud on the Bank; the fact that the Respondents had not expected payment in November 1995 and in Mr. Shields' submission were not "entitled" to payment at that time; and the fact the Bank had "no obligation" to pay the Respondents anything and received no consideration from them in return for the drafts. These arguments tended to merge in counsels' submissions with arguments relating to the alternate "holder in due course" issue, an issue that arises only if it is found that the Respondents were unjustly enriched or are otherwise liable to the Bank. On that issue, Mr. Shields argued at length that the bank drafts were not "negotiated" within the meaning of s. 59(1) of the *Bills of Exchange Act*, and that the Respondents could not be said to have given "value" for the drafts.

14 It is important, however, to keep the question of unjust enrichment separate from that of the meaning of "holder in due course" under the *Bills of Exchange Act*. In particular, it is important to keep in mind that "juristic reason" is a much broader concept than that of the value or consideration moving from the Respondents either to the Bank or to Mr. Carotenuto. In this regard, I note the comments of McLachlin J. for the majority in *Peter v. Beblow*, *supra*:

> 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. ...
>
> In every case, the fundamental concern is the legitimate expectation of the parties. ... [at 990]

No authority was cited to us that requires as a condition of the "juristic reason" in an action for unjust enrichment that a contractual obligation have existed between the payor and ultimate payee. Indeed, there is authority of this court to the contrary: in *Cherrington v. Mayhew's Perma Plants Ltd.* (1990), 45 B.C.L.R. (2d) 374 (B.C. C.A.), it was held that the presence of a juristic reason was not dependent "on any obligation or relationship as between the respondents and the appellant." (at 378) Thus a "juristic reason" was held to exist for the appellant's receipt of funds in *Cherrington* because the fraudulent actor had owed money to the recipient of the funds misappropriated from the respondents. Similarly, in *Royal Bank v. Harowitz* (1994), 17 O.R. (3d) 671 (Ont. Gen. Div.), a lender who had demanded and received repayment of her loan from a borrower who had obtained the funds by perpetrating a fraud on his bank, was held to have had a juristic reason for receiving the funds. The Court characterized as "absurd" the suggestion that "the juristic reason must always be tied irrevocably to the person who asserts the unjust enrichment." (at 682)

15 Mr. Shields notes, however, that the Court went on in *Cherrington* to add that there had been no suggestion that the debt was "other than enforceable at the time" of payment and that in *Harowitz*, the lender had made demand on her promissory note. Mr. Shields contrasts those situations with that of the Respondents who, he says, could not have sued Mr. Carotenuto for the return their funds before the expiration of the one-year period referred to in the one-page "agreements". Again, however, I am not persuaded that the existence of a "juristic reason" requires an enforceable obligation at the time of payment. In this case, Mr. Carotenuto had notified the Respondents that their agreements with him were effectively frustrated — the real estate projects that were the purpose of their investment had fallen through. (If the agreements gave rise to trusts, their purpose had fallen away and they were being terminated.) In these circumstances, the Respondents had, it seems to me, a commercially reasonable expectation of receiving their money back when they did, and perhaps even an "entitlement" to it. (Indeed, if the trust analogy is correct, they were receiving back their own funds.) This expectation, coupled with the documentary proof of their investments and the return of the same amount of money to them, support the inference that they were in fact receiving the return of their investments, and not, as Mr. Shields suggested, a gift or "windfall" payment from Mr. Carotenuto. In the absence of any evidence that the Respondents were not acting *bona fide*, then, one may reasonably conclude that there was a legitimate "juristic reason" for the Respondents' "enrichment". Conversely, the Bank fully expected to pay the funds to the Respondents when it did — its "mistake" did not relate to the nature of the drafts or the identity of the payees. It is not reasonable for it to expect that it may now change its mind about honouring the drafts because of a fraud in which the Respondents have not been shown to have participated.

16 By the same token, I would reject Mr. Barker's argument that the question of unjust enrichment should be coloured by the "relative positions of the parties" (i.e., the fact that "the Bank is certainly in a better position to absorb the loss in all of the circumstances"), and by the fact that the branch manager consciously "took a risk" in providing the drafts to Mr. Carotenuto. All the parties in this case took risks and questions of unjust enrichment are not decided according to which party has deeper pockets or greater assets.

Money had and Received/Conversion

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17 The balance of the Bank's claims were touched upon only briefly by counsel in his factum and oral argument, and the claims for conversion and 'money had and received' were treated as if they were interchangeable. In fact the two causes of action have different origins — the action for money had and received arises out of contract law and is now regarded as a restitutionary remedy; while conversion is a longstanding tort usually involving wrongful interference with goods, but also applied to funds or to instruments representing funds. (See the learned judgment of Robertson J.A. in *Arrow Transfer Co. v. Royal Bank*, [1971] 3 W.W.R. 241 (B.C. C.A.) at 255-261.) It appears, however, that neither cause of action lies in the case at bar. In general, the essence of the action for money had and received is that the defendant was under a liability to account to the plaintiff in respect of a benefit which the defendant received from a third person (*Halsbury's Laws of England*, 4th ed., v. 9 at para. 675). This may occur where the defendant has promised to pay to the plaintiff funds belonging to another person, but has neglected to do so; where the defendant is a stakeholder for both the plaintiff and the third party; where the defendant is an agent or employee of the plaintiff; or where the defendant has usurped an office belonging to the plaintiff: *Halsbury's*, *supra*. None of those circumstances exists in this case, as indeed Mr. Pan and Ms. Loranger were intended by all parties at the time to receive the funds in question as their own and conversely, the Bank intended to, and did, honour the drafts when they were presented.

18 The essence of the tort of conversion, which is a strict liability tort, is a "wrongful act of dealing with the goods of another in a manner inconsistent with the owner's rights". (*Halsbury's*, *supra*, v. 45 at para. 1422) Again, I do not think it can be said that the Bank remained the "owner" either of the drafts or the funds they represented. The Bank was aware that Mr. Carotenuto intended to hand the drafts over to the Respondents, and it honoured the drafts by paying the funds over to the Respondents' credit unions on presentment.

19 I would therefore dismiss the Bank's claims for conversion and for money had and received insofar as the Respondents are concerned.

Constructive Trust

20 Apart from a bare assertion that "Pan and Loranger hold the Bank's funds as constructive trustees and the Bank is entitled to an order for the return of those funds" and a reference to *Bruyninckx v. Bruyninckx* (1995), 4 B.C.L.R. (3d) 341 (B.C. C.A.), counsel for the Bank did not provide us with any analysis as to why a constructive trust should be imposed in this case. In *Bruyninckx*, such a remedy was granted to give effect to a finding of unjust enrichment, a finding that has not been made in this case. I am not persuaded that any other basis for the granting of the remedy has been shown, given Mr. Shields' acknowledgment that he is unable to prove any fraudulent intention on the part of the Respondents. I would dismiss this aspect of the Bank's claim as well.

Alternative Argument

21 Counsel before us spent a great deal of time and attention on the "chestnut" referred to earlier — the Respondents' alternate argument that in any event, they were holders in due course of the bank drafts and therefore entitled to the protection afforded by s. 56 of the *Bills of Exchange Act*. Much has been written on the question of whether the actual payee of a draft can qualify as a holder in due course. Our attention was drawn *inter alia* to the decision of the House of Lords in *R.E. Jones Ltd. v. Waring & Gillow Ltd.*, [1926] A.C. 670 (U.K. H.L.); Crawford and Falconbridge, *Banking and Bills of Exchange* (8th ed., 1986) at 1442-49; and two articles by Benjamin Geva, "Irrevocability of Bank Drafts, Certified Cheques and Money Orders" (1986) 65 *Can. Bar Rev.* 107 and "The Autonomy of the Banker's Obligation on Bank Drafts and Certified Cheques" (1994) 73 *Can. Bar Rev.* 21. These make it clear that the issue is a contentious one and of considerable importance to the banking industry. However, it is not necessary to enter into the debate, given my conclusions that all the Bank's claims against the Respondents must fail on the evidence that was before the court.

22 I would allow the appeal and substitute an order dismissing the Bank's action against the Respondents in place of the Chambers judge's earlier order remitting the matter to the trial list.

Appeal allowed in part.

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End of Document

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TAB 8

Most Negative Treatment: Check subsequent history and related treatments.

2012 ONCA 475
Ontario Court of Appeal

Sadie Moranis Realty Corp. v. 1667038 Ontario Inc.

2012 CarswellOnt 8327, 2012 ONCA 475, [2012] O.J. No. 3029, 111 O.R. (3d) 401, 218 A.C.W.S. (3d) 286, 22 C.P.C. (7th) 224, 294 O.A.C. 308

Sadie Moranis Realty Corporation, Plaintiff (Appellant) and 1667038 Ontario Inc. and George B. Callahan, Defendants (Respondents)

Laskin, Goudge, Rouleau JJ.A.

Heard: April 13, **2012**
Judgment: July 5, **2012**
Docket: CA C53832

Proceedings: affirming *Sadie Moranis Realty Corp. v. 1667038 Ontario Inc.* (2011), 2011 CarswellOnt 592, 2011 ONSC 671, 16 C.P.C. (7th) 312 (Ont. Div. Ct.); reversing *Sadie Moranis Realty Corp. v. 1667038 Ontario Inc.* (2009), 2009 CarswellOnt 3799 (Ont. S.C.J.); affirming *Sadie Moranis Realty Corp. v. 1667038 Ontario Inc.* (2008), 2008 CarswellOnt 7955 (Ont. Master)

Counsel: Kirkor Apel, for Appellant
Trent Morris, for Respondents

Subject: Civil Practice and Procedure; Contracts; Property; Torts

Related Abridgment Classifications

Civil practice and procedure
XVI Disposition without trial
  XVI.6 Money in court and offers to settle
    XVI.6.a Payment into court

Real property
IV Real estate agents
  IV.9 Rights of agent
    IV.9.a Commission
      IV.9.a.viii Miscellaneous

Headnote

Civil practice and procedure --- Disposition without trial — Money in court and offers to settle — Payment into court
Company refused to pay commission to listing agent due to dispute over manner of sale — Agent commenced action for payment of commission against company and lawyer who held remainder of proceeds of sale in trust — Agent's motion for order requiring lawyer to pay remaining proceeds into court pending outcome of action was granted by master, and court upheld order — Divisional court held that judge and master erred, and ordered that motion and costs orders below be dismissed — Agent appealed — Appeal dismissed — Rule 45.02 of Rules of Civil Procedure was limited exception to law's aversion to providing plaintiff with execution before trial — Test required by Rule could not be met when claim was for

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damages since claim for damages was not legal right to fund — Rule did not require that legal right to specific fund be proprietary right as claimed by Divisional court — Listing agreement provided for payment of commission on closing, but did not provide that commission be paid out of proceeds of sale.

Real property --- Real estate agents — Rights of agent — Commission — Miscellaneous
Company refused to pay commission to listing agent due to dispute over manner of sale — Agent commenced action for payment of commission against company and lawyer who held remainder of proceeds of sale in trust — Agent's motion for order requiring lawyer to pay remaining proceeds into court pending outcome of action was granted by master, and court upheld order — Divisional court held that judge and master erred, and ordered that motion and costs orders below be dismissed — Agent appealed — Appeal dismissed — Rule 45.02 of Rules of Civil Procedure was limited exception to law's aversion to providing plaintiff with execution before trial — Test required by Rule could not be met when claim was for damages since claim for damages was not legal right to fund — Rule did not require that legal right to specific fund be proprietary right as claimed by Divisional court — Listing agreement provided for payment of commission on closing, but did not provide that commission be paid out of proceeds of sale.

Table of Authorities

Cases considered by *Goudge J.A.*:

Assante Financial Management Ltd. v. Dixon (2004), 2004 CarswellOnt 2158, 8 C.P.C. (6th) 57, [2004] O.T.C. 452 (Ont. S.C.J.) — considered

News Canada Marketing Inc. v. TD Evergreen (2000), 2000 CarswellOnt 3544 (Ont. S.C.J.) — followed

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 45 — considered

R. 45.02 — considered

APPEAL by agent from judgment reported at *Sadie Moranis Realty Corp. v. 1667038 Ontario Inc.* (2011), 2011 CarswellOnt 592, 2011 ONSC 671, 16 C.P.C. (7th) 312 (Ont. Div. Ct.), reversing order for payment into court of certain funds.

***Goudge J.A.*:**

Introduction

1 The central issue in this case is whether the appellant meets the test required by rule 45.02 of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194 to obtain an order that certain funds be paid into court pending the outcome of this action.

2 Rule 45.02 reads:

> **SPECIFIC FUND**
>
> 45.02 Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

3 The appellant's motion under rule 45.02 succeeded before the Master. It was also awarded costs of $20,000. On appeal, the Superior Court judge upheld the order and awarded further costs of $8,746.83. Leave to the Divisional Court was granted,

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where the appeal was allowed, the orders of the judge and the Master, including the costs orders, were set aside, and the appellant's rule 45.02 motion was dismissed, with global costs to the respondents fixed at $10,000.

4 The appellant appeals with leave to this court. It seeks first to restore the Master's order pursuant to rule 45.02, and second, to restore the Master's costs order in any event.

5 As I will explain, I agree with the result reached by the Divisional Court, but for somewhat different reasons. I would therefore dismiss the appeal.

The Background

6 This litigation arose as a result of the sale of land by the respondent 1667038 Ontario Inc. (166). The respondent George B. Callahan (Callahan) was the solicitor for 166 on the transaction.

7 Pursuant to a listing agreement it signed with 166 on November 1, 2006 (the Listing Agreement), the appellant was the listing agent for the property. The Listing Agreement provided for the appellant to receive a commission of eight percent of the sale price on the closing of the sale.

8 On May 31, 2007, an offer to purchase the property for $2,000,000 was accepted. The purchaser paid a deposit of $5,000. The sale closed on or about May 15, 2008 and the deposit was applied to the appellant's commission. The balance of the proceeds of the sale were held in trust by Callahan.

9 166 refused to pay the remainder of the commission to the appellant because it says that the appellant, among other things, failed to ensure that certain lots within the property would remain with the vendor and would not be included in the sale.

10 The appellant therefore commenced this action on June 6, 2008. Callahan was sued only because he held the proceeds of the sale. By the time of the motion before the Master, all but some $40,000 of these proceeds had been disbursed.

11 As originally framed, the appellant's action sought its commission as being due and owing on closing pursuant to the Listing Agreement. On June 3, 2009, the Master (not the Master who dealt with the rule 45.02 motion) dismissed the appellant's motion to amend this claim to also seek recovery based on express or implied trust, unjust enrichment and constructive trust, and conversion. No appeal was taken from this order.

12 This appeal results from the motion under rule 45.02 brought by the appellant in its action against the respondents. The motion sought to require Callahan to pay into court the proceeds of the sale remaining in trust pending the outcome of the action for the appellant's commission.

13 On December 17, 2008, the Master granted the order. The Master found that it was not necessary that the appellant have a proprietary claim to succeed. She held that the words of the Listing Agreement were capable of establishing a term that the commission be paid out of the proceeds of the sale. The Master also found that, although the appellant did not plead trust principles, the record supported the appellant's claim to the monies in trust on the basis of constructive trust. The Master ordered costs of $20,000 to the appellant as fair and reasonable given the appellant's success, and taking into account the usual factors relevant to costs, together with the respondents' delay in disclosing the disbursal of much of the sale proceeds.

14 On appeal, the Superior Court judge upheld this order and the reasoning underlying it and assessed additional costs of $8,746.83.

15 On further appeal, the Divisional Court held that both the judge and the Master erred in finding that a plaintiff need not establish a proprietary claim to a specific fund in order to obtain relief under rule 45.02. The court found that the appellant's claim is framed as a breach of the Listing Agreement. In the absence of a proprietary claim, the court ordered that the rule 45.02 motion and the costs orders below be dismissed. It awarded the respondents global costs for all proceedings of $10,000.

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Analysis

16 The issue in this appeal is the test required by rule 45.02, and whether the appellant meets it in this case. To reiterate, rule 45.02 reads as follows:

> **SPECIFIC FUND**
>
> 45.02 Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

17 Rule 45.02 is part of Rule 45 which, as its title suggests, provides for the interim preservation of property pending litigation. The Rule is a limited exception to the law's deep-seated aversion to providing a plaintiff with execution before a trial. The risk of such an order, because of its invasive nature, is well explained by Sharpe J.A. in *Injunctions and Specific Performance*, looseleaf 3d ed. (Aurora: Canada Law Book, **2012**), at para. 2.760:

> Clearly, pre-trial execution of any kind poses definite problems. Attachment of assets or interference with disposition of assets will often constitute a serious interference with the defendant's affairs. That interference may be more readily justified where the plaintiff's right is specifically related to the asset in question. However, where the plaintiff asserts a general claim and looks to the assets only as a means of satisfying a likely or possible monetary judgment against the defendant, interference with the defendant's assets is more difficult to justify.

18 In my view, the policy approach dictated by this caution must inform the test required by rule 45.02. In *News Canada Marketing Inc. v. TD Evergreen*, [2000] O.J. No. 3705 (Ont. S.C.J.), at para. 14, Nordheimer J. put forward a test which does that, and which I would adopt:

> I conclude therefore that the appropriate test for relief under rule 45.02 should require the plaintiff to establish that:
>
> (a) the plaintiff claims a right to a specific fund;
>
> (b) there is a serious issue to be tried regarding the plaintiff's claim to that fund;
>
> (c) the balance of convenience favours granting the relief sought by the plaintiff.

19 The first of these requirements, the one under special scrutiny in this appeal, faithfully reflects the language of rule 45.02. It requires that there be a specific fund readily identifiable when the order is sought. It also requires that the plaintiff assert a legal right to the specific fund as a claim in the litigation. While I do not find it to be a helpful descriptor, I think it is in this sense that past jurisprudence has sometimes described the specific fund as "earmarked to the litigation".

20 The second and third requirements, though not centrally in issue in this case, are equally important in manifesting the policy behind the rule. They ensure that interference with the defendant's disposition of assets is limited to cases where the plaintiff has a serious prospect of ultimate success, and there is something compelling on the plaintiff's side of the scales, such as a real concern that the defendant will dissipate the specific fund, that is sufficient to outweigh the defendant's freedom to deal with his or her property.

21 Framed in this way, the test will not be met where a plaintiff's claim is for damages. That is so even if a specific fund is identifiable in the factual matrix of the litigation, because a claim for damages is not a claim to a legal right to that fund. In *Assante Financial Management Ltd. v. Dixon* (2004), 8 C.P.C. (6th) 57 (Ont. S.C.J.), Wilton-Siegel J. put it this way, at para. 28:

> There is a subtle but important difference between an amount that may be owing to the plaintiff and a right of the plaintiff to a fund.

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22 Where the test is met, the order secures the specific fund claimed by the plaintiff pending the outcome of the litigation. The order is distinguishable from a *Mareva* injunction (with its even stricter test), where the defendant is restrained from dealing with its own assets pending trial even though the plaintiff is not asserting a legal right to any of those assets.

23 Much of the argument in this court addressed the Divisional Court's refinement of the first part of the test from *News Canada Marketing Inc.* The Divisional Court required that the plaintiff's claim to the specific fund be proprietary in nature.

24 The Divisional Court was simply reflecting a notion that has crept into the rule 45.02 jurisprudence over the last decade, perhaps spurred by cases in which the claimed right to the specific fund was seen as clearly proprietary in nature (such as a claim of ownership) and therefore undoubtedly sufficient to meet the first part of the test. Where, however, the order is denied because the claimed right is not seen as proprietary a difficulty with the refinement arises.

25 One way to put that difficulty is that the language of the subrule does not require that the right to the specific fund claimed by the plaintiff be a proprietary right. The refinement is simply not true to the subrule.

26 Put another way, if the refinement (i.e. that the plaintiff's claim be to a proprietary right to the specific fund) is seen to confine the plaintiff to only a certain sort of legal right, it would unjustifiably narrow the subrule to something less than the subrule provides for. If, on the other hand, the refinement is seen as not affecting the test as stated in the subrule, it adds nothing. Moreover, it risks diverting the proper inquiry into an analysis of whether the legal right claimed has a "proprietary dimension" or is "proprietary in nature" as several of the cases have described. Either way, the refinement is not justified.

27 In short, I do not think that rule 45.02 requires that the legal right to the specific fund claimed by the plaintiff be a proprietary right.

28 What remains is to examine whether the appellant meets the test for a rule 45.02 order as I have framed it.

29 In my view, it is clear that the appellant does not do so. While the monies held in trust are in an identifiable fund, the appellant does not claim a legal right to that specific fund in this litigation.

30 I agree with the Divisional Court that the appellant's claim is for breach of contract because of the vendor's failure to pay the commission in accordance with the Listing Agreement. That agreement provides for the payment of the commission on closing and for the application of the deposit to that commission. Importantly, it does not provide for the commission to be paid out of the proceeds of the sale. In finding that the words of the Listing Agreement were capable of giving the appellant such a right, the Master was in error.

31 The Master also erred in finding that the appellant could claim a right to the monies in trust on the basis of trust principles. That conclusion is untenable in the face of the dismissal of the appellant's motion to amend its claim to do just that.

32 In short, the appellant cannot meet the test for an order under rule 45.02. The Divisional Court was correct to allow the appeal and dismiss the motion.

33 Since the motion fails, there is no justification for independently sustaining the costs order which was made by the Master based on the appellant's success.

34 In the result, I would dismiss the appeal with costs fixed at $5000 inclusive of disbursements and applicable taxes.

***Laskin J.A.*:**
I agree

***Rouleau J.A.*:**
I agree

Appeal dismissed.

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TAB 9

Most Negative Treatment: Recently added (treatment not yet designated)
Most Recent Recently added (treatment not yet designated): Caroti v. Kegalj | 2019 ONSC 5772, 2019 CarswellOnt 16125 | (Ont. S.C.J., Oct 4, 2019)

2000 CarswellOnt 3544
Ontario Superior Court of Justice

News Canada Marketing Inc. v. TD Evergreen

2000 CarswellOnt 3544, [2000] O.J. No. 3705, 100 A.C.W.S. (3d) 145, 100 A.C.W.S. (3d) 45

News Canada Marketing Inc., Plaintiff and TD Evergreen, A Division of TD Securities Inc./Valeurs Mobilieres TD Inc., Defendant

Nordheimer J

Heard: September 29, 2000
Judgment: October 4, 2000
Docket: 00-CV-188234CM

Counsel: *Joseph C. D'Angelo*, for Plaintiff.
F. Paul Morrison and *Ian A.C. MacKinnon*, for Defendant.

Subject: Property; Civil Practice and Procedure

Related Abridgment Classifications

Civil practice and procedure
XV Preservation of property rights pending litigation
XV.2 Interim preservation of property

Civil practice and procedure
XXIV Costs
XXIV.5 Persons entitled to or liable for costs
XXIV.5.f Non-party

Headnote

Practice --- Pre-trial procedures — Interim preservation of property
Purchaser and vendor entered in to share purchase agreement — Purchaser placed sum of purchase price into escrow account held by defendant and subject to escrow agreement — Vendor indemnified purchaser under share purchase agreement — Purchaser was to notify defendant regarding claims for indemnity and defendant would interplead disputed amount if no objection by vendor — Purchaser sent notice to defendant but it was not received until after defendant had advanced funds to vendor in advance of date set out in escrow agreement — In advance of its request to forward funds early, vendor knew of purchaser's notice and failed to inform defendant — Motion by purchaser to pay funds in escrow account into court was granted — Vendor was ordered to pay into court proportion of moneys improperly advanced, sufficient to bring total amount equal to purchaser's claim — Interpretation of indemnity clause was serious issue to be tried — Balance of convenience favoured maintenance and protection of fund held in escrow.

Table of Authorities

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Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 45 — considered

R. 45.01 — considered

R. 45.02 — considered

MOTION by purchaser for escrow funds held by defendant to be paid into court.

***Nordheimer J.*:**

1 In this motion, the plaintiff seeks an order requiring certain escrow funds to be paid into court or otherwise secured in favour of the plaintiff pending the disposition of this, and of a companion, action. The defendant actually took no position with respect to this motion. The opposition to the relief sought comes from the vendor under a share purchase agreement which I will describe in more detail below. The vendor's solicitors are also the solicitors for the defendant in this action.

2 In August 1994, the plaintiff (which was then known as Actmedia Canada Inc.) entered into a Share Purchase Agreement whereby it agreed to acquire the shares of a company which was, at the time, owned by Nedcorp Quebec and others. Pursuant to the terms of the Share Purchase Agreement, the sum of $2,380,000.00 of the purchase price was to be placed in an escrow account. The purpose of the escrow account, as stated in one of the preambles to the escrow agreement, was:

> ... to be used to satisfy certain potential indemnities of Nedcorp (including for this purpose, of Nedkov) as provided in section 8.1(a) of the Purchase Agreement;

3 The escrow agreement established certain dates on which portions of the escrow funds were to be paid out to the vendor. The sum of $550,000.00 was to be paid out on August 15, 1998; the sum of $950,000.00 was to be paid out on August 15, 1999; and the sum of $750,000.00 was to be paid out on August 15, 2000. The balance of the escrow funds was to be paid out on August 15, 2001. The escrow funds were placed into an account with the defendant.

4 Clause 8.1(a) of the Share Purchase Agreement says in part:

> each shareholder shall severally indemnify and hold harmless Purchaser against any losses, claims, damages or liabilities (together, "Claims") to which Purchaser may become subject insofar as such Claims (or actions in respect thereof) arising out of or are based upon
>
> > (i) a breach by such Shareholder of any representation, warranty or covenant made by such Shareholder herein or in any agreement executed pursuant hereto...

5 The essential process established under the escrow agreement is that if the plaintiff claims to be entitled to be indemnified by the vendor, it may deliver to the defendant a written notice requesting that the defendant pay all, or a portion, of the escrow funds to the plaintiff. If the defendant does not receive a written objection from the vendor within 14 days of such notice, the defendant may pay the amount to the plaintiff. If the defendant does receive an objection, then the defendant is permitted to interplead the disputed amount.

6 The amount due on August 15, 1998 was paid to the vendor. However, matters were considerably different a year later. On August 4, 1999 a letter from the plaintiff's solicitors was sent by courier to the defendant. The letter enclosed a notice

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pursuant to the terms of the escrow agreement requesting the defendant to pay to the plaintiff the amount of $1,462,192.00 to satisfy a claim for indemnity which the plaintiff claimed to have against the vendor. Copies of the letter and notice were concurrently sent by courier to the vendor. The defendant refused to accept the courier delivery because the letter was addressed to an individual who no longer worked for the defendant although this was the person identified in the escrow agreement as being the person to whom notices to the defendant should be addressed. It appears that the defendant had never advised the plaintiff that the individual in charge of the escrow account had changed.

7 Because of the defendant's refusal to accept the courier delivery, the next day copies of the letter and notice were sent by fax transmission to the defendant. In addition, on August 11, 1999 the original versions of the letter and notice were personally delivered to the defendant. The letter and notice eventually reached the individual within the defendant in charge of the escrow arrangement on August 17, 1999.

8 Meanwhile, and unknown to the plaintiff, the vendor requested the defendant to send to it, on August 13, 1999, the $950,000.00 that was to be paid on August 15, 1999. The reason for this request, it appears, was that August 15, 1999 was a Sunday. The defendant, after obtaining a signed confirming letter from the vendor, complied with the vendor's request and in fact released the funds to the vendor on August 12, 1999. Then by letter dated August 16, 1999, the solicitors for the vendor wrote to the defendant and objected to the notice which the plaintiff had delivered.

9 Over the next several months, and for reasons which are not explained, the defendant refused to respond to inquiries from the solicitors for the plaintiff as to the status of the funds in the escrow account. The plaintiff assumed that the defendant was proceeding to interplead the disputed funds. However, after several months had passed and with no evidence that the defendant was so proceeding, the plaintiff commenced this action. It was only when the defendant filed its statement of defence in this action that the plaintiff first became aware that the defendant had in fact released the $950,000.00 to the vendor.

10 As a consequence of this revelation, the plaintiff brought this motion in which it seeks essentially to have the remaining funds in the escrow account paid into court and to require the vendor to pay into court that portion of the $950,000.00 needed to make the total amount paid into court equal to the amount of the plaintiff's claim under its notice. The plaintiff seeks this relief because it says that it has lost faith in the defendant's impartiality because of the improper payment of the $950,000.00. In the alternative, the plaintiff seeks an injunction restraining the defendant from releasing or disbursing any further amounts from the escrow account.

11 The plaintiff principally relies on Rule 45 in support of the relief which it seeks, the relevant portions of which are:

> 45.01(1) The court may make an interim order for the custody or preservation of any property in question in a proceeding or relevant to an issue in a proceeding, and for that purpose may authorize entry on or into any property in the possession of a party or of a person not a party.
>
> (2) Where the property is of a perishable nature or likely to deteriorate or for any other reason ought to be sold, the court may order its sale in such manner and on such terms as are just.
>
> 45.02 Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

12 Both parties rely on the decision in *Sun v. Ho* (1998), 18 C.P.C. (4th) 363 (Ont. Gen. Div.) for the test applicable to a motion under rule 45. In that case, Rivard J., at p. 364, accepted the test put to him by counsel in the following terms:

> Mr. Birnboim, on behalf of the responding parties submits the following: firstly, under Rule 45.02 the plaintiff must establish a right to a specific fund; secondly, there must be a strong prima facie case and, thirdly, the balance of convenience requires the Court to inquire into the potential harm that would be incurred by the moving party if the relief is not granted.
>
> I have added the words, 'potential harm that would be incurred by the moving party if relief is not granted' because that is the test set out in the *Unigrand International Enterprises Ltd. v. Sea-Glo Seafoods Ltd.* (January 29, 1993), Doc.

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93-CQ-31872 (Ont. Gen. Div.) a case referred to the Court by counsel.

This same test is set out in *Tom Jones Corp. v. Mishemukwa Developments Ltd.* (1996), 46 C.P.C. (3d) 77 (Ont. Gen. Div.). In contrast, in the decision in *Kongrecki v. Rafael* (1993), 19 C.P.C. (3d) 58 (B.C.C.A.) there is no mention of a requirement that there be a "strong" prima facie case.

13 It is not clear to me where the requirement for a "strong" prima facie case is derived from. It is not found in the rule itself nor does it appear to be mentioned in earlier Ontario authorities under the rule. In one of the first cases to consider rule 45.02, *Rotin v. Lechcier-Kimel* (1985), 3 C.P.C. (2d) 15 (Ont. H.C.), White J. allowed an appeal from a decision of a Master and ordered certain monies paid into Court on the basis that the plaintiffs had established "a prima facie" entitlement to the funds. Similarly, in *Maybank Foods Inc. Pension Plan v. Gainers Inc.* (1988), 63 O.R. (2d) 687 (H.C.), MacFarland J. granted an order under rule 45.02 requiring that a specific fund be paid into court. In the course of her decision, Madam Justice MacFarland stated that the plaintiffs had raised a "substantial issue to be tried." Finally, in *Charlebois v. Denjon Construction Ltd.* (1997), 13 C.P.C. (4th) 150 (Ont. Gen. Div.) in considering a motion under rule 45.02, Platana J. adopted a "prima facie case" or "sufficient grounds" test.

14 I mention this issue because it seems strange to me that the requirement under rule 45.02, to obtain an order for payment into court of a specific fund, would be a higher or more onerous one than that required to obtain an interlocutory injunction, in which it is generally only necessary to show that there is a serious issue to be tried. I consider that there is some considerable logic to having the tests for either form of relief employ a similar standard since they are in large measure designed to accomplish a similar result. I conclude therefore that the appropriate test for relief under rule 45.02 should require the plaintiff to establish that:

(a) the plaintiff claims a right to a specific fund;

(b) there is a serious issue to be tried regarding the plaintiff's claim to that fund;

(c) the balance of convenience favours granting the relief sought by the plaintiff.

15 The vendor submits that the plaintiff's claim against the escrow funds is not covered by the indemnity agreement and therefore the plaintiff cannot establish that it has a strong, or any, prima facie claim to the funds. The vendor also submits that the relief being sought is in the nature of a *Mareva* injunction and that the plaintiff ought to have to satisfy the stringent tests for a *Mareva* injunction before any relief is granted to it. I will deal with each of these points in turn.

16 The plaintiff's claim against the escrow funds under its notice arises out of an issue with respect to the calculation of adjusted working capital for the purchased company as of the closing date. Under clause 1.3, depending on the results of that calculation, there was a requirement to adjust the purchase price. The plaintiff says that a calculation of the adjusted working capital, which the plaintiff also says was considerably delayed by the vendor, gave rise to an entitlement in the plaintiff to an adjustment of the purchase price which it now claims. The vendor disputes the plaintiff's claim and, in any event, submits that it is not a matter which is covered by the indemnity provisions in the share purchase agreement and therefore the escrow funds are not available to respond to it.

17 The vendor's position in this latter respect is based on the wording of clause 8.1(a), which I set out above, and specifically the use of the words "to which Purchaser may become subject". The vendor says that these words do not permit a claim to be made by the plaintiff on the indemnity where it is a claim for loss suffered by the plaintiff itself but only permits claims to which the plaintiff becomes "subject" at the instance of another. The vendor relies on the definition of "indemnify" contained in Black's Law Dictionary (7th edition, West Group, 1999) as meaning:

to reimburse (another) for a loss suffered because of a third party's act or default.

I note, however, that in the same dictionary the word "indemnity" is defined as:

a duty to make good any loss, damage, or liability incurred by another.

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Unlike the former definition, the latter definition contains no element of involvement by a third party.

18 I do not agree with the vendor's submissions on this point. In my view, the vendor's interpretation of clause 8.1(a) of the Share Purchase Agreement is overly narrow. It seems to me that a person can be "subject" to losses, claims, damages or liabilities without it being a necessary requirement for there to be a third party involved. I would further observe that if it had been intended to have such a narrow application of the indemnity provision in the Share Purchase Agreement much clearer language could have been employed to accomplish that purpose.

19 In any event, it is clear to me that there is a serious issue to be tried regarding this dispute. Until that dispute is resolved, I believe that the balance of convenience favours the maintenance and protection of the fund which the parties expressly set aside from the purchase price. While there was considerable discussion on the motion about the credit worthiness of the vendor and whether that impacted on the balance of convenience, it is obvious to me that the whole reason for setting aside a portion of the purchase price in an escrow account was to avoid any issue of the monies not being available from the vendor to answer for any claim that might be made by the plaintiff.

20 I also do not accept the submission of the defendants that the relief being sought is tantamount to a *Mareva* injunction and that the plaintiff must therefore satisfy the very strict tests for that relief. This situation is very much different than that to which a *Mareva* injunction is normally directed. Here we have a specific fund which the parties agreed should be set aside in the hands of an escrow agent to be available to answer for certain specified claims. In a *Mareva* injunction case, the plaintiff seeks to restrain the defendant from dealing with the defendant's own assets which the plaintiff would otherwise have no right to claim against, or interfere with, until such time as it had a judgment against the defendant. In my view the two situations are not at all comparable and I therefore do not see any reason to require the plaintiff to satisfy the prerequisites for a *Mareva* injunction in order to obtain relief either under rule 45.02 or in terms of the injunctive relief it seeks.

21 The vendor submits that to grant the relief being sought by the plaintiff, which would have the effect of removing the defendant as the escrow agent, is equivalent to the removal of an executor or trustee. The vendor then cites various authorities regarding the removal of trustees. Again, I do not find the analogy advanced by the vendor to be apt. However, even if it were, there is certainly evidence before me that would raise a legitimate issue as to the defendant's handling of the escrow account. In this regard, it is evident to me that the defendant was in error in forwarding to the vendor the sum of $950,000.00 on August 12, 1999. There was no basis for the vendor receiving such funds in advance of the August 15, 1999 due date and if, as was the case, that date fell on a Sunday then the appropriate date for payment of those funds became Monday, August 16, 1999 and not any earlier date. Further, had it not been for the defendant's own internal changes in personnel, it would have been in receipt of the plaintiff's notice in advance of the payment being made and would then have been absolutely precluded from making any payment to either party under the terms of the escrow agreement. The actions of the defendant in regard to this payment would satisfy me that there were sufficient grounds to question the good faith and reasonableness of the defendant's actions which in turn would provide sufficient grounds for the removal of it as a trustee — see *Re McLaren* (1922), 51 O.L.R. 538 (C.A.).

22 I have concluded therefore that the plaintiff is entitled to an order under rule 45.02 for the payment into court of the balance of the monies being held by the defendant in the escrow account together with all accrued interest. Lastly, I should also mention that the vendor had the plaintiff's notice in advance of prevailing upon the defendant to make the payment which the defendant did on August 12, 1999. It apparently did not mention this fact to the defendant when it made its request for the monies. In such circumstances, it is only fair and reasonable that the vendor should also have to pay into court that portion of the monies which it improperly received which is sufficient to bring the total amount (excluding accrued interest) equal to the amount of the plaintiff's claim.

23 I therefore grant an order directing the defendant to pay the sum of $880,000.00 into court together with all interest that has accrued in the escrow account, and that the sum of $582,192.00 be paid into court by Nedcorp Group Inc. and Nedcorp Holdings (Quebec) Inc., or that these sums be otherwise secured in favour of the plaintiff, pending the final disposition of the issues between the parties or further order of this court.

24 In the circumstances, I cannot see any reason why the plaintiff would not be entitled to its costs of this motion payable forthwith but, if there are matters which counsel wish to bring to my attention that might alter my view in this regard, they may do so by way of written submissions. I am also prepared to fix the costs of the motion if the parties cannot agree on them

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on receipt of appropriate submissions for that purpose. The plaintiff shall file its submissions within 10 days of the release of these reasons and the defendant/vendor shall file its responding submissions within 10 days thereafter. As always, I would appreciate it if counsel would keep their submissions brief.

Motion granted.

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TAB 10

2011 ONSC 7113
Ontario Superior Court of Justice [Commercial List]

Deol v. Morcan Financial Inc.

2011 CarswellOnt 13652, 2011 ONSC 7113, [2011] O.J. No. 5371, 210 A.C.W.S. (3d) 378, 38 C.P.C. (7th) 348

Harpinder Deol, Plaintiff and Morcan Financial Inc. o/a/R/E Active Mortgages, Guiseppe Taibi and Harold Kennedy, Defendants

D.M. Brown J.

Heard: October 21, November 15, 2011
Judgment: November 30, 2011
Docket: CV-11-9243-00CL

Counsel: S. Schneiderman, for Plaintiff
E. Snow, for Defendants

Subject: Civil Practice and Procedure; Property; Corporate and Commercial

Related Abridgment Classifications

Civil practice and procedure
XV Preservation of property rights pending litigation
XV.2 Interim preservation of property

Headnote

Civil practice and procedure --- Pre-trial procedures — Interim preservation of property
Plaintiff D sued defendants for damages for breach of oral contract under which she provided mortgage agent services to defendant M Inc. — D brought motion for, inter alia, order directing defendants to preserve, pending outcome of litigation, such finders' fees and volume bonuses in their possession on account of mortgage transactions for which D claimed commissions were owing to her, where those funds had not already been used — That part of motion dismissed — D relied primarily on "specific fund" rule, R. 45.02 of Rules of Civil Procedure, to support request for pre-trial preservation order — D did not demonstrate existence of specific fund to which she was asserting proprietary claim — In amended statement of claim, D contended M Inc. owed her $666,359.09 in unpaid finders' fees and that that amount was at all material times being held in trust by defendants — On examination for discovery, defendant T testified that during relevant period M Inc. only operated one bank account and financial institutions would deposit finders' fees into that account — Having reviewed references to other evidence contained in parties' factums, there did not appear to be any evidence M Inc. held in trust portions of finders' fees due to D — Nor, under legislation in force at relevant time, was M Inc. required to hold finders' fees in trust — Evidence strongly suggested finders' fees received by M Inc. prior to termination of D's retainer had since been used by M Inc. for operating expenses — What D really sought was order compelling defendants to put to one side general corporate funds to stand as security for judgment D hoped to secure at trial, and that sort of execution before judgment was not available under R. 45.02.

Table of Authorities

Cases considered by *D.M. Brown J.*:

Rosen v. Homelife/St. Andrew's Realty Inc. (1994), 1994 CarswellOnt 4528 (Ont. Gen. Div.) — referred to

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Sadie Moranis Realty Corp. v. 1667038 Ontario Inc. (2011), 2011 CarswellOnt 592, 2011 ONSC 671 (Ont. Div. Ct.) — referred to

Stearns v. Scocchia (2002), 2002 CarswellOnt 3700, 27 C.P.C. (5th) 339, [2002] O.T.C. 855 (Ont. S.C.J.) — considered

Statutes considered:

Business Corporations Act, R.S.O. 1990, c. B.16
Generally — referred to

Mortgage Brokers Act, R.S.O. 1990, c. M.39
Generally — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
Generally — referred to

R. 45 — considered

R. 45.02 — considered

Regulations considered:

Mortgage Brokers Act, R.S.O. 1990, c. M.39
General, R.R.O. 1990, Reg. 798

s. 6(1) — considered

RULING concerning part of motion by plaintiff in which plaintiff sought order directing defendants to preserve, pending outcome of litigation, such finders' fees and volume bonuses in their possession on account of mortgage transactions for which plaintiff claimed commissions were owing to her, where those funds had not already been used.

***D.M. Brown J.*:**

I. Motion for the interim preservation of funds

1 Ms. Harpinder Deol sues the defendants for damages for breach of an oral contract under which she provided mortgage agent services to Morcan Financial Inc. Those parts of the motion concerning discovery-related relief I dealt with by way of handwritten endorsements dated October 21 and November 15, 2011. Ms. Deol also seeks interim relief under Rule 45 of the *Rules of Civil Procedure*, specifically an order:

> Directing the Defendants to preserve, pending the outcome of this litigation, such finders' fees and volume bonuses in their possession on account of mortgage transactions for which the Plaintiff claims commissions are owing to her, where those funds have not already been used.

2 For the reasons set out below, I dismiss that part of her motion.

II. Background facts

3 In her Amended Statement of Claim Ms. Deol pleaded that she was retained by Morcan as a mortgage agent in 2004.

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Under the terms of her oral retainer contract she would find clients for Morcan and arrange mortgage funds for them from financial institutions. Deol and Morcan would then split the lender's finders' fees 90:10. Ms. Deol sues Morcan for her share of finders' fees which she alleges are owing to her for mortgages which she arranged during the period December, 2006 through to June, 2008.

4 As part of her pleading Ms. Deol alleges that the defendants held her share of the finders' fees in trust and that each defendant stood as a trustee of those funds towards her. Ms. Deol also invokes the oppression remedy under the *Ontario Business Corporations Act*, alleging that she is a "complainant" and that the defendants' failure to pay her a share of the finders' fees was oppressive conduct.

5 Morcan denies any liability, contending that Ms. Deol failed to submit required documentation to support her claim for a share of some finders' fees and that otherwise Morcan has paid her all commissions earned by her. The defendants deny the existence of any trust relationship and contend that Ms. Deol lacks standing to bring an oppression claim. Morcan has counterclaimed for an alleged overpayment of commissions to Ms. Deol.

6 The plaintiff commenced her action on December 29, 2008. She amended her Statement of Claim earlier this year to assert the breach of trust and oppression claims. Examinations for discovery have been held, although the defendants owe some answers to undertakings.

III. The principles governing the application of Rule 45.02

7 The plaintiff relies primarily on the "specific fund" rule, Rule 45.02, to support her request for a pre-trial preservation order. Rule 45.02 provides:

> 45.02 Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

8 Morden & Perell, in *The Law of Civil Procedure in Ontario*, write that "the purpose of the motion under rule 45.02 is to protect before trial a claimant who is asserting a proprietary claim to or proprietary interest in a specific asset."[1] They explain the policy underlying Rule 45.02 as follows:

> Rule 45.02 is an exception to the general rule that a plaintiff cannot obtain execution before judgment, and it is not to be used just as a means to obtain security for a debt or potential indebtedness of the defendant. While a *Mareva* injunction and an order under rule 45.02 share several policy concerns about prejudgment remedies, they are discrete or mutually exclusive interlocutory remedies, and a plaintiff does not have to satisfy the requirements for a *Mareva* injunction in order to obtain a remedy under rule 45.02.[2]

9 In *Stearns v. Scocchia* the Court emphasized the extraordinary nature of a Rule 45.02 order and the resulting need to scrutinize any request with care:

> Because of the extreme nature of a rule 45.02 order and/or a *Mareva* injunction, they are remedies that should be available only when it is necessary to balance the interests of the plaintiff and defendant. Both orders maintain the status quo until trial in a way that is fair to both the plaintiff and defendant and must not place the interests of the plaintiff before those of the defendant. Such orders are not merely procedural in nature and should be granted only in exceptional circumstances because they have the potential to injure a defendant before the plaintiff has proven its case at trial. Furthermore, it can place a defendant in an unfair position because it freezes a fund that would otherwise be available to the defendant and available for the purpose of operating its business. In short, such an order can appreciably tilt the scales in favour of a plaintiff on the basis of unproven allegations. Judicial discretion is therefore to be carefully exercised when considering a rule 45 order or the granting of a *Mareva* injunction given the severe prejudicial consequences that can result.[3]

10 The jurisprudence which has developed under Rule 45.02 indicates that in order for a moving party to obtain an order under Rule 45.02 it must meet three criteria:

(a) the plaintiff must claim a right to a specific fund, defined as "a reasonably identifiable fund earmarked to the

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litigation in issue", and that claim must be proprietary in nature;

(b) there must be a serious issue to be tried respecting the proprietary claim; and,

(c) the balance of convenience must favour granting the relief sought.[4]

11 As to the first requirement to demonstrate the existence of a "specific" fund", Morden & Perell write:

Funds held in trust may constitute a specific fund, but a specific fund is not limited to trust funds; rather, a specific fund refers to a reasonably identifiable fund earmarked for the pending litigation. The rule has been used when the property at issue is a claim to pension funds held for employees. The rule has been applied with respect to sale proceeds held in a trust account.

A deposit payable in a real estate transaction has been held not to constitute a specific fund. Revenue from the operation of a parking lot does not constitute a specific fund. *A claim to funds due under a contract does not constitute a specific fund.*

Although the tracing of the fund may be done in the appropriate circumstance to prevent an injustice, the right to a remedy under the rule may be lost if before the motion is brought the specific fund is intermingled with other funds.

Where the specific fund is no longer available, an order may not be made under this rule requiring the defendant to pay other monies into court.[5]

12 On the last point MacFarland J. (as she then was) commented on the specificity requirement under Rule 45.02:
Were I to make an order requiring this sum of money to be paid into court, the defendant against whom the order was made would have to obtain funds from other sources or his/its own resources. In my view, that is not what is contemplated by Rule 45.02. The rule provides jurisdiction, in my view, only for the "specific fund" to be paid into court and not, where that fund is no longer available, for other monies to be paid into court in lieu thereof.[6]

IV. Analysis

13 The plaintiff has not demonstrated, on the evidence before me, the existence of a specific fund to which she is asserting a proprietary claim. In her Amended Statement of Claim the plaintiff contends that Morcan owes her $666,359.09 in unpaid finders' fees and pleads that that amount "was at all material times being held in trust by the Defendants..." On his examination for discovery Mr. Taibi testified that during the relevant time period Morcan only operated one bank account and financial institutions would deposit finders' fees into that account either directly or by cheque. Having reviewed the references to other evidence contained in the parties' factums, there does not appear to be any evidence that Morcan held in trust portions of finders' fees due to Ms. Deol.

14 Nor, under the legislation in force at the relevant time, was Morcan required to hold finders' fees in trust. Section 6 of Ont. Reg 798 made under the former *Mortgage Brokers Act*, R.S.O. 1990, c. M.39 provided:
6. (1) All funds received by a mortgage broker in connection with a mortgage transaction other than those which are clearly made as payment for fees earned shall be deemed to be trust funds.[7]

15 Moreover, the evidence strongly suggests that finders' fees received by Morcan from financial institutions prior to the termination of Ms. Deol's retainer in June, 2008 have since been used by Morcan for operating expenses.

16 As I assess the evidence, no specific fund exists in the hands of Morcan. What the plaintiff really seeks is an order compelling the defendants to put to one side general corporate funds to stand as security for a judgment which the plaintiff hopes to secure at trial. That sort of execution before judgment is not available under Rule 45.02.

V. Conclusion

17 For these reasons I dismiss that part of the plaintiff's motion brought under Rule 45.02.

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18 I would encourage the parties to try to settle the costs of all aspects of this motion. If they cannot, the plaintiff may serve and file with my office written cost submissions, together with a Bill of Costs, by Friday, December 9, 2011. The defendants may serve and file with my office responding written cost submissions by Monday, December 19, 2011. The costs submissions shall not exceed three pages in length, excluding the Bill of Costs.

Motion partly dismissed.

Footnotes

1 John Morden and Paul Perell, *The Law of Civil Procedure in Ontario, First Edition* (Toronto: LexisNexis, 2010), p. 186.

2 *Ibid.*

3 *Stearns v. Scocchia* (2002), 27 C.P.C. (5th) 339 (Ont. S.C.J.), para. 22.

4 *Ibid.*, para. 9. As to the "proprietary nature" of the claim, see *Sadie Moranis Realty Corp. v. 1667038 Ontario Inc.*, 2011 ONSC 671 (Ont. Div. Ct.), para. 7.

5 *Morden & Perell, supra.*, pp. 186-7 (emphasis added).

6 *Rosen v. Homelife/St. Andrew's Realty Inc.*, [1994] O.J. No. 2887 (Ont. Gen. Div.), para. 11.

7 Emphasis added.

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TAB 11

2007 CarswellOnt 3444
Ontario Superior Court of Justice

American Axle & Manufacturing Inc. v. Durable Release Coaters Ltd.

2007 CarswellOnt 3444, [2007] G.S.T.C. 142, [2007] O.J. No. 2138, 157 A.C.W.S. (3d) 937, 49 C.P.C. (6th) 180, 86 O.R. (3d) 53

American Axle & Manufacturing, Inc. (Plaintiff / Respondent) v. Durable Release Coaters Limited (Defendant / (Appellant)

Pattillo J.

Heard: February 8, 2007
Judgment: June 1, 2007
Docket: 03-CV-255954-CM3

Proceedings: reversing *American Axle & Manufacturing Inc. v. Durable Release Coaters Ltd.* (2006), 2006 CarswellOnt 5273 (Ont. Master)

Counsel: Jean M. DeMarco for Plaintiff
Gregory M. Sidlofsky for Defendant

Subject: Goods and Services Tax (GST); Civil Practice and Procedure; Property

Related Abridgment Classifications

Civil practice and procedure
XV Preservation of property rights pending litigation
XV.2 Interim preservation of property

Civil practice and procedure
XXIII Practice on appeal
XXIII.13 Powers and duties of appellate court
XXIII.13.i Upon appeal from Master
XXIII.13.i.iii Miscellaneous

Headnote

Tax --- Goods and Services Tax — Importations
Plaintiff shipped gear rotors that it manufactured in Buffalo, New York across border to defendant in Mississauga, Ontario for coating and return to plaintiff — Plaintiff was "importer of record" on customs documents and paid GST on value of gear rotor shipments — Pursuant to refund agreement, defendant agreed to aid plaintiff in recovering past GST by applying for input tax credit on GST amounts already paid on rotors by plaintiff — Defendant received GST refund cheque, which it deposited into its operating account — Bank applied proceeds to pay down defendant's line of credit — Plaintiff commenced action — Plaintiff brought successful motion for order for interim preservation of property pursuant to R. 45.02 of Rules of Civil Procedure — Master found that agreement made it clear that any refund that defendant obtained belonged to plaintiff, and that any refund monies obtained were trust funds for plaintiff — Defendant appealed — Appeal allowed — Rule 45.02 of RCP could not be invoked in absence of specific fund — Absent specific fund, order made by master was injunctive and not within master's jurisdiction — Record before master was not sufficient to support finding that trust existed — Even if it was, finding of trust and breach of trust were not necessary to determination of whether there was specific fund.

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Tax --- Goods and Services Tax — Input tax credits — Who entitled
Plaintiff shipped gear rotors that it manufactured in Buffalo, New York across border to defendant in Mississauga, Ontario for coating and return to plaintiff — Plaintiff was "importer of record" on customs documents and paid GST on value of gear rotor shipments — Pursuant to refund agreement, defendant agreed to aid plaintiff in recovering past GST by applying for input tax credit on GST amounts already paid on rotors by plaintiff — Defendant received GST refund cheque, which it deposited into its operating account — Bank applied proceeds to pay down defendant's line of credit — Plaintiff commenced action — Plaintiff brought successful motion for order for interim preservation of property pursuant to R. 45.02 of Rules of Civil Procedure — Master found that agreement made it clear that any refund that defendant obtained belonged to plaintiff, and that any refund monies obtained were trust funds for plaintiff — Defendant appealed — Appeal allowed — Rule 45.02 of RCP could not be invoked in absence of specific fund — Absent specific fund, order made by master was injunctive and not within master's jurisdiction — Record before master was not sufficient to support finding that trust existed — Even if it was, finding of trust and breach of trust were not necessary to determination of whether there was specific fund.

Civil practice and procedure --- Pre-trial procedures — Interim preservation of property
Plaintiff shipped gear rotors that it manufactured in Buffalo, New York across border to defendant in Mississauga, Ontario for coating and return to plaintiff — Plaintiff was "importer of record" on customs documents and paid GST on value of gear rotor shipments — Pursuant to refund agreement, defendant agreed to aid plaintiff in recovering past GST by applying for input tax credit on GST amounts already paid on rotors by plaintiff — Defendant received GST refund cheque, which it deposited into its operating account — Bank applied proceeds to pay down defendant's line of credit — Plaintiff commenced action — Plaintiff brought successful motion for order for interim preservation of property pursuant to R. 45.02 of Rules of Civil Procedure — Master found that agreement made it clear that any refund that defendant obtained belonged to plaintiff, and that any refund monies obtained were trust funds for plaintiff — Defendant appealed — Appeal allowed — Rule 45.02 of RCP could not be invoked in absence of specific fund — Absent specific fund, order made by master was injunctive and not within master's jurisdiction — Record before master was not sufficient to support finding that trust existed — Even if it was, finding of trust and breach of trust were not necessary to determination of whether there was specific fund.

Civil practice and procedure --- Practice on appeal — Powers and duties of appellate court — Upon appeal from Master — General principles
Plaintiff shipped gear rotors that it manufactured in Buffalo, New York across border to defendant in Mississauga, Ontario for coating and return to plaintiff — Plaintiff was "importer of record" on customs documents and paid GST on value of gear rotor shipments — Pursuant to refund agreement, defendant agreed to aid plaintiff in recovering past GST by applying for input tax credit on GST amounts already paid on rotors by plaintiff — Defendant received GST refund cheque, which it deposited into its operating account — Bank applied proceeds to pay down defendant's line of credit — Plaintiff commenced action — Plaintiff brought successful motion for order for interim preservation of property pursuant to R. 45.02 of Rules of Civil Procedure — Master found that agreement made it clear that any refund that defendant obtained belonged to plaintiff, and that any refund monies obtained were trust funds for plaintiff — Defendant appealed — Appeal allowed — Master was clearly wrong — Rule 45.02 of RCP could not be invoked in absence of specific fund — Absent specific fund, order made by master was injunctive and not within master's jurisdiction — Record before master was not sufficient to support finding that trust existed — Even if it was, finding of trust and breach of trust were not necessary to determination of whether there was specific fund.

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Howitt v. Howden Group Canada Ltd. (1999), 170 D.L.R. (4th) 423, 1999 CarswellOnt 659, 26 E.T.R. (2d) 1, 20 C.C.P.B. 250, 1999 C.E.B. & P.G.R. 8356 (headnote only) (Ont. C.A.) — referred to

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Sun v. Ho (1998), 1998 CarswellOnt 995, 18 C.P.C. (4th) 363 (Ont. Gen. Div.) — considered

Union Bank of Switzerland v. Batky (1998), 157 D.L.R. (4th) 364, 107 O.A.C. 241, 40 R.F.L. (4th) 440, 1998 CarswellOnt 840, 24 C.P.C. (4th) 157 (Ont. Div. Ct.) — referred to

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s. 101(1) — referred to

Excise Tax Act, R.S.C. 1985, c. E-15
s. 180 [en. 1990, c. 45, s. 12(1)] — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 37.02 — referred to

R. 40 — referred to

R. 45.02 — considered

APPEAL by defendant from decision reported at *American Axle & Manufacturing Inc. v. Durable Release Coaters Ltd* (2006), 2006 CarswellOnt 5273 (Ont. Master), granting plaintiff's motion for order for interim preservation of property pursuant to R. 45.02 of *Rules of Civil Procedure*.

***Pattillo J.*:**

1 The defendant appeals from the Order of Master Hawkins dated August 25, 2006, requiring it to pay $623,000 into court pursuant to rule 45.02 of the Rules of Civil Procedure, R.R.O. 1990, Reg. 194.

2 Rule 45.02 provides as follows:

> Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

Background

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3 The plaintiff is a major public company that designs and manufactures various products for the automobile industry. It produces gear rotors, which are components of axles, in its facility in Buffalo, New York.

4 The defendant is a private corporation that carries on the business of coating metal and other forged products in Mississauga, Ontario.

5 In February 2000, the plaintiff contracted with the defendant to coat the gear rotors that the plaintiff was producing at its facility in Buffalo, New York. The rotors were shipped across the border by the plaintiff, coated by the defendant, and returned to the plaintiff in the United States.

6 At the outset of the relationship, the plaintiff was named as the "importer of record" and was accordingly required to pay excise tax ("GST") to the Canadian Government. After paying in excess of $600,000 in GST, the plaintiff became aware that GST need not be paid where the manufactured items did not originate in Canada. In order to obtain such a result, the defendant would have to be named as the "importer of record".

7 On October 31, 2000, the plaintiff and the defendant entered into a written agreement entitled the "Letter of Agreement for NAFTA Certificates and Goods and Services Tax" (the "Agreement"). The Agreement provided that the defendant would become "importer of record". It further provided as follows:

> Goods and Services Tax: DRC (defendant) will support AAM (plaintiff) with claims for past G.S.T. (prior to Nov. 1, 2000) and assist with the applications for refunds (under Section 180 of the *Canadian Excise Tax Act*) from Revenue Canada. AAM will supply the necessary supporting documentation.

Section 180 of the *Excise Tax Act*, R.S. 1985, c. E-15 required that the defendant, as a resident of Canada, apply for the refund in its name, as importer of record.

8 The plaintiff hired Deloite & Touche to prepare all the necessary documentation to apply for the refund. Disagreements arose between the parties in respect of their business relationship. The defendant initially refused to submit the refund application. Eventually it was submitted.

9 On November 4, 2002, the defendant received a cheque from the Government of Canada in the amount of $697,537 on account of the GST refund. By this time, the relationship between the parties had deteriorated significantly. Upon receipt, the defendant deposited the GST refund cheque in its operating account, and the defendant's bank automatically applied the funds to pay down the defendant's existing line of credit. The defendant did not advise the plaintiff it had received the cheque.

10 The defendant's position is that it refused to release the GST refund to the plaintiff because of unpaid invoices that were outstanding at the time of receipt and because of losses that it had incurred that were attributable to the plaintiff's breaches of contract. The plaintiff takes issue with this position, which it says has no merit.

11 Sometime after November 4, 2002, the plaintiff learned through an independent third party inquiry with the government that the defendant had received the GST refund. On September 25, 2003 it commenced this action claiming, *inter alia*, payment of the GST refund in the amount of $697,819.89 plus interest, a declaration that the plaintiff is the legal and equitable owner of the refund, unjust enrichment, breach of fiduciary duty and constructive trust. The plaintiff alleged in paragraph 24 of its claim that the defendant's retention of the refund constituted a breach of contract.

12 By Statement of Defence and Counterclaim dated November 3, 2003, the defendant alleged the plaintiff had breached the contract in relation to gear rotors, pleaded set-off with respect to the amount claimed in the Statement of Claim and counterclaimed for damages. The defendant expressly denied that it owed a fiduciary duty to the plaintiff or that it had been unjustly enriched.

13 The plaintiff commenced its motion for, *inter alia*, interim preservation of property pursuant to rule 45.02 requiring the defendant to pay into court the sum of $625,000 in January 2006. The plaintiff reduced the amount sought to be paid into court by some $75,000 on the basis that it conceded that it owed the defendant that amount on account of unpaid invoices. It denied any further amounts were owing to the defendant.

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14 The matter was argued before the Master on July 19, 2006 and the Master released written reasons for decision dated August 25, 2006.

The Decision Appealed From

15 In allowing the plaintiff's motion and requiring the defendant to pay the sum of $623,000 into court in accordance with rule 45.02, the Master referred to and followed the test laid down by Rivard J. in *Sun v. Ho* (1998), 18 C.P.C. (4th) 363 (Ont. Gen. Div.) in respect of a motion under rule 45.02 as follows:

> 1. the plaintiff must establish a right to a specific fund;
>
> 2. there must be a strong *prima facie* case; and
>
> 3. the balance of convenience requires the court to inquire into the potential harm that would be incurred by the moving party.

16 In applying the first test for a rule 45.02 order, involving the right to a specific fund, the Master was of the view that the terms of the Agreement made it clear that any refund that the defendant obtained belonged to the plaintiff. Although the Agreement did not expressly refer to trust, the Master held that the circumstances surrounding the refund application were such that any refund monies obtained were trust funds for the plaintiff. The Master rejected the defendant's argument that there was no specific fund because the refund had been deposited by the defendant into its bank account and was no longer available. He regarded the defendant's actions as a breach of trust and held that the defendant's wrongdoing should not defeat the motion. Finally, relying on *Leung Estate v. Leung*, [2004] O.J. No. 1417 (Ont. S.C.J.), the Master held that notwithstanding that the specific fund had been spent, the court could order the defendant to restore the fund and pay the proceeds into court.

17 The Master found, on the evidence before him, that the plaintiff had made out a strong *prima facie* claim to the specific fund that was the refund monies received by the defendant.

18 Finally, the Master held that the balance of convenience favoured the granting of the order. He described the financial condition of the defendant as "delicate" based on an analysis of the financial statements of the defendant for the year ended November 30, 2005. At the same time he referred to evidence from the defendant on cross-examination that it had the ability to comply with an order of the court to pay the $623,000 into court.

19 The defendant appeals from the Master's order on two grounds: first, that the Master erred in law in holding that there was a specific fund with the meaning of R. 45.02; and second, that the Master erred in law in finding that the refund monies were trust funds and that the defendant had committed a breach of trust.

Standard of Review

20 The Divisional Court in *Bank of Nova Scotia v. Liberty Mutual Insurance Co.* (2003), 67 O.R. (3d) 699 (Ont. Div. Ct.) considered the test to be applied in respect of the review of a case management Master's decision. Dunnet J. on behalf of the court at p. 702 stated as follows:

> [12] We accept that the test to be applied on the review of a Master's decision is as follows:
>
> (a) if the matter is one of discretion, the court should not interfere unless the master was clearly wrong;
>
> (b) if the matter is one of law that is not vital to the disposition of the law suit, the court should not interfere unless the master was clearly wrong; and

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(c) if the matter is one of law that is deemed vital to the disposition of the law suit, the test should be one of correctness.

[13] Where the Master is dealing with interlocutory matters not vital to the disposition of the case; the motion ought to be heard as an appeal and not *de novo*.

[14] The notion of an increased level of deference that ought to be shown to Case Management Masters result from their unique role in the civil litigation process. This is not to say that there will not be situations where motions regarding productions are indeed vital to the lawsuit. This will depend on the nature of the case and the production in issue.

21 In the present case, the question of the operation of rule 45.02 is a question of law. The matter is clearly interlocutory. The real issue in determining the proper standard of review is the question of whether the decision is "vital to the disposition of the lawsuit". The defendant argues, given the nature of the order under appeal, which effectively grants the plaintiff execution before judgment, that it meets the "vital" test. The plaintiff on the other hand submits that the defendant's representative on cross-examination testified that the defendant had the ability to pay the amount ordered into court and that its future business prospects were positive. Accordingly, payment of the amount ordered will not impair the defendant's business or its ability to defend the action.

22 Rule 45.02 is one of the few exceptions that exist to the general rule that there can be no execution prior to judgment. Another exception is a Mareva injunction. The exceptions, however, are few and they are viewed by the courts as extreme remedies to be exercised with caution. In *Stearns v. Scocchia*, [2002] O.J. No. 4244 (Ont. S.C.J.), in considering a motion pursuant to rule 45.02, G.P. Smith J. stated a para. 22 as follows:

Because of the extreme nature of a rule 45.02 order and/or a Mareva injunction, they are remedies that should be available only when it is necessary to balance the interests of the plaintiff and defendant. Both orders maintain the status quo until trial in a way that is fair to both the plaintiff and defendant and must not place the interests of the plaintiff before those of the defendant. Such orders are not merely procedural in nature and should be granted only in exceptional circumstances because they have potential to injure a defendant before the plaintiff has proven its case at trial. Furthermore, it can place a defendant in an unfair position because it freezes a fund that would otherwise be available to the defendant and available for the purpose of operating its business. In short, such an order can appreciably tilt the scales in favour of a plaintiff on the basis of unproven allegations. Judicial discretion is therefore to be carefully exercised when considering a rule 45 order or the granting of a Mareva injunction given the severe prejudicial consequences that can result.

23 The extreme nature of rule 45.02 combined with the fact that the money ordered to be paid into court by the Master represents the entire amount of the plaintiff's claim, raise the possibility that the order appealed from could involve a matter vital to the disposition of the lawsuit. However, on the record, I am unable to determine that it does. While the defendant's financial position is "delicate", it has indicated that it can pay the money into court if required. Therefore it is my view that in order to succeed on this appeal, the defendant must establish that the Master was clearly wrong in his decision.

Rule 45.02

24 In *News Canada Marketing Inc. v. TD Evergreen*, [2000] O.J. No. 3705 (Ont. S.C.J.), Nordheimer J. dealt with a motion for an order under rule 45.02. After referring to the test set forth in *Sun v. Ho*, *supra*, and referring to other cases dealing with rule 45.02, Nordheimer J. was of the view that the requirements to obtain an order for payment into court of a specific fund should be no higher or more onerous than the requirements to obtain an interlocutory injunction. Nordheimer J. expressed the test for a rule 45.02 order as follows at para. 14:

a) the plaintiff must claim a right to a specific fund;

b) there is a serious issue to be tried regarding the plaintiff's claim to that fund; and

c) the balance of convenience favours granting the relief sought by the plaintiff.

25 I agree with the test as stated by Nordheimer J. Having said that, and notwithstanding that the Master followed the test set out by Rivard J. in *Sun v. Ho, supra,* no reversible error results; in fact, the test applied by the Master is more stringent in respect of the strength of the plaintiff's claim.

26 Counsel for the defendant concedes that at the time that the defendant received the refund cheque from the government on November 4, 2002 a "specific fund" existed. He submits, however, that the Master erred in holding that, some four years later, after the monies had long since been used by the defendant, the fund continued to exist and that the defendant should be required to effectively replenish it and pay the funds into court.

Specific Fund

27 Having regard to the wording of the rule 45.02, the extreme nature of the remedy and the majority of the authorities, in order to succeed on a motion pursuant to rule 45.02, a specific fund must be in existence and, in the case of money, be reasonably identifiable as earmarked for the litigation in issue.

28 Rule 45.02 refers to a "specific fund". In *Rotin v. Lechcier-Kimel,* [1985] O.J. No. 466 (Ont. H.C.), White J. stated:

> In my opinion, "Specific Fund", in the absence of jurisprudence indicating otherwise, means a reasonably identifiable fund earmarked to the litigation in issue. That which a mortgagor owes on a mortgage is a mere chase in action and in my opinion has not assumed the status of a specific fund.

29 In *Rosen v. Homelife/St. Andrew's Realty Inc.,* [1994] O.J. No. 2887 (Ont. Gen. Div.), MacFarland J. (as she then was) summed up what is required in connection with a specific fund under rule 45.02:

> The heading or title for Rule 45.02 is "Interim Preservation of Property". In my view, the rule is intended for the preservation of property which is in existence and in the case of money, is reasonably identifiable fund which can be earmarked to the litigation in issue. See *Rotin et al. v. Lechier-Kimel et al.,* [1985] 3 C.P.C. (2nd) 15. In each of the cases to which counsel referred, the funds were available to be paid into court; in this case the specific fund is no longer available. Were I to make an order requiring this sum of money to be paid into court, the defendant against whom the order was made would have to obtain funds from other sources or his/its own resources. In my view, that is not what is contemplated by Rule 45.02. The rule provides jurisdiction, in my view, only for the 'specific fund' to be paid into court and not, where that fund is no longer available, for other monies to be paid into court in lieu thereof.

See also: *Miller v. Carley,* [2006] O.J. No. 1813 (Ont. S.C.J.) and *Union Bank of Switzerland v. Batky* (1998), 157 D.L.R. (4th) 364 (Ont. Div. Ct.) at para 81.

30 In reaching his decision that the defendant must pay the money into court in the absence of a "specific fund", the Master relied on *Leung Estate v. Leung, supra.* That case involved, in part, a motion by estate trustees preventing the defendants from disposing, depleting, transferring or encumbering assets and to pay into court certain amounts pending the trial. The motion sought relief by way of certificates of pending litigation, an injunction and an order pursuant to rule 45.02. The evidence indicated that prior to the deceased's death, the defendant, who was his son and was acting under a power of attorney, transferred money from the deceased's brokerage account to Hong Kong and shortly after his death, transferred the money back to Ontario to a company controlled by the defendant and his brothers. Madam Justice Greer found that the money deposited in the company's account was a "specific fund" under rule 45.02 but that the money had not remained and was used for other purposes. Notwithstanding, and with no discussion of the case law concerning rule 45.02 or what constituted a "specific fund" under the rule, Greer J. ordered that the company sell specific liquid assets (mutual funds and GIC's) and pay the money into court. The learned judge stated in her consideration of the injunction portion of the motion that if she had not ordered payment under rule 45.02, she would have ordered some injunctive relief to protect the assets into which the deceased's money could be traced. In my view, and having regard to the authorities I have already referred to, I

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think that the decision is wrong to the extent that it holds that rule 45.02 can be invoked in the absence of the existence of a specific fund.

31 The plaintiff also relied upon the decision of the decision of Aitken J. in *Carleton University v. Mercier*, [2000] O.J. No. 1446 (Ont. S.C.J.). That case involved an interim preservation order pending the return of an interlocutory injunction. The learned motions judge noted that the test for an interim interlocutory injunction was the same as that for an interlocutory injunction and proceeded to review the facts of the case having regard to the three requirements — serious question to be tried; irreparable harm; and balance of convenience. He also referred to rule 45.02 in reference to the fact that if funds paid to the defendant were paid to third parties who appear not to be operating at arm's length from the defendant in apparent contradiction of the terms of a signed contract, he would have no hesitation in ordering their preservation pending a judicial determination of entitlement to the fund. Notwithstanding the reference to rule 45.02, the granting of the interim injunctive relief requested was, in my view, pursuant to the court's injunctive power and not pursuant to rule 45.02.

32 In *Aetna Financial Services Ltd. v. Feigelman*, [1985] 1 S.C.R. 2 (S.C.C.), the Supreme Court of Canada confirmed that courts in Canada have the power to grant a Mareva injunction to prevent a defendant from dealing with his assets or removing them from the jurisdiction in advance of judgment. Such an order can only be granted by a judge (Section 101(1), *Courts of Justice Act*, R.S.O. 1990, c. C.43). Rule 37.02 provides that the Master has the jurisdiction of a judge unless a statute or rule provides otherwise. Rule 40 provides that an interlocutory or mandatory injunction is within the jurisdiction of a judge.

33 In coming to the decision he did in this case, the Master stated that the order he was asked to make was not injunctive in nature. While that is the case in respect of an order pursuant to rule 45.02, in the absence of a specific fund, the order which the Master made is clearly injunctive and accordingly not within the Master's jurisdiction.

Trust

34 The defendant's second ground of appeal is that the Master erred in law in finding that the refund monies were trust monies and that the defendant committed a breach of trust by placing them in its bank account. The trust determination formed part of the Master's decision in relation to whether there was a specific fund and the defendant's argument that the monies were no longer available. In my view, the Master erred in making the finding that he did having regard to the issues and the record before him.

35 While the issue of whether the refund monies constituted trust funds is an issue in the action, it was not something that should have been determined on a rule 45.02 motion. The authorities are clear that in order for a trust to be found there must be evidence of the three certainties: certainty of intention to create a trust, certainty of subject matter and certainty of the objects: see *Howitt v. Howden Group Canada Ltd.* (1999), 170 D.L.R. (4th) 423 (Ont. C.A.). The record before the Master was not sufficient to support the Master's finding, particularly in respect of certainty of intention. Even if it was, I do not think that a finding of trust and a breach thereof was necessary to a determination of whether there was a specific fund. Rule 45.02 encompasses specific funds of all types, whether trust monies or otherwise. As already discussed, in the absence in this case of the existence of a specific fund, even if a trust fund were involved, rule 45.02 would not apply.

36 Accordingly, for the reasons given, I am of the view that in the absence of jurisdiction, the Master was clearly wrong in making the order he did. In the result, I would allow the appeal and set aside the order of the Master dated August 25, 2006.

37 The Master ordered costs in the cause of $2,000. In my view because the defendant was successful on the appeal it should have its costs, on a partial indemnity basis of both the appeal and the appearance before the Master. Accordingly I award the defendant costs fixed at $8750.00, including disbursements and GST, which amount includes $2,000 for the appearance before the Master.

Appeal allowed.

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Most Negative Treatment: Reversed
Most Recent Reversed: American Axle & Manufacturing Inc. v. Durable Release Coaters Ltd. | 2007 CarswellOnt 3444, [2007] G.S.T.C. 142, 49 C.P.C. (6th) 180, [2007] O.J. No. 2138, 86 O.R. (3d) 53, 157 A.C.W.S. (3d) 937 | (Ont. S.C.J., Jun 1, 2007)

2006 CarswellOnt 5273
Ontario Superior Court of Justice

American Axle & Manufacturing Inc. v. Durable Release Coaters Ltd.

2006 CarswellOnt 5273, [2007] G.S.T.C. 141, 150 A.C.W.S. (3d) 1026

American Axle & Manufacturing Ing. v. Durable Relase Coaters Limited

Master T.R. Hawkins

Heard: July 19, 2006
Judgment: August 25, 2006
Docket: 03-CV-255954CM 3

Counsel: Jean M. DeMarco, for Moving Plaintiff
Gregory M. Sidlofsky, for Responding Defendant

Subject: Goods and Services Tax (GST); Civil Practice and Procedure; Property

Related Abridgment Classifications

Civil practice and procedure
XV Preservation of property rights pending litigation
XV.2 Interim preservation of property

Headnote

Tax --- Goods and Services Tax — Importations
Plaintiff shipped gear rotors that it manufactured in Buffalo, New York across border to defendant in Mississauga, Ontario for coating and return to plaintiff — Plaintiff was "importer of record" on customs documents and paid GST on value of gear rotor shipments — Pursuant to refund agreement, defendant agreed to aid plaintiff in recovering past GST by applying for input tax credit on GST amounts already paid on rotors by plaintiff — Defendant received GST refund cheque, which it deposited into its operating account — Bank applied proceeds to pay down defendant's line of credit — Plaintiff commenced action — Plaintiff brought motion for order for interim preservation of property pursuant to R. 45.02 of Rules of Civil Procedure — Motion granted — Defendant was ordered to pay sum of $623,000 into court — Plaintiff made out strong prima facie claim to specific fund of refund monies which defendant received — Terms of refund agreement made it clear that any refund which defendant obtained from Canada Customs and Revenue Agency belonged to plaintiff, not defendant — Any refund monies obtained were indeed trust funds which defendant held in trust for plaintiff.

Tax --- Goods and Services Tax — Input tax credits — Who entitled
Plaintiff shipped gear rotors that it manufactured in Buffalo, New York across border to defendant in Mississauga, Ontario for coating and return to plaintiff — Plaintiff was "importer of record" on customs documents and paid GST on value of gear rotor shipments — Pursuant to refund agreement, defendant agreed to aid plaintiff in recovering past GST by applying for input tax credit on GST amounts already paid on rotors by plaintiff — Defendant received GST refund cheque, which it deposited into its operating account — Bank applied proceeds to pay down defendant's line of credit — Plaintiff commenced

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action — Plaintiff brought motion for order for interim preservation of property pursuant to R. 45.02 of Rules of Civil Procedure — Motion granted — Defendant was ordered to pay sum of $623,000 into court — Plaintiff made out strong prima facie claim to specific fund of refund monies which defendant received — Terms of refund agreement made it clear that any refund which defendant obtained from Canada Customs and Revenue Agency belonged to plaintiff, not defendant — Any refund monies obtained were indeed trust funds which defendant held in trust for plaintiff.

Civil practice and procedure --- Pre-trial procedures — Interim preservation of property
Plaintiff shipped gear rotors that it manufactured in Buffalo, New York across border to defendant in Mississauga, Ontario for coating and return to plaintiff — Plaintiff was "importer of record" on customs documents and paid GST on value of gear rotor shipments — Pursuant to refund agreement, defendant agreed to aid plaintiff in recovering past GST by applying for input tax credit on GST amounts already paid on rotors by plaintiff — Defendant received GST refund cheque, which it deposited into its operating account — Bank applied proceeds to pay down defendant's line of credit — Plaintiff commenced action — Plaintiff brought motion for order for interim preservation of property pursuant to R. 45.02 of Rules of Civil Procedure — Motion granted — Defendant was ordered to pay sum of $623,000 into court — Plaintiff made out strong prima facie claim to specific fund of refund monies which defendant received — Terms of refund agreement made it clear that any refund which defendant obtained from Canada Customs and Revenue Agency belonged to plaintiff, not defendant — Any refund monies obtained were indeed trust funds which defendant held in trust for plaintiff.

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Sun v. Ho (1998), 1998 CarswellOnt 995, 18 C.P.C. (4th) 363 (Ont. Gen. Div.) — followed

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 45.02 — considered

R. 60.11 — referred to

R. 60.12 — considered

MOTION by plaintiff for order for interim preservation of property pursuant to R. 45.02 of *Rules of Civil Procedure*.

Master Hawkins:

1 At the opening of this motion by the plaintiff the defendant moved for an order striking certain items from a brief of documents which the plaintiff had filed in support of its motion. Defence counsel complained that the plaintiff's brief documents contained items which were not properly identified, which were filed after the cross-examinations in connection with the plaintiff's motion were completed and which were filed after the defendant had the ability to file responding materials. I gave defence counsel two opportunities to have the plaintiff's motion adjourned to enable him to conduct further cross-examinations and to file further material, if so advised. He declined both these opportunities. In these circumstances I declined to exclude documents from the plaintiff's brief of documents on the ground of late filing.

2 In this motion the plaintiff seeks several distinct forms of relief. The parties wish me to hear first the plaintiff's motion for an interim preservation order, rule on that motion, and hear the balance of the plaintiff's motion later.

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3 The plaintiff moves for an order under subrule 45.02. That subrule provides as follows:

> Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

4 The plaintiff is a manufacturer of driveline systems, chassis systems and forged products for trucks, buses and cars. The plaintiff is located in Detroit, Michigan.

5 The defendant carries on the business of coating metal and formed products in Bramalea, Ontario.

6 Beginning in 2000 the plaintiff began shipping gear rotors to the defendant for coating. For several months the customs broker involved completed importation documents showing the plaintiff as the importer of record of the gear rotors being sent to the defendant in Bramalea, Ontario. In consequence the plaintiff had to pay and did pay goods and services tax on the value of each shipment of gear rotors. The plaintiff says that it paid over $697,000 in GST on these shipments over several months.

7 In the fall of 2000 the plaintiff learned that if the defendant were shown as the importer of record of the gear rotors the plaintiff would be exempted from paying GST on the value of the rotors in future and that the defendant could apply for an input tax credit or refund of the GST already paid by the plaintiff. By written agreement dated October 31, 2000 (the "Refund Agreement") the defendant agreed to assist the plaintiff in recovering the GST which the plaintiff had paid by applying for an input tax credit. This application was completely successful and in November 2002 the defendant received a refund of $697,537 from the Canada Customs and Revenue Agency.

8 Although the defendant does not claim to be entitled to this refund to the exclusion of the plaintiff, or that the plaintiff has never had any entitlement to this refund, the defendant did not forward the refund to the plaintiff. Rather the defendant deposited the refund cheque in its bank account. The defendant's bank applied the deposit proceeds to reduce the defendant's loan from the bank.

9 The plaintiff submits that the refund proceeds are a "specific fund" within the meaning of rule 45.02 the right to which is in question and that this court should order the bulk of the refund proceeds paid into court or otherwise secured pending trial. The plaintiff is seeking an order that the defendant pay only $623,000 of the refund proceeds into court because it acknowledges that some $75,000 in invoices from the defendant to the plaintiff are unpaid.

10 The defendant advances several arguments in response. First the defendant says that there is now no specific fund to preserve pending trial. Once the defendant deposited the refund cheque in its bank and the bank applied the deposit proceeds so as to reduce the defendant's loan (as the defendant knew the bank would) the defendant submits that any specific fund was gone.

11 This is not an answer to the plaintiff's motion. In *Leung Estate v. Leung*, [2004] O.J. No. 1417 (Ont. S.C.J.) Greer J. heard a motion for an order under rule 45.02. There one of the defendants had a power of attorney from his father. He used this power of attorney to remove funds from his late father's account at a stockbroker firm and later deposited the funds in the account of one of the corporate defendants. By the time the motion was brought the defendant son had spent some $1,200,000 of the funds. Greer J. held the money in the corporate defendant's account to be a specific fund under rule 45.02. She applied the test lad down by Rivard J. in *Sun v. Ho* (1998), 18 C.P.C. (4th) 363 (Ont. Gen. Div.) for motion under rule 45.02. There Rivard J. said the following (at paragraph 1).

> [F]irstly, under Rule 45.02 the plaintiff must establish a right to specific fund;
>
> secondly, there must be a strong prima facie case and,
>
> thirdly, the balance of convenience requires the court to inquire into the potential harm that would be incurred by the moving party if the relief is not granted.

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12 The fact that the defendant son had spent a large part of the funds in the corporate defendant's account did not defeat the rule 45.02 motion before Greer J. She ordered liquid assets of the corporate defendant to be cashed in and the proceeds paid into court.

13 In my view the plaintiff in this action has met the tripartite test which Rivard J. laid down in *Sun v. Ho*, supra. The terms of the Refund Agreement make it clear that any refund which the defendant obtained from Canada Customs and Revenue Agency belonged to the plaintiff, not the defendant. Although the Refund Agreement did not expressly refer to any refund obtained as being trust funds, the circumstances surrounding the refund application were such that any refund monies obtained were indeed trust funds which the defendant held in trust for the plaintiff.

14 The defendant has a counterclaim for damages based on the plaintiff's alleged breaches of the agreements for coating services between the parties. The defendant claims the right to apply the refund monies which it obtained in partial satisfaction of its claim for damages and to set off those damages against the plaintiff's claims. A trustee may not claim set-off against trust funds. See *Commercial Union Life Assurance Co. of Canada v. John Ingle Insurance Group Inc.*, [2000] O.J. No. 3289 (Ont. S.C.J.) per Stinson J. at paragraph 334.

15 The plaintiff has, on the evidence before me, made out a strong prima facie claim to the specific fund of refund monies which the defendant received.

16 The balance of convenience favours the granting of the order sought. There is a real potential of harm to the plaintiff if the order sought under rule 45.02 is not granted. The financial position of the defendant is delicate. The defendant says that it has the ability to comply with an order that it pay the net sum of $623,000 into court pending trial and that its future business prospects are positive. Set against this are the following facts. In the year ending November 30, 2005 the defendant had a large demand loan owing to a related corporation. It had net earnings of $68,452. Its financial statements do not take the current litigation into account. Most troubling is the fact that it has a deficit in retained earnings of $959,191.

17 I reject the defendant's argument that this motion should be dismissed because the defendant itself spent the refund monies by paying down its bank loan and a specific fund no longer exists. I regard the defendant's use of the refund monies as a breach of trust. The court is not anxious to see a litigant defeat a proceeding for reasons based on its own misconduct.

18 It is clear from the decision of Greer J. in *Leung Estate v. Leung*, supra, that the court may make an order under rule 45.02 that are responding party who has spent part of a specific fund restore the fund and pay the proceeds into court. It makes no difference that the responding party has spent all of the specific fund rather than part of it.

19 The order that I am asked to make is not injunctive in nature. Masters may make orders under rule 45.02. Masters may not grant injunctions. The remedy for non-compliance with a master's order for payment of money under rule 45.02 is not a contempt motion under rule 60.11 but rather a motion under rule 60.12 for failure to comply with an interlocutory order with a typical sanction being an order dismissing the non-complying party's proceeding or striking out the party's defence.

20 For all these reasons an order will issue that within 30 days the defendant is to pay the sum of $623,000 into court pending the trial of this action or further order of this court.

Motion granted.

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TAB 12

1994 CarswellOnt 4528
Ontario Court of Justice (General Division)

Rosen v. Homelife/St. Andrew's Realty Inc.

1994 CarswellOnt 4528, [1994] O.J. No. 2887, 51 A.C.W.S. (3d) 1254, 6 W.D.C.P. (2d) 27

Joanne Rosen, Plaintiff and Homelife/St. Andrew's Realty Inc. William Porteous and Aldo D'Aguanno, Defendants

MacFarland J.

Heard: December 1, 1994
Judgment: December 2, 1994
Docket: Newmarket 94-CQ58281

Counsel: Wendy J. Linden, for Plaintiff
Paul H. Caroline, for Defendants

Subject: Corporate and Commercial

Headnote

Commercial law

MacFarland J.:

1 The plaintiff is a licensed real estate agent, who at all material times was associated with the corporate defendant. The defendant William Porteous is the president of Homelife and Aldo D'Aguanno, a licensed real estate agent also associated with the corporate defendant.

2 The issues in this litigation concern the plaintiff's entitlement to certain commission monies received by the corporate defendant as the result of the completion of a certain real estate transaction with which the plaintiff had certain involvement.

3 The total commission owing to the corporate defendant as the result of this transaction is said by the plaintiff, to be $138,000.00, of which she is entitled to the sum of $111,100.00. Mr. Porteous admits in his affidavit that the corporate defendant did receive a payment in the sum of $138,000.00 in respect of the subject transaction, which he deposes were paid ... "in full and complete satisfaction of any and all claims which Homelife might make with regard to the Royal Bank's sale of certain lands to Kaitlin Holdings Ltd." Whether the monies are characterized as commission owing, or monies paid in settlement, is immaterial to the matter which I must determine.

4 It is admitted that Homelife, on November 2, 1994, received the sum of $138,000.00 in payment of the commission owing in respect of the subject transaction and have paid Ms. Rosen nothing to date in spite of her request that they do so.

5 The plaintiff claims that she is, by virtue of her agreement with Homelife, entitled to be paid $111,100.00. Her contract provides that she is required to pay an administrative fee of 30% of gross commission up to $80,000.00 and 5% of any gross commission earned beyond or above that amount. The defendants, Homelife and Porteous dispute the amount owing to the plaintiff. In his affidavit, Porteous claims both he and the defendant D'Aguanno were involved in the negotiations and the plaintiff had failed to live up to certain other parts of the contract with the defendant Homelife and was thereby not entitled to be paid commission in accordance with the formula set out above.

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6 There can be no doubt on the evidence before me, that Ms. Rosen had at least some significant involvement in this transaction. Mr. Porteous' own letter to the solicitors of the mortgagee dated October 5, 1994, is evidence of the fact. I have trouble with his statement in his affidavit filed, wherein he now says that letter was an attempt on his part to bolster the ego of the plaintiff. He does not, however, go so far as to say that the statement made in the letter was untrue.

7 When Ms. Rosen did not receive the commission money to which she felt she was entitled, despite her request that she be paid, she instructed her solicitor to write to the corporate defendant. That letter is dated November 7, 1994 and was sent both by facsimile transmission and by mail. The defendant admits receiving the $138,000.00 on November 2, 1994 and on November 15, 1994 transferring the funds to the operating account of the corporate defendant from where they were applied to satisfy an outstanding "...overdraft and/or Line of Credit..." owed by Homelife to its banker. The balance, some $28,000.00 according to the affidavit of Mr. Porteous, remained as a credit in the operating account of the company and has since been used for the day to day operating expenses of the corporate defendant.

8 The plaintiff seeks an order pursuant to the provisions of Rule 45.02 requiring that the defendants be required to pay into court the sum of $111,100.00.

9 I am satisfied that the $138,000.00, had it remained in the Homelife trust account, or even in the general account for that matter, would have constituted a specific fund as is contemplated by Rule 45.02. The difficulty here is that the funds have been disbursed.

10 Ms. Linden, on behalf of the plaintiff, argues that if I do not make the order she requests, it will send out the wrong message to litigants. It will, she says, encourage unscrupulous litigants to spend monies which they hold and entitlement to which, they know, is disputed. The obvious fear is that there will be no money left at the end of the litigation road with which to pay the judgment.

11 The heading or title for Rule 45 is "Interim Preservation of Property". In my view, the rule is intended for the preservation of property which is in existence and in the case of money, is a reasonably identifiable fund which can be earmarked to the litigation in issue. See *Rotin et al v. Lechcier-Kimel et al*, (1985) 3 C.P.C. (2nd) 15. In each of the cases to which counsel referred, the funds were available to be paid into court; in this case the specific fund is no longer available. Were I to make an order requiring this sum of money to be paid into court, the defendant against whom the order was made would have to obtain funds from other sources or his/its own resources. In my view, that is not what is contemplated by Rule 45.02. The rule provides jurisdiction, in my view, only for the "specific fund" to be paid into court and not, where that fund is no longer available, for other monies to be paid into court in lieu thereof.

12 In result therefor, the application is dismissed, but in the circumstances, without costs.

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TAB 13

2009 CarswellOnt 2032
Ontario Superior Court of Justice [Commercial List]

DSLC Capital Corp. v. Credifinance Securities Ltd.

2009 CarswellOnt 2032, [2009] O.J. No. 1568, 176 A.C.W.S. (3d) 1133

DSLC CAPITAL CORP. (Plaintiff) and CREDIFINANCE SECURITIES LIMITED, DONABO INC., GEORGES BENARROCH, MARJORIE ANN GLOVER, and CREDIFINANCE CAPITAL CORP. (Defendants)

Cameron J.

Heard: March 30-31, 2009; April 7, 2009
Judgment: April 20, 2009
Docket: 09-CL-8003

Counsel: Gregory Sidlofsky for Plaintiff
John L. Longo for Defendants, Credifinance Securities Limited, Marjorie Ann Glover
Fred Tayar for Defendants, Donabo Inc., Georges Benarroch, Credifinance Capital Corp.

Subject: Corporate and Commercial; Civil Practice and Procedure; Contracts

Related Abridgment Classifications

Business associations
III Specific matters of corporate organization
III.2 Shares
III.2.c Subscription for shares
III.2.c.i General principles

Business associations
V Legal proceedings involving business associations
V.3 Practice and procedure in proceedings involving corporations
V.3.a General principles

Debtors and creditors
XIII Loans
XIII.1 General principles

Remedies
II Injunctions
II.9 Form and operation of order
II.9.h Dissolution of injunction
II.9.h.i Prima facie case

Remedies
II Injunctions
II.9 Form and operation of order
II.9.h Dissolution of injunction
II.9.h.iii Balance of convenience

Remedies

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II Injunctions
  II.9 Form and operation of order
    II.9.h Dissolution of injunction
      II.9.h.viii Miscellaneous

Headnote

Business associations --- Specific corporate organization matters — Shares — Subscription for shares — General principles

Business associations --- Legal proceedings involving business associations — Practice and procedure in actions involving corporations — General principles

Debtors and creditors --- General principles — Loans

Remedies --- Injunctions — Form and operation of order — Dissolution of injunction — Grounds for dissolution — Prima facie case

Remedies --- Injunctions — Form and operation of order — Dissolution of injunction — Grounds for dissolution — Balance of convenience

Remedies --- Injunctions — Form and operation of order — Dissolution of injunction — Grounds for dissolution — Miscellaneous

Table of Authorities

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Rosen v. Homelife/St. Andrew's Realty Inc. (1994), 1994 CarswellOnt 4528 (Ont. Gen. Div.) — considered

Rotin v. Lechcier-Kimel (1985), 3 C.P.C. (2d) 15, 1985 CarswellOnt 405 (Ont. H.C.) — considered

United States v. Friedland (1996), 1996 CarswellOnt 5566 (Ont. Gen. Div.) — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
  R. 45.02 — considered

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Cameron J.:

Motions

1 This is a motion to continue until trial the interim Mareva injunction granted *ex parte* to DSLC Capital Corp. ("DSLC") by The Honourable Mr. Justice Morawetz dated February 6, 2009, as modified by me on February 12, 2009. I discontinued the injunction as against Marjorie Ann Glover but continued it as against the remaining defendants.

2 In the alternative, DSLC moves to have the $392,300 plus $1,600 U.S. loaned pursuant to the Subordinated Loan Agreement in the form required by the Investment Dealers Association ("IDA") paid into Court under Rule 45.02.

3 The defendants bring cross motions to dissolve the injunction on the grounds that:

1.) Morawetz J. was misled; and

2.) R. 45.02 is applicable only to a specific fund which does not exist here because of a commingling of funds.

4 The *ex parte* order of Morawetz J. on February 6, 2009, stated, in part:

> ...I am satisfied that the 3 part test set out in *RJR McDonald* has been satisfied and the requested ruling be granted.
>
> The plaintiff has established a strong *prima facie* case and in view of the relocation of Mr. Benarroch to France and the evidence that the National Bank account has been closed and the defendants are under an investigation conducted by IIROC - I am of the view that there is a serious risk of dissipation of assets if the relief sought is not granted.
>
> The plaintiff has established that in view of the allegations that damages may not provide an adequate remedy, and a freezing of assets is appropriate. I am also satisfied that the balance of convenience favours the plaintiff.
>
> An undertaking as to damages has been filed. ...

5 The undertaking was filed by DSLC.

6 Since July 1, 2008 the IDA has been known as the Investment Industry Regulatory Organization of Canada ("IIROC").

Salient Facts

7 Georges Benarroch had been a resident of France for over 10 years. He also had business interests in Florida where he visits four times a year for a week at a time. He comes to Canada five times a year for a week at a time and for vacations. There is no evidence of any property he owned in Canada. His home and cottage in Ontario were owned by his four sisters, children, nephews, nieces and himself through an off-shore family trust. He was Chairman of the Board, President and CEO of Credifinance and indirectly owned the shares of Credifinance.

8 Marjorie Glover has been the Treasurer and Chief Compliance Officer of Credifinance since 1991.

9 On September 30, 2005, Foundation Investment Partners Inc. ("Foundation"), a company in which Adam Szweras, David Carbonaro ("David") and John Lorenzo were principals, signed an Option Agreement to acquire a 10% interest in Credifinance Securities Ltd. ("Credifinance") for $250,000 and a purchase option to acquire a further 70% of Credifinance.

10 In reply to due diligence inquiries the IDA advised that "it is conducting an investigation into certain activities at Credifinance." Benarroch made David aware of the IDA letter. Foundation elected to terminate its initial 10% equity and the right to exercise the purchase option and Credifinance refunded the $250,000.

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11 Mr. Alistair Crawley, counsel for Credifinance, had met with David on December 16, 2005. He was unclear as to the specifics of the discussion. He said that the investigation was quite unfocussed. He recalled "having difficulty ascertaining the precise issues that the IDA was investigating."

12 Mr. Benarroch sent a fax to Fortune on December 18, 2005 which did not clarify the issue.

13 In 2006, Credifinance sold its seats on the TSE and MSE and declared a dividend of over $1 million. This effectively stripped Credifinance of its assets.

Share Subscription Agreement

14 In November 2007, when Credifinance Capital Corp. ("CCC") controlled Credifinance, DSLC entered a Share Subscription Agreement with Credifinance drafted by David. It recited that Credifinance was a licensed securities dealer and a member of the IDA. DSLC agreed to purchase the initial 100,000 common shares for $1,000 giving it 9.1% of the shares. In addition, it agreed to lend, by way of a subordinated loan agreement, $400,000 to Credifinance on closing which would be deposited in trust with counsel for DSLC pending a Uniform Subordinated Loan Agreement attached as a schedule. The representations and warranties would survive the closing for 3 years. They agreed to negotiate in good faith a Unanimous Shareholders Agreement to lend a further $1,600,000 by way of subordinated loans in not more than 36 monthly installments together with the purchase of 1,496,647 shares for 60% of the shares. Mr. Benarroch would serve as chairman of the board for 5 years and remain CEO of Credifinance until the aggregate of $2 million had been contributed by way of subordinated loans. John Lorenzo, Georges Benarroch and Anne Glover would be the directors subject to contrary agreement. The Share Subscription Agreement was subject to an "entire agreement" clause.

15 The IDA approved the transaction on January 17, 2008.

Uniform Subordination Agreement

16 The Uniform Subordination Agreement between DSLC, Credifinance and IIROC dated January 24, 2008 subordinated the $400,000 payment to the claims of the general creditors of Credifinance before DSLC could lay claim to it. Paragraph 7 of the Uniform Subordination Agreement provided that it could be terminated by IIROC "by notice in writing given to the Creditor and to the Member" (Credifinance).

17 The $400,000 was invested in a GIC until late October, 2008.

Guarantee of $25,000 Revenue

18 In the summer of 2007, when the Share Subscription Agreement was being discussed, Georges Benarroch agreed to contribute $25,000 monthly to Credifinance on account of expenses by responding "Looks fine" in an email on October 1, 2007. By the signing on November 13, he had changed his mind and refused to insert in the agreement any requirement that CCC contribute one-half of the monthly expenses of Credifinance. However, he did make the payments for 2007 and January and February, 2008, but not thereafter. He said it was pursuant to a Term Engagement Agreement dated May 1, 2007 between CCC and Credifinance to pay whatever he felt necessary and that there was no need for it after February 2008. DSLC thought that the $550,000 plus $400,000 loan would remain in Credifinance.

19 Mr. Lorenzo says Mr. Benarroch originally included the commitment of CCC and DSLC to generate a fee income of $25,000 each per month under Article 6 (f) (i) of the Share Subscription Agreement. It was later determined that Credifinance might not be determined by the IDA to have satisfied its revenue rules so they deleted the references to guaranteed fees by CCC and DSLC. However, the parties agreed to honour their commitments outside of the Share Subscription Agreement in accordance with memoranda in August 2007, agreed by both parties. DSLC abided by the commitment to generate at least $25,000 per month in order to maintain the account at about $550,000. This term requiring CCC and DSLC to guarantee fee income of $25,000 each was essential to DSLC. Ms. Glover sent invoices to DSLC requesting DSLC to pay $25,000 to

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Credifinance "in accordance with Agreement". It was not honoured by CCC after February 2008. Mr. Benarroch says there was no agreement.

20 After September 2008, DSLC made no further loans to Credifinance as Mr. Benarroch had not signed a shareholders' agreement under the Share Subscription Agreement and had not appointed Mr. Lorenzo or Robert to the board of directors.

21 Notwithstanding regular financial reporting to Robert, only mild complaint was made in an email as to non-payment of the $25,000 in June, 2008 and then not again until the Share Purchase Agreement and the explicit term that Mr. Benarroch would not contribute funds. In February 2008, Robert Carbonaro ("Robert"), brother of David, told Mr. Benarroch to vacate his office as he was "taking over" as CEO.

22 From April 15, 2008, on, Robert was developing business for Credifinance in the Middle East among wealthy people who were prepared to invest in Canadian securities.

23 He was Vice President and COO. Until his departure in December 2008, he or Mr. Lorenzo received all financial and other information requested from Marjorie Glover but he did not tell Morawetz J.

24 Robert discussed with Ms. Glover in February 2008 the investigation against Mr. Benarroch, Ms. Glover and Credifinance. She told him it had been dismissed on appeal in July, 2007 and that there had been nothing further since then. She did not mention an examination of Benarroch in April 2007 or a further request for information in July 2007 by IDA.

25 This was the same information that had been provided to John Lorenzo and David, on behalf of DSLC, in August 2007, by Mr. Benarroch when they were negotiating the Share Subscription Agreement between DSLC and Credifinance.

26 In 2008, CCC transferred its shares in Credifinance to Donabo Inc., a Nova Scotia company.

27 In the Fall of 2008, Mr. Benarroch refused to open any new accounts or hire staff pending negotiation and closing of a new purchase agreement.

Share Purchase Agreement

28 In the summer of 2008 it was decided that the Share Subscription Agreement was too complicated. DSLC and Donabo negotiated and signed on October 9, 2008, a Share Purchase Agreement between DSLC, as purchaser, and Donabo Inc., as vendor, for shares of Credifinance for $600,000, payable $350,000 on closing and $250,000 within 90 days. Closing was to be the later of October 31, 2008 or the date of regulatory approvals. There would be 4 directors with 3 nominated by the purchaser and one by the vendor. Among the vendor's representations was "that to the best of its knowledge and belief...(f) The material debts, contracts and liabilities, present or future, contingent or otherwise ... have been disclosed to the Purchaser (and accurately set out in the financial statements of the Corporation annexed hereto as Schedule "B")..." Georges Benarroch would be chairman of the board for 5 years at $75,000 per year plus payment of his disability insurance premiums of $20,000. The vendor would have no obligation to generate revenue for Credifinance. Approval of IIROC was a condition of closing. Donabo would continue to hold 15% of the shares. If the transaction did not close for any reason, the Share Purchase Agreement would terminate and the terms of the Share Subscription Agreement between DSLC and Credifinance of November 13, 2007 would reactivate.

IIROC Charges

29 On November 6, 2008, in an email from Mr. Fenton of Aird, Berlis, Credifinance was accusing DSLC of delay for failure to close, notwithstanding DSLC had not yet received consent from IIROC. They threatened to terminate the agreement if not closed by November 11 saying there were "regulatory reasons".

30 Mr. Crawley said he received a draft notice of hearing on November 7, 2008 for the purpose of setting a date to determine a hearing. He then advised Mr. Benarroch by telephone.

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31 Late on Thursday, November 13, 2008, Marjorie Glover of Credifinance received notice from IIROC of a hearing in the matter of Georges Benarroch, Marjorie Ann Glover, Linda Kent and Credifinance. The charges related to misconduct between January 2003 and March 2006 in respect of Magnum D'Or Resources Inc. and Osprey Gold Corp. It also related to Benarroch allegedly misleading IDA investigators between September 2005 and April 2007. Ms. Glover forwarded it to Mr. Benarroch on November 14, 2008. Mr. Benarroch sent it to Mr. Crawley, with whom he wanted to discuss it on November 14, 2008 before sending it to anyone else. It was not sent to DSLC.

32 The charges exposed the principals to fines of up to $1 million and Credifinance of a fine of up to $5 million and expulsion from membership in IIROC.

The Missed Closing

33 On Friday, November 14, 2008, IIROC sent notice to Robert that "it did not object to the purchase of an additional 833,000 shares of Credifinance from Donabo Inc. by DSLC."

34 On November 17, 2008, Robert discovered on the IIROC website the notice of hearing of November 13, 2008, independent of any efforts by Credifinance or its principals. Ms. Glover normally sent IIROC emails to Robert, but not that of November 13. Ms. Glover said she thought Mr. Benarroch had done so.

35 The charges resulted in a "contingent liability" for costs and expenses relating to the pending hearing and for fines and other penalties that may be imposed by IIROC. It also resulted in material impairment to the goodwill and market value of Credifinance.

36 On November 24, 2008, Credifinance terminated its Share Purchase Agreement. The Share Subscription Agreement was thus reactivated. Further, Mr. Benarroch declared DSLC in default of the Share Subscription Agreement since it had the obligation to provide up to $2 million in subordinated loans to Credifinance. However, it required that they negotiate in good faith a unanimous shareholders agreement. There was no firm agreement to lend the further $1.6 million until such an agreement was negotiated. None was signed.

37 Credifinance alleges that DSLC stalled in closing pending efforts to obtain the $350,000. It said DSLC's bank account showed that it did not have the $350,000 available to close the Share Purchase Agreement before Credifinance cancelled the agreement on November 24, 2008.

38 Mr. Lewis and Robert advised Mr. Fenton of Aird, Berlis on November 6, 2008 that DSLC was in funds to close, notwithstanding there was only $82,857 in the account. DSLC's bank account did not have the $350,000 necessary to close until November 25, 2008. On November 26 and 28, $130,000 was taken out and returned to investors.

Subsequent Events

39 DSLC demanded repayment of the loan of $400,000 in early December. Credifinance refused.

40 Robert resigned December 8, 2008, leaving substantial fees owing to him.

41 Credifinance took steps to close down retail operations and resign its membership in IIROC on December 23, 2008. It started to re-develop its M&A activity, advisory business and raising capital for clients by way of private placements or from institutional clients for which it did not need IIROC membership. It continued to deal with the closing of retail accounts, supervision of the preparation of Credifinance's termination audit, dealing with the IIROC investigation, closing of Canaccord accounts and termination of membership in IIROC.

42 Credifinance paid $20,645 to Benarroch in Paris as a consulting fee in January 2009. This was the first time such a payment was made. It was at the rate of about $5,000 or 3000 per month.

43 On February 10, 2009 Credifinance had $392,334.86 and $1,606.60 (U.S.) with National Bank and $150,257 with

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Canaccord. I released $40,000 on February 12 and $50,000 on March 19, 2009 to pay expenses. There should be at least $60,257 in Canaccord and $392,334 plus $1,606 (U.S.) in National Bank of Canada.

44 Credifinance's membership in IIROC was suspended on March 6, 2009 due to a deficiency of about $250,000 in firm capital after release of $40,000 on February 12, 2009.

45 On April 1, 2009 IIROC terminated the Subordinated Loan Agreement, removing IIROC's restriction on repayment of the loan. In doing so, IIROC noted $632,000 in cash to meet liabilities of $26,000 before subordinated loans of $400,000. This would leave about $56,000 available after the authorized payout of $90,000 on February 12 and March 19, 2009 and approximately $60,000 for expenses for December 24, 2008 to February 12, 2009 and the $20,300 for consulting fees to Mr. Benarroch.

46 Credifinance's lease of 2,000 sq. ft. of space in Yorkville for $6,600 per month expires at the end of 2009. It is trying to sublet some or all of the space. Ms. Glover and a bookkeeper are the only employees. Ms. Glover has been employed since 1991 and earns $78,000 per year.

The Law

Mareva Injunction

47 This case highlights the dilemma of a Mareva injunction. If dissolved, the defendant Mr. Benarroch may move the $460,000 or some large part of it offshore making execution of a judgment more difficult. Or, the money could be used to defend the claim on the loan and to prosecute a damage claim, thus reducing the amount available. On the other hand, if the injunction is maintained or the money paid into court, it will remain secure pending the outcome of the action for the recovery of the loan or damages, and for costs. This would be unfair to the defendant unless good grounds exist to justify the injunction.

48 A Mareva injunction is a highly unusual *ex parte* remedy. It is issued only if the applicant has a strong *prima facie* case of fraud sufficient to overcome the common law rule of no execution before judgment. The plaintiff must make a full and frank disclosure of material matters and fairly state the defendant's case. He must also show that there is a real and genuine risk the defendant will put his assets beyond his creditors for the purpose of avoiding judgment so as to render tracing remote. The defendant is entitled to use his assets to carry on his business but he is not entitled to dissipate his assets or remove his assets to avoid judgment. Further, the plaintiff must show irreparable harm that can't be compensated in damages and that the balance of convenience favours him. See *Chitel v. Rothbart* (1982), 39 O.R. (2d) 513 (Ont. C.A.); *Aetna Financial Services Ltd. v. Feigelman* (1985), 15 D.L.R. (4th) 161 (S.C.C.) . If there is a material non-disclosure or misstatement, the injunction must be set aside as a matter of right, without regard to whether the injunction might be sustainable on the basis of a corrected record: See *United States v. Friedland*, [1996] O.J. No. 4399 (Ont. Gen. Div.)per Sharpe. J. at p. 178.

49 The plaintiff wishes to tie up money which could otherwise be used on expenses such as payment of suppliers in the ordinary course, salaries and termination pay for employees, rent coming due by the end of the lease term and legal fees to resist the action. All such expenses will reduce the money available to satisfy any judgment.

Rule 45.02

50 Alternatively, the plaintiff seeks an order under Rule 45.02 which reads as follows: Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

51 In order to succeed:

a) the plaintiff must claim a right to a specific fund;

b) there is a serious issue to be tried regarding the plaintiff's claim to that fund;

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c) the balance of convenience favours granting the relief sought by the plaintiff.

See *News Canada Marketing Inc. v. TD Evergreen*, 2000 CarswellOnt 3544 (Ont. S.C.J.).

52 The requirement of a strong *prima facie* case does not apply to R. 45.02. However, it is an extreme remedy and judicial discretion, including a serious issue to be tried, irreparable harm and balance of convenience favouring the plaintiff, should be exercised before an order is made. *American Axle & Manufacturing Inc. v. Durable Release Coaters Ltd.* (2007), 86 O.R. (3d) 53 (Ont. S.C.J.).

Specific Fund

53 In *Rotin v. Lechcier-Kimel*, [1985] O.J. No. 466 (Ont. H.C.) White J. stated:

> In my opinion, "Specific fund" ... means a reasonably identified fund earmarked to the litigation in issue. That which a mortgagor owes on a mortgage is a mere chose in action and ... has not assumed the status of a specific fund.

54 In *Rosen v. Homelife/St. Andrew's Realty Inc.*, [1994] O.J. No. 2887 (Ont. Gen. Div.) McFarland J. said:

> ...the rule is intended for the presentation of property which is in existence and in the case of money, is reasonably identifiable fund which can be earmarked to the litigation in issue ... The rule provides jurisdiction ... only for the "specific fund" to be paid into court and not, where the fund is no longer available, for other monies to be paid into court in lieu thereof.

55 In *Assante Financial Management Ltd. v. Dixon*, [2004] O.J. No. 2237 (Ont. S.C.J.) para. 28 Wilton-Siegel J. noted that there was a "subtle but important difference between an amount that may be owing to the plaintiff and a right of the plaintiff to a fund". The plaintiff had only established a possible claim for payment of damages leased on an alleged breach of contract. Therefore the plaintiff was really seeking execution before judgment rather than preservation of a specific fund.

56 To the extent the funds have been commingled, they cannot be subject to R. 45.02. To the extent they have not been commingled, I see no reason why they cannot be subject to R. 45.02. They are the remaining integral part of the $407,500.

57 The plaintiff claims it is entitled to the $407,524 originally held in a GIC with National Bank of Canada. It was held in a GIC until October 27, 2008 and then was placed in its bank account and used, to the extent of some $43,000, to pay creditors' expenses. It reached as low as $364,000 on December 31, 2008 and is now at $392,334.86 plus $1,606.60 (U.S.). Subject to examination, these expenses appear to be in the normal course of business with the possible exception of the $20, 300 consulting fee. I hold that while there was some commingling of monies, $310,500 constitutes a specific fund to which the plaintiff lays claim. To the extent of $310,500 of the $407,524, there was no commingling of funds.

Discussion

Possible Risk of Removal

58 Mr. Benarroch has lived in Paris for 10 years. There is evidence that he periodically visits a home in the Annex of Toronto and his family cottage in Ontario. These properties are owned by a foreign trust for his family, not by Mr. Benarroch. He refused to answer questions about other property he may own in Ontario. There is no evidence he owns any property or other assets in Ontario. Subject to the injunction, he may take the $392,334 and $1,606 (U.S.) and $60,200 and move it offshore. He has already taken $20,300 by way of management fees from the company in 2009 and had it paid to Paris. I see nothing to prevent his taking more offshore. If he does, it is gone with nothing to replace it. He could, but not necessarily would, take these assets offshore.

Contribute $25,000 Monthly

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59 On October 1, 2007 Mr. Lorenzo suggested in an email that Benarroch invest $25,000 or so a month in Credifinance as one-half the expenses and to maintain cash at $550,000 to $600,000. Benarroch replied in an email "Looks fine" and then went on to arrange to meet Lorenzo at the Café de la Paix in Paris. David, who drafted the Share Subscription Agreement, was persuaded to omit this from the agreement and to put an "entire agreement" clause in the agreement. He says it was because there already was a letter agreement or at least they had orally agreed to contribute equally. Notwithstanding this, Benarroch paid the $25,000 in January and February 2008 and then ceased. Mr. Benarroch said it was payable pursuant to a Term Engagement dated May 1, 2007 by CCC but was no longer required after February, 2008. Robert, who was producing fee-paying business totalling more than $25,000 per month on behalf of DSLC, raised the issue in June 2008. Benarroch replied with a collateral argument. Nothing further was heard of the matter until the Share Purchase Agreement which said he would not have to contribute. It is debatable whether there was a commitment to contribute. This was not enunciated in the materials before Morawetz J. The judge was left with the impression that there was a clear obligation to contribute.

Non-Appointment of Lorenzo

60 In para. 27 of the motion record Mr. Lorenzo complained that he was not appointed as a director of Credifinance. However, Mr. Lorenzo had earlier said that he was not an expert in securities dealers' financing and Robert would have been a better nominee as director. In fact Mr. Benarroch appointed neither.

61 Paragraph 43 of the motion record said that the defendants failed to produce any financial reporting to DSLC. Robert was provided with everything he asked for from January to November, 2008.

The $400,000

62 DSLC said in the *ex parte* Motion Record at paragraph 51 of Mr. Lorenzo's affidavit, referring to December 2008:

> ...following the demand for repayment of the $400,000 loan, the defendants proceeded to close the account with National Bank of Canada in which the loan was deposited and held. It is unknown what the defendants did with the proceeds of the loan.

At para. 53 Mr. Lorenzo said:

> ...It is alleged in the notice of claim that Benarroch and Glover conspired to convert the loan to their own use and dissipated it. Other than the approximate $80,000.00 in commissions owed to Carbonaro and Michael, there were no creditors of Credifinance that would have had a priority claim to the loan and the $400,000 ought to have been repaid to DSLC subject to the approval of the IIROC which had already been requested.

At para. 55:

> ...DSLC alleges in the notice of action that the defendants have converted these funds to their own use and otherwise dissipated the funds so that they are not available to pay amounts owing to DSLC.

63 Paragraph 51 is wrong. Ms. Glover asked Robert about liquidation of the GIC but he did not respond. Nothing required that the $400,000 be kept in any particular form or instrument. Ms. Glover liquidated it on October 27, 2008. The National Bank account was still open. There were no grounds for saying it had been removed.

64 Paragraph 53 states as sworn evidence what is unsworn in the Notice of Claim but that is not in fact correct. There are also claims for rent, salary, telephone and other supplies and termination pay. The terms of the Subordinated Loan Agreement required that it be available to other creditors in the ordinary course of business before DSLC could lay claim to the funds. It did not say DSLC would rank equally with those other creditors. That only changed when the Subordinated Loan Agreement was cancelled on April 1, 2009.

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65 Paragraph 55 is clearly wrong. The defendants have not converted those funds materially below the $400,000 or converted them to their own use and have not dissipated them. There is no evidence of dissipation. There was only suspicion. This was not drawn to the attention of Morawetz J.

66 However, because they failed to contribute the $25,000 per month the defendants used the funds in Canaccord and the $400,000 to pay the continuing expenses. If they had contributed $25,000 per month towards expenses there would have been about $200,000 more in Credifinance.

67 I find there is still about $395,000 in Credifinance, plus another $60,000 in Canaccord, after allowing for expenses of $90,000 which I have approved.

DSLC Not Aware of Investigation

68 While representing Fortune in 2005, David learned of an IDA investigation. In August 2007, Mr. Lorenzo and David were advised of the IDA charges and were told Credifinance's appeal had been successful. Robert discussed the charges with Ms. Glover in February 2008 and was told the same thing and that there had not been any activity on the investigation for many months. They had read the appeal decision of July 2007. It was not apparent to them from the appeal decision that there were also misconduct charges continuing to be investigated. Mr. Crawley's evidence of December 2005 confirms this. Credifinance suggests otherwise. Having read the decision of the appeal panel three times, I agree with DSLC that there were no other charges apparent or pending. IIROC would certainly not tell Credifinance or anyone else that it was investigating charges. DSLC was not aware of further "misconduct" charges or that they were still under investigation. The November 13, 2008 charges, discovered on November 17, were a surprise to DSLC and raised a problem with the Credifinance finances and membership in IIROC so essential to DSLC.

69 Mr. Benarroch said, after receiving the November 13 notice, that he wanted to discuss it with Mr. Crawley first before advising DSLC. Ms. Glover said it was an oversight that it was not sent to DSLC. DSLC was not aware of it until Monday, November 17, 2008. It is a question of fact whether there was an effort to conceal the hearing until the transaction closed.

70 Credifinance's March 31, 2007 statements issued in August 2007 noted the success of the appeal decision in July 2007. However, the March 31, 2008 statements issued in 2008 made no reference to the investigation of the IDA charges. Mr. Benarroch said that IIROC did not require that statements disclose a continuing investigation if no charges had been laid. IIROC concurred with this non-disclosure in the Spring of 2008.

DSLC Insolvent

71 In February 2009, when DSLC gave its undertaking to pay damages, it appears DSLC was insolvent. It had $2,000 in cash and subject to Credifinance's expenses, $407,000 or less repayable by Credifinance. It had about $750,000 in shareholder loans. Accordingly, it was $341,000, or more, in deficit. If liable for $2 million plus costs on default of the Share Subscription Agreement it was seriously in deficit. This shortfall was not made apparent to Morawetz J. before granting the injunction. The defendants claim that the undertaking is insufficient.

U.S. Lawsuit

72 CCC and Credifinance were engaged in litigation with some U.S. investors. Mr. Benarroch did not tell DSLC or the auditors of this litigation because they were fully indemnified by BMB Munai, a large public company which was a co-defendant. It was not noted on the financial statements. Mr. Benarroch says IIROC did not require disclosure. DSLC says it was misled.

Other Expenses

73 Credifinance paid Ms. Glover and a bookkeeper but the employees did other work for Mr. Benarroch besides the

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normal course of business for Credifinance. Credifinance was also using its funds to pay the legal fees of all the defendants and it would be liable for supplier costs, termination costs for these employees and for continued payment of rent to the expiry of the term in January 2010. DSLC says these are not costs for which it should be liable. Further, these costs could well eat into the $407,000.

Conclusion

74 I am satisfied that if the injunction were dissolved, Mr. Benarroch could move the funds offshore so as to render tracing remote. If he does so, the plaintiff will be irreparably harmed. The balance of convenience clearly favours the plaintiff. Donabo and CCC are not subject to the order of the Ontario courts so no order by this court would affect them.

75 However, the plaintiff did not make a full and frank disclosure of material matters and fairly state the defendant's case in respect of the errors noted in paras. 43, 51, 53 and 55 of his affidavit, the "obligation" to pay $25,000 per month and in respect of the solvency of the plaintiff in giving the undertaking. Mr. Lorenzo was substantially speculative with respect to the location of the $407,000 after liquidating the GIC. Mr. Lorenzo obviously did not know things Robert knew but this lack of communication must fall at the feet of the plaintiff.

76 There was also no evidence presented to Morawetz J. that Mr. Benarroch or CCC may or may not be obliged to pay $25,000 per month by way of sharing expenses. The plaintiff made much of this point and it deserved to be presented to Morawetz J. fairly.

77 There is much evidence of fraud but I do not think the plaintiff had made out a strong *prima facie* case of fraud.

78 A strong *prima facie* case of fraud is not a consideration under R. 45.02. However, there must be a specific fund. The $407,000 was commingled with other funds but at any month-end it never fell below $364,742.72 on December 31, 2008 and on February 10, 2009 it stood at $392,334.56 plus $1,606.66 (U.S.). To the extent the $407,000 was depleted, there was no depletion of the original fund, according to the General Ledger Activity for January, 2009, below $310,500. I find a specific fund of $310,500 remaining.

Disposition

79 I order the defendant Credifinance to pay $310,500 into court under R. 45.02 pending the ultimate disposition or settlement of this action whereupon the injunction will be dissolved and terminated.

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TAB 14

COURT FILE NO.: 188/09
DATE: 20090723

ONTARIO

SUPERIOR COURT OF JUSTICE

DIVISIONAL COURT

B E T W E E N:	)	
DSLC CAPITAL CORP.	)	Gregory Zidlofsky, for the Plaintiff
Plaintiff	)	
- and -	)	
CREDIFINANCE SECURITIES LIMITED, DONABO INC., GEORGES BENARROCH, MARJORIE ANN GLOVER, and CREDIFINANCE CAPITAL CORP.	)	John Longo, for the Defendants
Defendants	)	
	)	**Heard: June 10, 2009**

Ellen Macdonald J.

REASONS FOR DECISION

[1] The Defendant, Credifinance Securities Limited ("Credifinance") seeks leave to appeal the order of the Honourable Mr. Justice Cameron made on April 20, 2009. Justice Cameron ordered Credifinance to pay $310.500 into court pursuant to rule 45.02. Rule 45.02 states:

> Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

[2] The motion before Justice Cameron was heard on March 30, 31, and April 7, 2009. The motion sought to continue until trial the interim *Mareva* injunction granted *ex parte* to DSLC Capital Corp. ("DSLC") by Justice Morawetz on February 6, 2009. The order of Justice Morawetz was modified by Justice Cameron on February 12, 2009, when he discontinued the injunction as against Marjorie Ann Glover, but continued it as against the remaining Defendants.

[3] Credifinance (the moving party) requests that this court grant leave to appeal from the order of Justice Cameron with costs. According to rule 62.02(4), leave to appeal to the Divisional Court shall not be granted unless:

> (a) there is a conflicting decision by another judge or court in Ontario or elsewhere on the matter involved in the proposed appeal and it is, in the opinion of the judge hearing the motion, desirable that leave to appeal be granted; or
>
> (b) there appears to the judge hearing the motion good reason to doubt the correctness of the order in question and the proposed appeal involves matters of such importance that, in his or her opinion, leave to appeal should be granted.

[4] In this motion, Credifinance submits that the requirements of both r. 62.02(4)(a) and (b), above, are met here. First, with respect to (4)(a), it submits that there are conflicting decisions on the matters raised in the proposed appeal, and that it is desirable that leave to appeal be granted, since litigants in Ontario would benefit from a pronouncement by a full panel of the Divisional Court as to the scope of rule 45.02 jurisdiction.

[5] Second, even if the requirements of (4)(a) are not met, Credifinance submits that the requirements of (4)(b) are met. There is reason to doubt the correctness of Justice Cameron's finding that a specific fund ever existed. Further, even if there was a specific fund at one time, Justice Cameron ought to have found that it ceased to exist once it was commingled with other funds. These doubts are significant not only as they relate to this case, and not only as they relate to this parties. Rather, they are of such general importance to the development of law and the administration of justice, that leave to appeal should be granted.

[6] DSLC counters that there are no decisions that conflict with the order appealed from, and no reasons to doubt the correctness of this order. Rather, Justice Cameron correctly found that the $310,500 in question was a specific fund. Further, DSLC submits that the order is of significance only to the parties, and that there are no general issues of public importance raised by Credifinace in this motion for leave.

[7] It is common ground that for the court to grant an order under rule 45.02, the following requirements must be met: (a) the plaintiff must claim a right to a specific fund; (b) there must be a serious issue to be tried regarding the plaintiff's claim to the fund; and (c) the balance of

convenience must favour granting the relief sought. This motion for leave concerns the first branch of this three-part test. Justice Cameron's reasons with respect to this branch are detailed and comprehensive. I refer specifically to paras. 56 and 57 of his decision:

> To the extent the funds have been commingled, they cannot be subject to R. 45.02. To the extent they have not been commingled, I see no reason why they cannot be subject to R. 45.02. They are the remaining integral part of the $407.500.
>
> The plaintiff claims it is entitled to the $407,524 originally held in a GIC with National Bank of Canada. It was held in a GIC until October 27, 2008 and then was placed in its bank account and used, to the extent of some $43,000, to pay creditors' expenses. It reached as low as $364,000 on December 31, 2008 and is now at $392,334.86 plus $1,606.60 (U.S.). Subject to examination, these expenses appear to be in the normal course of business with the possible exception of the $20,300 consulting fee. I hold that while there was some commingling of monies, $310,500 constitutes a specific fund to which the plaintiff lays claim. To the extent of $310,500 of the $407,524, there was no commingling of funds.

[8] I agree with Credifinance that a party seeking a rule 45.02 order must claim a specific fund, and that even where a specific fund is claimed, a rule 45.02 order may be rendered unavailable to the extent that the specific fund has been commingled with other funds. The jurisprudence is clear on these points.

[9] Upon a thorough review of the record before Justice Cameron and the record before this court, however, I see no good reason to doubt the findings of Justice Cameron that these requirements were met in this case. A specific fund was defined in *Rotin v. Lechcier-Kimel*, [1985] O.J. No. 466 (H.C.J.), as "a *reasonably* identifiable fund earmarked to the litigation in issue" (emphasis added). It was reasonable for Justice Cameron to find that the right of DSLC to a specific fund was in question, notwithstanding that that DSLC's claim is sounded in damages. Further, it was reasonable for him to find that while this fund was no long traceable in its entirety, there remained $310,500 which were directly traceable to the original fund, and which had not been commingled. There is therefore no conflict between Justice Cameron's order and the case law concerning Rule 45.02, nor is there any other good reason to doubt the former's correctness.

[10] Given my finding that Justice Cameron's order is consistent with the case law, and that there is no other good reason to doubt its correctness, it is my opinion that an appeal is neither desirable, nor necessary to ensure the resolution of matters of public importance.

[11] For these reasons, this application for leave to appeal is dismissed.

[12] During oral submissions, counsel agreed that there would be no costs awarded if Credifinance proved successful on this motion, and that DSLC would receive $3,000 in the event this motion was dismissed. Accordingly, costs are awarded to DSLC in the amount of $3,000.

Ellen Macdonald J.

Released: July 23, 2009

COURT FILE NO.: 188/09
DATE: 20090723

ONTARIO

SUPERIOR COURT OF JUSTICE

DIVISIONAL COURT

BETWEEN:

DSLC CAPITAL CORP.

Plaintiffs

- and -

CREDIFINANCE SECURITIES LIMITED, DONABO INC., GEORGES BENARROCH, MARJORIE ANN GLOVER, and CREDIFINANCE CAPITAL CORP.

Defendants

REASONS FOR DECISION

Ellen Macdonald J.

TAB 15

2009 CarswellOnt 7350
Ontario Superior Court of Justice (Divisional Court)

167986 Canada Inc. v. GMAC Commercial Finance Corp.-Canada/Societe Financiere Commerciale GMAC-Canada

2009 CarswellOnt 7350, [2009] O.J. No. 4976, 182 A.C.W.S. (3d) 1060, 258 O.A.C. 100, 66 B.L.R. (4th) 41, 80 C.P.C. (6th) 251

167986 CANADA INC. (Applicant / Appellant) and GMAC COMMERCIAL FINANCE CORPORATION-CANADA/SOCIÉTÉ FINANCIÈRE COMMERCIALE GMAC-CANADA, BLACK SAXON QRC INC. and QRC LIMITED PARTNERSHIP (Respondents / Respondents on Appeal)

Whalen, Dambrot, Swinton JJ.

Heard: November 6, 2009
Judgment: November 25, 2009
Docket: Toronto 234/09

Proceedings: affirming *167986 Canada Inc. v. GMAC Commercial Finance Corp.-Canada/Societe Financiere Commerciale GMAC-Canada* (2009), 2009 CarswellOnt 2690, 75 C.P.C. (6th) 265 (Ont. S.C.J. [Commercial List])

Counsel: Alan Lenczner, Philip Cho for Applicant / Appellant
Alan B. Mersky, Katherine Smirle for Respondent, GMAC Commercial Finance Corporation-Canada/Société Financière Commerciale GMAC-Canada
Daniel S. Murdoch for Respondents, Black Saxon QRC Inc., QRC Limited Partnership

Subject: Corporate and Commercial; Civil Practice and Procedure; Property; Contracts; Insolvency

Related Abridgment Classifications

Bills of exchange and negotiable instruments
V Letters of credit

Civil practice and procedure
XV Preservation of property rights pending litigation
XV.2 Interim preservation of property

Debtors and creditors
I General principles
I.4 Miscellaneous

Guarantee and indemnity
II Guarantee
II.1 Contract of guarantee
II.1.b Existence of guarantee

Guarantee and indemnity
IV Practice and procedure
IV.1 Guarantee
IV.1.i Miscellaneous

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Remedies
II Injunctions
II.1 Principles relating to availability of injunctions
II.1.g Existence of legal or equitable right capable of enforcement

Headnote

Bills of exchange and negotiable instruments --- Letters of credit
Applicant 167 Inc. had long-standing relationship with S Ltd., who entered into loan agreement with GMAC — 167 Inc. agreed to enter loan agreement as third party guarantor and provide letter of credit to GMAC — GMAC entered into forbearance agreement with S Ltd. as it attempted to restructure — S Ltd. obtained protection under Companies' Creditors Arrangement Act — 167 Inc. became aware of forbearance agreement — When letter expired, 167 Inc. directed GMAC to convert it into cash collateral — 167 Inc. took position that cash collateral was not assignable, and that forbearance agreement invalidated loan agreement — GMAC advised 167 Inc. of intent to assign cash collateral to another firm — 167 Inc. applied for determination of whether its obligations under loan agreement were terminated — 167 Inc.'s motion for preservation order directing payment into court of cash collateral pending determination of application was dismissed — 167 Inc. appealed — Appeal dismissed — Motions judge correctly held that cash collateral was not specific fund against which 167 Inc. could make proprietary claim — Funds paid on letter of credit were property of issuing bank, and loan agreement did not create proprietary claim to specific fund — Until liquidation occurred, 167 Inc. had no claim to any part of cash collateral funds — Wording of agreement permitting GMAC to commingle cash collateral with its own funds indicated there was no specific fund.

Guarantee and indemnity --- Guarantee — Contract of guarantee — Miscellaneous issues
Applicant 167 Inc. had long-standing relationship with S Ltd., who entered into loan agreement with GMAC — 167 Inc. agreed to enter loan agreement as third party guarantor and provide letter of credit to GMAC — GMAC entered into forbearance agreement with S Ltd. as it attempted to restructure — S Ltd. obtained protection under Companies' Creditors Arrangement Act — 167 Inc. became aware of forbearance agreement — When letter expired, 167 Inc. directed GMAC to convert it into cash collateral — 167 Inc. took position that cash collateral was not assignable, and that forbearance agreement invalidated loan agreement — GMAC advised 167 Inc. of intent to assign cash collateral to another firm — 167 Inc. applied for determination of whether its obligations under loan agreement were terminated — 167 Inc.'s motion for preservation order directing payment into court of cash collateral pending determination of application was dismissed — 167 Inc. appealed — Appeal dismissed — Motions judge correctly held that cash collateral was not specific fund against which 167 Inc. could make proprietary claim — Motions judge properly determined that law of guarantee did not apply to agreement, regardless of title given by parties — Because of qualities of letter of credit, including its critical difference from guarantee, its use as form of security was fundamental part of substance of agreement — Agreement was not contract of guarantee, since only recourse available to GMAC was right to letter of credit or cash collateral derived from it — 167 Inc.'s obligation under agreement was primary obligation to provide letter of credit on which GMAC could draw if proper documents were presented to bank.

Civil practice and procedure --- Pre-trial procedures — Interim preservation of property
Applicant 167 Inc. had long-standing relationship with S Ltd., who entered into loan agreement with GMAC — 167 Inc. agreed to enter loan agreement as third party guarantor and provide letter of credit to GMAC — GMAC entered into forbearance agreement with S Ltd. as it attempted to restructure — S Ltd. obtained protection under Companies' Creditors Arrangement Act — 167 Inc. became aware of forbearance agreement — When letter expired, 167 Inc. directed GMAC to convert it into cash collateral — 167 Inc. took position that cash collateral was not assignable, and that forbearance agreement invalidated loan agreement — GMAC advised 167 Inc. of intent to assign cash collateral to another firm — 167 Inc. applied for determination of whether its obligations under loan agreement were terminated — 167 Inc.'s motion for preservation order directing payment into court of cash collateral pending determination of application was dismissed — 167 Inc. appealed — Appeal dismissed — Motions judge did not determine merits of underlying application, but merely found that 167 Inc. did not even meet low threshold of whether there was serious issue to be tried with respect to its claim to cash collateral — Motions judge correctly held that cash collateral was not specific fund against which 167 Inc. could make proprietary claim — Motions judge properly determine that law of guarantee did not apply to agreement, regardless of title given by parties, since it was letter of credit rather than guarantee.

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Guarantee and indemnity --- Practice and procedure — Guarantee — General principles
Applicant 167 Inc. had long-standing relationship with S Ltd., who entered into loan agreement with GMAC — 167 Inc. agreed to enter loan agreement as third party guarantor and provide letter of credit to GMAC — GMAC entered into forbearance agreement with S Ltd. as it attempted to restructure — S Ltd. obtained protection under Companies' Creditors Arrangement Act — 167 Inc. became aware of forbearance agreement — When letter expired, 167 Inc. directed GMAC to convert it into cash collateral — 167 Inc. took position that cash collateral was not assignable, and that forbearance agreement invalidated loan agreement — GMAC advised 167 Inc. of intent to assign cash collateral to another firm — 167 Inc. applied for determination of whether its obligations under loan agreement were terminated — 167 Inc.'s motion for preservation order directing payment into court of cash collateral pending determination of application was dismissed — 167 Inc. appealed — Appeal dismissed — Motions judge did not determine merits of underlying application, but merely found that 167 Inc. did not even meet low threshold of whether there was serious issue to be tried with respect to its claim to cash collateral — Motions judge correctly held that cash collateral was not specific fund against which 167 Inc. could make proprietary claim — Motions judge properly determined that law of guarantee did not apply to agreement, regardless of title given by parties — Because of qualities of letter of credit, including its critical difference from guarantee, its use as form of security was fundamental part of substance of agreement — Agreement was not contract of guarantee, since only recourse available to GMAC was right to letter of credit or cash collateral derived from it.

Debtors and creditors --- General principles — Miscellaneous issues
Preservation order — Applicant 167 Inc. had long-standing relationship with S Ltd., who entered into loan agreement with GMAC — 167 Inc. agreed to enter loan agreement as third party guarantor and provide letter of credit to GMAC — GMAC entered into forbearance agreement with S Ltd. as it attempted to restructure — S Ltd. obtained protection under Companies' Creditors Arrangement Act — 167 Inc. became aware of forbearance agreement — When letter expired, 167 Inc. directed GMAC to convert it into cash collateral — 167 Inc. took position that cash collateral was not assignable, and that forbearance agreement invalidated loan agreement — GMAC advised 167 Inc. of intent to assign cash collateral to another firm — 167 Inc. applied for determination of whether its obligations under loan agreement were terminated — 167 Inc.'s motion for preservation order directing payment into court of cash collateral pending determination of application was dismissed — 167 Inc. appealed — Appeal dismissed — Motions judge did not determine merits of underlying application, but merely found that 167 Inc. did not even meet low threshold of whether there was serious issue to be tried with respect to its claim to cash collateral — Motions judge correctly held that cash collateral was not specific fund against which 167 Inc. could make proprietary claim — Motions judge properly determined that law of guarantee did not apply to agreement, regardless of title given by parties.

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Generally — referred to

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36
Generally — referred to

Rules considered:

Rules of Civil Procedure, R.R.O. 1990, Reg. 194
R. 45.02 — considered

APPEAL by 167986 Inc. from judgment reported at *167986 Canada Inc. v. GMAC Commercial Finance Corp.-Canada/Societe Financiere Commerciale GMAC-Canada* (2009), 2009 CarswellOnt 2690, 75 C.P.C. (6th) 265 (Ont. S.C.J. [Commercial List]), dismissing its motion for preservation order.

Swinton J.:

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Overview

1 167986 Canada Inc. ("167") appeals with leave from the order of Morawetz J. dated May 14, 2009, in which he dismissed 167's motion under rule 45.02 for an order preserving a certain sum of money. At issue in this appeal is the application of the law relating to guarantees to the rights and obligations under a Letter of Credit Agreement between 167 and GMAC Commercial Finance Corporation-Canada ("GMAC").

The Background

2 On January 9, 2006, GMAC entered into a Loan Agreement to provide a revolving credit facility to SAAN Stores Ltd., a company operating a chain of discount retail stores. 167 is a long-term supplier of goods to SAAN and, as it was owed money for goods sold to and received by SAAN, it was also a creditor of SAAN.

3 The Loan Agreement was altered three times, the third time on June 21, 2007. Prior to the third change, GMAC indicated that it was prepared to increase its lending to SAAN if a third party guaranteed a portion of the increased lending. 167 came forward as a guarantor and entered into an agreement with GMAC and SAAN entitled the Letter of Credit Agreement ("LC Agreement").

4 Under the LC Agreement, 167 agreed to obtain a Letter of Credit from the Bank of Montreal ("the Bank") in the amount of $3.5 million. Section 2.01 of the agreement begins with the words "Limited Recourse Guarantee". In the first sentence, 167, defined as the Investor, "unconditionally guarantees and promises to pay to the Lender, on demand" the indebtedness of SAAN (defined as the Borrower) under the Loan Agreement, subject to the terms and conditions of the LC Agreement. The section goes on to say,

> Notwithstanding the preceding sentence or anything to the contrary contained herein, the liability of and recourse to the Investor hereunder will be limited to the Letter of Credit, the Lender will not have any right to sue or commence any action against the Investor to recover any amounts owing by the Investor pursuant to the provisions hereof except to the extent necessary to permit the Lender to realize upon the security constituted by the Letter of Credit ...

5 Section 2.04 permits SAAN, the Borrower, to substitute another Letter of Credit, cash collateral or letter of guarantee in certain circumstances. Section 2.05 deals with the renewal of the Letter of Credit. It states that the Letter of Credit will expire on March 31, 2008, and the Investor will have no obligation to renew it. However, the Borrower is obligated to have the Letter of Credit replaced or renewed annually for additional one-year periods. If the Letter of Credit has not been renewed within three months of maturity, the Lender has the right to draw against it within 30 days of maturity and to hold the proceeds as Cash Collateral.

6 Section 2.06 deals with enforcement of the Letter of Credit, permitting the Lender to retain the Letter of Credit or the Cash Collateral as security against any ultimate shortfall in recovery of the Borrower's indebtedness, if the Lender issues a notice of intention to enforce security pursuant to the *Bankruptcy and Insolvency Act* ("BIA").

7 Section 2.07 then deals with realization of the security. It requires the Lender to dispose of all of the Borrower's inventory before claiming any payment under the Letter of Credit or the Cash Collateral. If there is a shortfall on the loan after disposal of the inventory, the Lender can draw against the Letter of Credit or the Cash Collateral. Once the loan is paid in full, if there are funds remaining on the Letter of Credit or from the Cash Collateral, the Lender is to notify the Bank to cancel the Letter of Credit or return the remaining funds to the Investor.

8 Pursuant to section 2.10, the Investor states that it will not have, and hereby waives, any rights of subrogation until the Borrower's indebtedness under the Loan Agreement has been paid in full to the Lender. Finally, section 2.11 deals with the Cash Collateral, stating,

> To the extent that the Lender is, in accordance with section 2.05, to hold the Cash Collateral, the Investor hereby irrevocably assigns, pledges, hypothecates, transfers and sets over to the Lender, and grants to the Lender a security

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interest in, hypothec on, and right to set off (compensate) against the Cash Collateral. The hypothec created herein is for the amount of the Cash Collateral. The Cash Collateral shall be held by the Lender, without interest, in an account designated by the Lender for such purposes in its books and records and may be commingled with the Lender's own funds. ...

9 Section 3.04 provides that the agreement will enure to the benefit and be binding on the Investor, Borrower, Lender and their successors and assigns.

10 In consideration for the LC Agreement, SAAN entered into a Credit Support Agreement with 167, which provided 167 with the right of subrogation. SAAN also provided guarantees from the Chahine II Family Trust and Tony Chahine, principal of SAAN, in the event the Letter of Credit was drawn on by GMAC.

11 As required, 167 obtained the Letter of Credit (entitled a "Letter of Guarantee") from the Bank with GMAC named as beneficiary. According to that document, payment was to be made under the Letter of Credit if GMAC provided appropriate documentation. The documentation must state that the amount claimed is due to GMAC, as GMAC is entitled to draw under the Guarantee in accordance with the terms and conditions of the Letter of Credit Agreement dated June 4, 2007. In return for the Letter of Credit, GMAC increased SAAN's credit facility to $25 million.

12 On October 25, 2007, GMAC gave SAAN notice of default under its credit facility and notice of its intention to enforce its security pursuant to s. 244(1) of the BIA. SAAN advised that it was seeking to restructure its affairs and intending to dispose of its assets *en bloc*.

13 On December 17, 2007, GMAC entered into a Forbearance Agreement to the Loan Agreement with SAAN. The Forbearance Agreement provided for an increase in the maximum advance under the Loan Agreement from $25 million to $30 million, to be available from December 17, 2007 until December 31, 2007, when the maximum reverted to $25 million. GMAC also agreed to forbear until the earlier of March 31, 2008 or the occurrence of additional acts of default.

14 In conjunction with the Forbearance Agreement, the respondent Black Saxon and GMAC entered into Loan Put Agreements dated December 17, 2007 and January 2, 2008. By these agreements, Black Saxon granted GMAC put options requiring Black Saxon to purchase and acquire, by way of assignment, GMAC's interest in the credit facility provided to SAAN. The combined put option price was $12.8 million.

15 On December 28, 2007, SAAN obtained protection under the *Companies Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("CCAA"). In the Initial Order made by Morawetz J. in the CCAA proceedings, the Forbearance Agreement was specifically referred to and approved

16 In addition to providing the Letter of Credit, 167 was a trade creditor of SAAN. It retained counsel in February 2008 and participated in the CCAA proceedings. The evidence shows that 167 became aware of the Forbearance Agreement in February or March 2008.

17 On March 31, 2008, the Letter of Credit expired. Rather than renew it, 167 directed GMAC to call upon the Letter of Credit and convert it into the Cash Collateral.

18 On April 25, 2008, 167 brought a motion to be declared an unaffected creditor under the CCAA proceedings.

19 On June 6, 2008, GMAC sought and obtained the appointment of PriceWaterhouseCoopers LLP ("PWC") as the interim receiver and receiver of SAAN. The Receiver's task was to ensure the orderly completion of SAAN's liquidation. 167 did not oppose the Receivership.

20 Up to this point, 167 had raised no issue with respect to GMAC's entitlement to the Cash Collateral. Lee Karls, president of 167, gave evidence that he had become aware of the CCAA proceedings in December 2007 or January 2008. On cross-examination, he said the following (Transcript, pp. 103-104):

474.

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Q. Okay. And were you waiting to see if that was going to happen?

A. I was waiting for everything to happen. I didn't know what was going to happen. I really didn't know what was going to happen. So it's not like I waiting until that happened to - the picture was painted that everything was going to be beautiful. And that's kind of where, the end of March when it wasn't such a rosy picture and I didn't believe everything I heard anymore, that might be the time when the rift started. So -

475.

Q. What was going to be beautiful?

A. Stalking horse. Everything getting moved over to the new company. Everything's status quo.

476.

Q. Your LC would be okay and wouldn't get called on?

A. Correct.

21 At another point in his cross-examination, Mr. Karls stated (Transcript at pp. 112-13, Q. 506):

> ... I thought there was a deal that the stores were being bought. So I didn't really care. If the stores had been bought, my money's secure ... Each one of those things that I was told, I knew I was getting my money back, and besides my LC money back I was getting, I was getting merchandise money back.

22 On July 4, 2008, 167 first took the position that its obligations under the Letter of Credit Agreement may have been terminated. It took the position that the Cash Collateral was not assignable, and that GMAC's loan had been or would be satisfied in full.

23 Subsequently, on July 18, 2008, 167 took the position that the Forbearance Agreement invalidated the LC Agreement.

24 On October 3, 2008, GMAC advised 167 that it would be assigning on an "as is where is" basis to Black Saxon all of its rights and obligations under the Loan Agreement with SAAN and the security documents relating thereto, including the LC Agreement. This prompted 167 to launch an application to determine whether its obligations under the LC Agreement were terminated because of amendments to the Loan Agreement by the Forbearance Agreement in December 2007. As noted by the motions judge, 167 is concerned that if it succeeds on its application, it may be required to seek payment from Black Saxon, which it believes to be of "questionable solvency" (Reasons, at para. 27).

25 On October 14, 2008, Morawetz J. ordered, on consent, that the Cash Collateral be paid into escrow by GMAC to Stikeman Elliot LLP as the escrow agent.

The Rule 45.02 Motion

26 167 then brought a motion under rule 45.02 to preserve the Cash Collateral by an order paying it into court. Rule 45 deals with orders for interim preservation of property. Rule 45.02 provides:

> Where the right of a party to a specific fund is in question, the court may order the fund to be paid into court or otherwise secured on such terms as are just.

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27 The motions judge dismissed the motion for reasons found at 2009 CanLII 24224 [*167986 Canada Inc. v. GMAC Commercial Finance Corp.-Canada/Societe Financiere Commerciale GMAC-Canada*, 2009 CarswellOnt 2690 (Ont. S.C.J. [Commercial List])]. He concluded that 167 has no proprietary interest in the Cash Collateral, as the funds paid under a letter of credit are the funds of the issuing party, here the Bank. He also noted that the LC Agreement provides that the title to the Cash Collateral was assigned to GMAC upon conversion of the Letter of Credit. Moreover, the LC Agreement did not provide for the Cash Collateral to be held as an indivisible and traceable fund. Therefore, he concluded that 167 has no proprietary interest in the Cash Collateral: "The Cash Collateral was derived from the LC Agreement and 167 has no proprietary interest in the Letter of Credit" (at para. 40). Therefore, "167 has, in my view, failed to establish a right to any specific fund" (at para. 42).

28 The motions judge also concluded that 167 had failed to establish a serious issue to be tried with respect to 167's claim to the Cash Collateral (at para. 55). 167 had argued that it was released from its obligations under the LC Agreement and entitled to the return of the Cash Collateral because GMAC entered into the Forbearance Agreement. This argument rests on the proposition that the LC Agreement is a guarantee, and 167, as guarantor, was released from its obligations because there was a material change to the indebtedness under the Loan Agreement that it guaranteed.

29 The motions judge held that the law of guarantee was not applicable to the LC Agreement. He described that agreement as a contract entered into by 167 to supply a standby letter of credit, with 167's only rights being to have that letter of credit drawn upon in accordance with the terms of the agreement (at para. 45). Changes to the Loan Agreement, including GMAC's decision to enter into the Forbearance Agreement, are irrelevant to the LC Agreement and do not discharge 167's obligations (at para. 48).

30 In the alternative, if 167 were a guarantor under the LC Agreement, the motions judge concluded that 167 was not entitled to a release under the law of guarantee, as 167 had implicitly ratified any forbearance by its conduct through the CCAA proceedings (at para. 49).

31 The motions judge also held that the assignment to Black Saxon was valid, a conclusion that was not appealed.

32 Given his conclusions, the motions judge did not find it necessary to deal with the issue of the balance of convenience. He dismissed the motion and stated that the Cash Collateral should be transferred by GMAC to Black Saxon pursuant to the Loan Put Agreements.

The Test on a Rule 45.02 Motion

33 The test for relief under rule 45.02 requires the moving party to show:

1. that the party claims a right to a specific fund,

2. that there is a serious issue to be tried regarding the party's claim to that fund, and

3. the balance of convenience favours granting the relief sought. (

News Canada Marketing Inc. v. TD Evergreen, [2000] O.J. No. 3705 (Ont. S.C.J.) at para. 14)

The Issues on Appeal

34 There are four issues on this appeal:

1. Did the motions judge err by resolving conflicts in the evidence and determining difficult questions of law on a rule 45.02 motion?

2. Did the motions judge err in finding that the Cash Collateral was not a specific fund within the meaning of rule

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45.02?

3. Did the motions judge err in applying the law governing letters of credit to the LC Agreement, rather than applying the law governing guarantees?

4. Did the motions judge err in finding an implied ratification by 167?

Analysis

Issue No. 1: Did the motions judge err by resolving conflicts in the evidence and determining difficult questions of law on a rule 45.02 motion?

35 This Court should intervene only if the motions judge made an error in law or a palpable and overriding error in his appreciation of the evidence.

36 The order under appeal was made by an experienced judge of the Commercial List in his role as the supervising judge of the CCAA proceedings involving SAAN. As the Court of Appeal has indicated, the expertise of such judges in insolvency proceedings is deserving of deference (*BNY Capital Corp. v. Katotakis*, [2005] O.J. No. 623 (Ont. C.A. [In Chambers]) at para. 8; *Algoma Steel Inc., Re*, [2001] O.J. No. 1943 (Ont. C.A.) at para. 8).

37 167 submits that the motions judge went too far in his scrutiny of the merits of the case. While he was required to determine whether 167 had established there was a serious issue to be tried with respect to 167's claim to the Cash Collateral, he in fact determined the merits of the application. This is contrary to the instruction in *Metropolitan Stores (MTS) Ltd. v. Manitoba Food & Commercial Workers, Local 832*, [1987] 1 S.C.R. 110 (S.C.C.) at para. 40 that a court at the interlocutory stage should not try to resolve conflicts of evidence or decide difficult questions of law.

38 In my view, the motions judge did not determine the merits of 167's application. He was required to decide if there was a serious issue to be tried with respect to 167's claim to the Cash Collateral, and he determined that 167 did not meet even this low threshold. He came to this conclusion based on the application of well-known legal principles to the uncontested facts and in light of the terms of the LC Agreement.

Issue No. 2: Did the motions judge err in finding that the Cash Collateral was not a specific fund within the meaning of rule 45.02?

39 In his reasons, the motions judge stated the first part of the test under rule 45.02 required the moving party to establish "a right to a specific fund", rather than a *claim* of a right to a specific fund (at paras. 30, 42). However, it is clear from his reasons that his first question was whether there was a claim to a specific fund.

40 To determine that question, a motions judge has to make a preliminary assessment as to whether the moving party has a proprietary claim. Here, he concluded that there was no specific fund, and that 167 had no basis to make a proprietary claim against the Cash Collateral. Therefore, he held that 167 did not satisfy the first part of the test. I agree with his conclusion.

41 A "specific fund" is a reasonably identifiable fund, earmarked to the litigation in issue (*Rotin v. Lechcier-Kimel* (1985), 3 C.P.C. (2d) 15 (Ont. H.C.) at para. 5). The party seeking a rule 45.02 order must have a proprietary claim against the specific fund (*DIRECTV Inc. v. Gillott* (2007), 84 O.R. (3d) 595 (Ont. S.C.J.) at paras. 59 and 62). Establishing a possible claim for payment of damages for breach of contract does not establish a right to a specific fund (*Assante Financial Management Ltd. v. Dixon*, [2004] O.J. No. 2237 (Ont. S.C.J.) at para. 28).

42 The motions judge correctly held that the Cash Collateral was not a specific fund against which 167 could make a proprietary claim. The law governing letters of credit is clear: the funds paid on a letter of credit are the property of the issuing bank (*Angelica-Whitewear Ltd. v. Bank of Nova Scotia*, [1987] 1 S.C.R. 59 (S.C.C.) at para. 10). As Blair J. (as he

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then was) said in *885676 Ontario Ltd. (Trustee of) v. Frasmet Holdings Ltd.*, [1993] O.J. No. 113 (Ont. Gen. Div. [Commercial List])) ("*Frasmet*") at para. 29:

> Letters of credit are a specialized form of commercial credit, designed by their very nature to be free and clear of the equities between the parties to the underlying transaction which they are issued to secure. They constitute an independent contract between the issuer (usually a bank, as in this case) and the beneficiary (one of the parties to the underlying transaction - a landlord in this case). This principle of "autonomy" goes to the root of the practice surrounding their issuance. The only admitted exception to the principle is fraud.

43 In the present case, the Bank paid the Cash Collateral to GMAC pursuant to the Letter of Credit, an autonomous agreement to which the Bank and GMAC were the only parties. 167 had no proprietary claim to the Letter of Credit or its proceeds at the time they were drawn upon by GMAC.

44 167 relies on the terms of the LC Agreement to show that it has a claim to the Cash Collateral. In particular, it relies on the fact that GMAC is not entitled to draw down on the Cash Collateral unless there is a shortfall on the SAAN loan after the SAAN inventory has been liquidated. If the liquidation is sufficient to satisfy the loan, 167 is entitled to the return of the Cash Collateral. Alternatively, 167 is entitled to any amount of the Cash Collateral that is surplus after the funds from the liquidation are used to pay down the loan.

45 In my view, these provisions do not create a proprietary claim to a specific fund. According to the LC Agreement, GMAC has a contractual obligation to account for the Cash Collateral funds it received from the Bank after the liquidation and to pay the balance owing after the liquidation, if any. Until the liquidation occurs, 167 has no right to claim any part of the Cash Collateral funds.

46 As the motions judge noted, section 2.11 of the LC Agreement expressly provides that 167 "hereby irrevocably assigns, pledges, hypothecates, transfers and sets over to the Lender" the Cash Collateral. This wording indicates that 167 had no proprietary interest in the Cash Collateral.

47 Moreover, the wording of the LC Agreement permitting GMAC to commingle the Cash Collateral with its own funds indicates that there is no specific fund to which 167 could assert a proprietary claim.

48 This is not a case where there is a claim for trust funds, as in some of the cases relied on by 167 (see, for example, *Rotin, supra* at para. 13; *1463150 Ontario Ltd. v. 11 Christie Street Inc.*, 2007 CarswellOnt 6937 (Ont. Master)).

49 In any event, 167 is not claiming the return of the Cash Collateral under the LC Agreement. In its Notice of Application, it seeks payment of the amount of the Cash Collateral plus interest on the basis that its obligations under the LC Agreement are discharged under the law of guarantee. This is a claim in damages, as 167 has no proprietary interest in the Letter of Credit or the funds drawn on it. What 167 is seeking is execution before judgement; it cannot do so through a rule 45.02 motion.

Issue No. 3: Did the motions judge err in applying the law governing letters of credit to the LC Agreement, rather than applying the law governing guarantees?

50 167's application is based on the assertion that the LC Agreement was a contract of guarantee. It then asserts that the acts of forbearance by GMAC were material amendments to the guarantee, and, therefore, 167 was discharged from its obligations under the guarantee. It relies on the decision of the Supreme Court of Canada in *Manulife Bank of Canada v. Conlin*, [1996] 3 S.C.R. 415 (S.C.C.) at para. 2, where the Court referred to the well-established principle of law that a guarantor will be released from liability on the guarantee where the lender and the principal borrower agree to a material alteration of the terms of their loan agreement without the consent of the guarantor.

51 167 argues that the motions judge's error in refusing to apply the law of guarantee is rooted in his failure to distinguish the substance of a guarantee from the substance of a standby letter of credit. He is said to have erred by defining the parties' relationship based on the form of security given for the LC Agreement, rather than the substance of the agreement.

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52 167 relies on *Wichita Eagle & Beacon Publishing Co. v. Pacific National Bank of San Francisco*, 493 F.2d 1285 (U.S. Cal. C.A. 1974), where the Court held that it was not bound by the label on an instrument describing it as a letter of credit. The Court in that case went on to look at the terms of the agreement, concluding that the instrument was really a contract of guarantee, because the issuer was not required to deal only with documents in order to determine whether payment would be made. Rather, the issuer would be required to determine facts relating to the performance of a separate contract, a lease, in order to determine whether to make payment. Therefore, the instrument was held to be, in substance, a guarantee.

53 In the present case, the motions judge carefully considered the terms of the LC Agreement to determine whether the law of guarantee applied to it. He recognized that the classification of the agreement should be determined by its substance and not just by the title given to a particular document.

54 It is significant that 167 contracted with GMAC in the LC Agreement to cause the Bank to issue an irrevocable standby letter of credit as security for the obligations of SAAN as borrower. As Blair J. observed in *Frasmet Holdings, supra*,

> There is a fundamental difference between a letter of credit, which is a very specialized form of security, and a guarantee, which is not a form of security at all (except in a loose, non-legal sense of that term). (at para. 26)
>
> . . . . .
>
> Thus, it can be seen that a letter of credit is a creature quite different from a simple guarantee. It is a form of security which may be called upon by the secured creditor when the event for which the security has been given occurs, without regard to the circumstances existing between the parties to the underlying transaction. (at para. 34)

55 While 167 argues that the motions judge improperly let form triumph over substance, I disagree. Because of the qualities of a letter of credit, its use as a form of security is a fundamental part of the substance of the LC Agreement. As Farley J. stated in *Westpac Banking Corp. v. Duke Group Ltd.*, [1994] O.J. No. 2203 (Ont. Bktcy.)), "a standby letter of credit is critically different from a guarantee or indemnity" (at para. 17). Farley J. quoted with approval from *Carley Capital Group, Re*, 119 B.R. 646 (U.S. W.D. Wis. 1990), which held that a letter of credit creates a primary liability - to pay on the presentation of documents - rather than a secondary liability, to pay in the event that the borrower defaults.

56 In *Westpac*, Farley J. stated (at para. 28):

> One must remember that the parties chose the letter of credit method as the way of satisfying the requirements; thus they chose how the substance of this transaction would be dealt with. The autonomy principle is not form, it is a foundation of the letters of credit regime. It is this regime which on a policy basis is recognized as being quite valuable to society (and the economy) as a whole.

57 167 argues that *Carley* can be distinguished because, in that case, there was no privity of contract between the lender and the party who arranged the letter of credit. Here, there is privity between GMAC and 167 because of the LC Agreement.

58 It is common to find side agreements between a party who provides a standby letter of credit and a lender in order to deal with issues such as enforceability and conditions of payment (see Lazar Sarna, *Letters of Credit: The Law and Current Practice*, 3rd ed. (Thomson Carswell) at pp. 3-8 to 3-8.1). However, the existence of privity between GMAC and 167 does not turn the LC Agreement into a contract subject to the law governing guarantees. To determine whether the law of guarantee applies, one must consider the terms of the LC Agreement, including the fact that the security provided in it is a letter of credit.

59 Moreover, an examination of the terms of the LC Agreement confirms that it is not a contract of guarantee. The only recourse available to GMAC under the agreement is to the Letter of Credit (or the Cash Collateral derived from it).

60 As well, there is no provision for waiver of forbearance in the LC Agreement, as one would expect in a commercial guarantee instrument (see Geraldine Andrews and Richard Millet, *Law of Guarantees*, 4th ed. (London: Sweet & Maxwell,

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2005) at p. 528).

61 In addition, 167 entered into a separate Credit Support Agreement with SAAN in order to create a right of subrogation. As a guarantor, 167 would have no need to obtain such a right, as the right of subrogation arises by law for a guarantor (*Westpac*, *supra*, at para. 17).

62 If 167 wanted the right to have its obligations discharged in the event of a material change to the Loan Agreement, it could have sought such rights by contract as well. Instead, the LC Agreement appears to contemplate the possibility of further amendments to the Loan Agreement, defining it "as the same may be further amended, modified, replaced, restated or supplemented from time to time."

63 167 argues that its obligations under the LC Agreement were secondary obligations and, therefore, it is a guarantor. In fact, 167's obligations under the agreement are primary obligations to GMAC - to provide the Letter of Credit on which GMAC could draw if the proper documents are presented to the Bank. 167 was required to provide the Letter of Credit before and irrespective of any default by SAAN, the principal borrower. The proceeds ultimately drawn on the Letter of Credit by GMAC were the Bank's funds; it was the Bank, not 167, that paid the debt of SAAN.

64 In contrast, a guarantee creates a secondary obligation, requiring payment by the guarantor on the default of the borrower (*Carley Capital Group, Re*, *supra* at p. 2). That is not the situation under the LC Agreement.

65 167 argues that the LC Agreement creates a secondary obligation on the part of 167 because payment from the Letter of Credit or the Cash Collateral can be made only if the loan is not satisfied by SAAN or by the liquidation of the SAAN inventory. Again, it is not correct to say the obligation is secondary. 167's obligation under the LC Agreement is primary; the agreement does not require 167 to do anything after it has provided the Letter of Credit. 167 may, in certain circumstances, have a right to monies from GMAC, but only if there is a surplus from the funds advanced by the Bank after the liquidation of the inventory and payment of the loan. As Blair J. said in *Frasmet*, *supra*, at para. 33:

> An irrevocable letter of credit has been said to be the equivalent of cash or moneys worth placed at risk to its full face value the moment it is issued, subject to the happening of certain specific events ...

66 167 also argues that the Letter of Credit is security for 167's guarantee under the LC Agreement, and not security for SAAN's indebtedness. However, the terms of the LC Agreement and the Letter of Credit make it clear that the Letter of Credit was security for SAAN's indebtedness under the Loan Agreement and not security for a guarantee provided by 167. Section 2.06 states clearly that in the event of insolvency proceedings against SAAN, "GMAC may retain the Letter of Credit, or the Cash Collateral, as the case may be as security against any ultimate shortfall of the Borrower's indebtedness."

67 Therefore, reading the LC Agreement as a whole and in light of the obligation assumed by 167, there is no serious issue that the law of guarantee applies to the agreement so as to permit 167 to argue that its obligations as a guarantor were discharged as a result of the Forbearance Agreement.

Issue No. 4: Did the motions judge err in finding an implied ratification by 167?

68 In the alternative, if the LC Agreement is subject to the law relating to guarantees, the motions judge held that 167 implicitly ratified the changes to the Loan Agreement.

69 167 argues that a guarantor has no legal obligation to warn a creditor when the creditor engages in conduct that may discharge the guarantee (see *Birch Lake (Municipal District) v. London Guarantee & Accident Co.*, [1930] 3 W.W.R. 634 (Alta. T.D.) at para. 11).

70 However, if a guarantor, upon learning of a material variation in the guaranteed loan, continues to allow a creditor to supply credit to the debtor, the guarantor is deemed to have ratified the variation after a reasonable period has elapsed (*Transamerica Commercial Finance Corp. Canada v. Northgate RV Sales Ltd.*, 2006 CarswellBC 3180 (B.C. S.C. [In Chambers]) at paras. 37 and 39).

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71 167 concedes the possibility that ratification may exist in the context of guarantees, but submits that the motions judge erred in determining that there had been ratification. There was no express ratification of the changes to the Loan Agreement, and 167 argues that any implied ratification must be clear and unequivocal (*John Ziner Lumber Ltd. v. Kotov* (2000), 5 C.L.R. (3d) 44 (Ont. C.A.) at para. 31). 167 submits that its participation in the CCAA proceedings, as a trade creditor, could not constitute clear and unequivocal ratification of amendments to the Loan Agreement.

72 I see no error on the part of tbe motions judge with respect to ratification. The evidence is clear that 167 was aware of the Forbearance Agreement at the latest in February or March 2008. It participated in the CCAA proceedings over the course of several months, including the Receivership motion, without raising any issue about the Letter of Credit or the termination of its obligations under the LC Agreement. While 167 states that it participated in the CCAA proceedings as a trade creditor rather than guarantor, it is clear that 167 knew of the Forbearance Agreement through its participation, and it raised no objection.

73 As well, it directed GMAC to draw down the Cash Collateral, rather than renew the Letter of Credit at the end of March 2008, again without raising any issue about the termination of the LC Agreement. The evidence of Mr. Karls shows that 167 raised no concerns because he hoped that a restructuring of SAAN would result in the recovery of the monies advanced under the Letter of Credit and payment of amounts owing to 167.

74 While the motions judge did not determine whether there were material cbanges that would affect the validity of the Loan Agreement, the evidence suggests that the Forbearance Agreement would not discharge the Loan Agreement. SAAN defaulted under the Credit Facility in October 2007, leading GMAC to issue a notice of its intention to enforce its security. By section 2.06 of the LC Agreement, GMAC was then entitled to retain the Letter of Credit or Cash Collateral as security against any ultimate sbortfall in recovery of SAAN's indebtedness. Thus, GMAC's rights against the guarantee crystallized before the Forbearance Agreement. As noted in *Alberta Opportunity Co. v. Wilson*, [1994] A.J. No. 498 (Alta. Master), once a guarantor becomes liable on the guarantee, later accommodations to the borrower would not change the terms of the guarantee (at para. 41).

Conclusion

75 For 167 to succeed in this appeal, it was required to show that the motions judge erred on each of three issues: the specific fund, the applicability of the law relating to the law of guarantee, and ratification. In my view, the motions judge did not err in concluding that there was not a specific fund to which 167 had a proprietary claim. Nor was there a serious issue with respect to 167's claim that the LC Agreement was terminated, thus entitling 167 to the Cash Collateral. Given this conclusion, there is no need to address the balance of convenience.

76 The appeal is dismissed. If the parties cannot agree on the costs of the motion for leave to appeal and the appeal, they may make brief written submissions through the Divisional Court Office within 21 days of the release of this decision.

Appeal dismissed

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TAB 16

2003 CarswellOnt 892
Ontario Superior Court of Justice

Mutual Tech Canada Inc. v. Law

2003 CarswellOnt 892, [2003] O.J. No. 1015, 121 A.C.W.S. (3d) 252

Mutual Tech Canada Inc. v. Pui Ching Law et. al.

Master MacLeod

Judgment: March 5, 2003
Docket: 98-CV-143329CM

Proceedings: additional reasons at *Mutual Tech Canada Inc. v. Law* (May 5, 2003), Doc. 98-CV-143329CM (Ont. Master)

Counsel: *Ralph Cuervo-Lorens*, for Plaintiff/Moving Party
Harvey S. Dorsey, for Defendants/Responding Parties

Subject: Employment; Public

Related Abridgment Classifications

Civil practice and procedure
XXIV Costs
XXIV.10 Costs of particular proceedings
XXIV.10.e Interlocutory proceedings
XXIV.10.e.ii Motions and applications

Labour and employment law
II Employment law
II.5 Wages and benefits
II.5.c Bonus contracts
II.5.c.i Bonus based on profits
II.5.c.i.B Miscellaneous

Headnote

Employment Law --- Wages and benefits — Bonus contracts — Bonus based on profits — General

Table of Authorities

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Chitel v. Rothbart (1982), 39 O.R. (2d) 513, 30 C.P.C. 205, 69 C.P.R. (2d) 62, 141 D.L.R. (3d) 268, 1982 CarswellOnt 508 (Ont. C.A.) — referred to

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Micallef v. Gainers Inc. (1988), 25 C.P.C. (2d) 248, (sub nom. *Maybank Foods Inc. Pension Plan v. Gainers Inc.*) 63 O.R. (2d) 687, 1988 CarswellOnt 347 (Ont. H.C.) — referred to

News Canada Marketing Inc. v. TD Evergreen (2000), 2000 CarswellOnt 3544 (Ont. S.C.J.) — considered

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Taribo Holdings Ltd. v. Storage Access Technologies Inc. (2002), 2002 CarswellOnt 3811, 27 C.P.C. (5th) 194 (Ont. S.C.J.) — referred to

Tom Jones Corp. v. Mishemukwa Developments Ltd. (1996), 46 C.P.C. (3d) 77, 1996 CarswellOnt 641 (Ont. Gen. Div.) — referred to

***Master Macleod*:**

1 The plaintiff seeks an order that a specific fund be paid into court pursuant to Rule 45.02. The motion (combined with other relief) was originally launched by the plaintiff in June of 1998 and it came before Juriansz J. in September of that year. At that time, paragraphs 1 a) and b) of the original notice of motion were adjourned "on consent *sine die* to be brought on seven days' notice". In the intervening period, the parties have engaged in a series of examinations and interlocutory motions. There have also been some efforts to settle both the motion and the action. The motion was eventually argued before me on November 27th, 2002 and January 21, 2003. I should note that the action was ordered into case management on May 15th, 2000.

2 The plaintiff is a wholesaler of integrated circuits and related computer parts and services and until the beginning of February 1998 the defendant Law was the general manager. It is undisputed that Ms. Law worked for Mutual Tech since approximately July of 1993 and was fully responsible for its operations and business. The plaintiff apparently reported to Francis C.W. Wong and he, in turn, asserts that his responsibility was to monitor the operations of Mutual Tech for his mother who is the owner. For the purpose of this motion, the ownership is not critical. There is no doubt that Ms. Law had responsibility for the day to day operations of the company.

3 There is also no real dispute that Ms. Law was compensated by way of salary and bonus. The bonus appears to have been a percentage of the profits of the corporation. Apparently there was an agreement that certain of the expenses of Mutual Tech which were expenses for the benefit of Francis Wong or the owner were not to be considered in the calculation of profit. The manner in which this usually worked was that Ms. Law would calculate her bonus and send the calculations to Mr. Wong. Ms. Law's evidence is that she would then call Mr. Wong and he would verbally acknowledge her calculation. She would then pay herself the bonus in a fashion that would least interfere with cash flow and the bonus would be divided between herself and her husband, K. Leung, also an employee of Mutual Tech and one of the defendants in this action.

4 While Mr. Wong asserts there was a discretionary element to the bonus, it appears that Ms. Law's calculation of bonus was never vetoed. At the time Ms. Law left the employment of Mutual Tech, she had not been paid a bonus for the fiscal year ending March 31, 1997 and of course the fiscal year ending March 31, 1998 was still in progress. For the purpose of this motion, it is not disputed that Ms. Law would have been entitled to a bonus for the previous fiscal year. There remains a dispute about whether or not she was entitled to a bonus for the partial fiscal year in which she left her employment, whether or not the corporation made any profit that year and whether any bonus would be offset by damages.

5 Ms. Law contends that in late 1997, Mr. Wong attempted to diminish her responsibilities in Mutual Tech. She also contends Mr. Wong was setting up companies to compete with Mutual Tech and by so doing breached her contract of employment and an oral agreement between herself and Mr. Wong. She alleges constructive dismissal. The plaintiff on the other hand, alleges that Ms. Law wrongfully left her employment without notice and set up a competing business in breach of her fiduciary duty. There are other allegations such as use of confidential information and destruction of documents including non competition agreements.

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6 Whether or not Ms. Law was justified in taking the steps she did is of course the central issue in this litigation. What is not in dispute is that she, Mr. Leung and all or substantially all of the other employees resigned and set up shop in a similar business, the defendant 1275809 Ontario Inc carrying on business as MMAX Group Association. There is also no dispute, that prior to leaving, Ms. Law paid herself the sum of $700,000.00 on account of bonus for 1997 and 1998. This sum was divided between Ms. Law and Mr. Leung and approximately 50% of the amount was remitted to Revenue Canada as a source deduction.

7 It is this $700,000.00 which is the focus of the motion and the "fund" the plaintiff sought to have paid into court. As I understand it, it is now conceded for the purpose of the motion that a 1997 bonus of $331,002.00 would have been owing. This results in a fund of $368,998.00, being the remainder of the $700,000.00. It has also been conceded since the first time the parties attended before me that the funds paid to Revenue Canada are not part of the fund to be paid into court. The fund, in other words would be the $368,998.00 less the amount remitted to Revenue Canada or roughly 180,000.00. The parties are able to work out the exact mathematics. The question before me is whether or not the order should be made.

8 Cases cited by counsel suggest a three part test for granting an order under Rule 45.02 which include a claim by the plaintiff to a specific fund; a strong prima facie case; and the balance of convenience.[1] More recent decisions cast doubt on the need for a "strong" prima facie case but rather suggest there must be a "serious issue to be tried".[2] I prefer this latter view as expressed by Nordheimer J. in *News Canada Marketing Inc. v. TD Evergreen* . In that decision he ruled that "strong" prima facie case puts the test too high. It should only be necessary to demonstrate that there is a serious issue to be tried.

9 In essence, these are injunctive tests. The serious issue test set out in *American Cyanamid*[3] is the appropriate test to be applied for most types of injunctive relief in Ontario. Mareva injunctions and injunctions to enforce restrictive covenants are exceptions which require the higher test of a *prima facie* or strong *prima facie* case.[4]

10 An order under Rule 45.02 is not a Mareva injunction. Were it so, quite apart from the question of whether it would be appropriate for a master to make the order, it would not be appropriate without an undertaking in damages and without the higher standard. That is because a Mareva injunction seeks to restrain a defendant from dealing with his or her own assets by restraining removal from the jurisdiction. The Rules Committee should not be assumed to have intended by means of Rule 45.02 to allow the court to grant injunctive relief without the usual safeguards. Injunctions are an exercise of the inherent power of a Superior Court judge and are governed by s. 101 of the *Courts of Justice Act*. Rule 45 by contrast should be seen as an expression of the authority conferred by s. 104 of the Act and interpreted accordingly.

11 There is a serious issue to be tried concerning the entitlement to bonus for the fiscal year 1998. For the purposes of the motion, the plaintiff has abandoned the argument there is a serious issue about the 1997 bonus. I am also of the view that the 1998 estimated bonus at some point in time constituted a fund to which the plaintiff claims entitlement. The funds removed from the plaintiff constituted an asset which is the very subject matter of this aspect of the litigation. While it was not an identifiable designated trust fund as was the case in *Micallef v. Gainers Inc.*[5], it was a clearly identifiable sum of money removed from the plaintiff's bank account and it could be readily traced.

12 The evidence before me is clear that the disputed money no longer exists as a segregated fund. In fact the funds were used to capitalize the defendant corporation. The plaintiff argues that the defendant should not be permitted to avoid the reach of Rule 45.02 by the simple act of utilizing the disputed funds. I do not think that will always be correct. Intermingling of funds may well mean there can not be recourse to Rule 45.02. To hold otherwise, would render the words "a specific fund" meaningless and would more resemble execution in advance of judgment than preservation of a fund. On the other hand, I agree that taking steps to intermingle funds in the face of a pending motion should not be rewarded. A party who alters the status quo in the face of a pending motion will be unable to rely on that fact. It may well be a matter of timing. It may also be the case that recourse to injunctive relief is necessary if the preconditions for an order under Rule 45.02 no longer exists. In either case, failure to move promptly may be fatal.

13 In the case at bar, there is no evidence that the defendants sought to thwart the motion by disposing of the funds in the face of the motion so I think that argument is something of a "red herring". While the timing of the motion and the actions taken by each party may impact the date on which the court should assess the facts, timing (or delay) is more often a factor to be weighed when assessing the balance of convenience.

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14 In the case at bar, the funds were apparently removed on January 27th, 1998. Demand letters were written on February 6th and 13th, 1998. The action was commenced on March 10th, 1998 and the original notice of motion was served on June 5th, 1998. Plaintiff's counsel argues that in the circumstances of this case, the plaintiff could not have moved more promptly. I note that the motion, originally returnable in August, was not heard until September and at that time, the portion I am concerned with was adjourned on consent.[6] The plaintiff contends that discussions ensued and it was only in January of 1999 that they broke down and the defendant made it clear the funds would not be paid into court voluntarily.

15 This however is neither 1998 nor 1999 but 2003. I need only determine if the timing of events in 1998 and 1999 was reasonable if the intervening time does not matter. It would take an extraordinary set of circumstances to persuade the court that a preservation order makes any sense some 5 years after the funds were removed from the plaintiff and used in establishing the defendant corporation. Both companies appear to be carrying on business. I have not been presented with evidence there is any danger a judgment for the $180,000 (which is now said to be the disputed fund) will be less likely to be enforceable if the requested relief is refused.

16 The only extraordinary set of events has been the conduct of the litigation itself. Huge amounts of time and money have been expended and I am advised that despite mountains of transcripts, the parties can not agree to use them for discovery purposes. The action in other words is barely underway. Mountains of paper have been filed. Witnesses have been examined at length. Days of court time have been spent obtaining rulings and directions.[7]

17 In support of this motion, the plaintiff relied upon an affidavit of Francis C.W. Wong. That affidavit was sworn in July of 1998. It was met with responding affidavits served in August. Following the adjournment of the motion and the amendment of the pleadings, the plaintiff then responded with a reply affidavit of Mr. Wong in March of 1999. I am advised this was met with more affidavits by the defendants, notices of cross examination and summonses to witnesses. There then ensued a motion to strike the defendants affidavits and summonses to witnesses and an appeal of the master's order. This occupied the balance of 1999 and the appeal was heard in January 2000. Francis Wong served another reply affidavit responding to the defendants' further affidavits in March of 2000.

18 Examinations and cross examinations were conducted during 2000 and refusals and undertakings motions were heard over several days in 2001 and 2002. I am advised that there was mediation in a related proceeding in the United States sometime in early 2001 and in February of 2002 the parties and their counsel participated in a lengthy settlement conference with me. Cross examinations resumed in 2002. In October of 2002, the defendant served two further affidavits. There was a further flurry of affidavits just before the hearing of this motion on November 27th, 2002.[8]

19 The plaintiff argues that it is inequitable to allow the defendants to resort to self help, have the use of the disputed funds and to inflict this huge amount of evidence on the plaintiff and the court and then to refuse to order the funds paid into court because of the passage of time. There are at least three problems with that argument. In the first place, the original motion was adjourned on consent to be brought back on seven days notice. For most of the intervening time, the plaintiff could have insisted on having the motion heard.

20 In the second place, the propriety of the affidavit material, cross examinations and examinations in aid of the motion have already been argued and the plaintiff did not prevail. Thirdly, the plaintiff resisted questions which were the subject of the refusals motions and the propriety of those refusals have also been determined. There is no basis for me to conclude today that the delay in hearing this motion should be found to be solely or even substantially the result of unacceptable tactics on the part of the defendants.

21 The balance of convenience test is not a theoretical construct but a test to be measured against real events in the real world. What purpose would be served in ordering these funds paid into court? Far from preserving the status quo, it would at this stage simply give the plaintiff an advantage in the litigation. I am unable to conclude the balance of convenience favours payment into court. Accordingly the motion must be dismissed.

22 This can not be construed as the court condoning the defendant's actions. The plaintiff may win the day at trial. If the defendant is found to have left abruptly, hired away the employees and started a competing business while helping herself to a bonus that was not yet due or payable, she may well be visited with substantial damages and the other relief sought in the statement of claim. The relief claimed contains all the tools necessary for the court to visit a full measure of condemnation

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and opprobrium on these events if they were unjustified.

23 It is not my role on the motion to pre-judge the merits of the action. Application of either the substantial issue or strong *prima facie* case tests do not involve prejudging the outcome. These are hurdles to be overcome by a plaintiff seeking extraordinary interim relief and are not to be equated with summary judgment. I must assume the plaintiff may be successful but I am equally required to assume the defendant may prove her allegations. The rules of civil procedure are designed to ensure the just determination of cases on their merits and in appropriate cases to preserve the status quo pending that outcome. To make an order today restoring the situation to that which existed in 1998 would accomplish neither of these ends.

24 In summary, the motion for payment into court is dismissed. The question of costs may be addressed in writing on a schedule to be agreed between counsel.

25 Upon receipt of these reasons, counsel are to attempt to agree on a timetable for discoveries and all other steps necessary to bring the action to a conclusion. Consideration should be given to appropriate dispute resolution options. A case conference will be convened at the request of either counsel or if an agreed upon timetable has not been filed with my office before the end of March, 2003.

Footnotes

1 See, *Sun v. Ho* (1998), 18 C.P.C. (4th) 363 (Ont. Gen. Div.) and *Tom Jones Corp. v. Mishemukwa Developments Ltd.* (1996), 46 C.P.C. (3d) 77 (Ont. Gen. Div.)

2 See *News Canada Marketing Inc. v. TD Evergreen*, [2000] O.J. No. 3705, 2000 CarswellOnt 3544 (Ont. S.C.J.) which was cited by counsel and *Taribo Holdings Ltd. v. Storage Access Technologies Inc.*, [2002] O.J. No. 3886 (Ont. S.C.J.) which was not.

3 *American Cyanamid Co. v. Ethicon Ltd.*, [1975] 1 All E.R. 504 (U.K. H.L.)

4 *Chitel v. Rothbart* (1982), 141 D.L.R. (3d) 268, 39 O.R. (2d) 513 (Ont. C.A.); *Jet Print Inc. v. Cohen* (1999), 43 C.P.C. (4th) 123 (Ont. S.C.J.)

5 (1988), 63 O.R. (2d) 687 (Ont. H.C.)

6 The relief granted by Juriansz J. involved striking certain — but not all — impugned paragraphs of the statement of defence and counterclaim.

7 Not all of the interlocutory activity has been solely related to this motion. Production issues, for example, have also been argued.

8 Mr. Dorsey served two affidavits of non parties in October after the cross examinations were under way. Mr. Cuervo-Lorens asked that the affidavits not be admitted but if they were he wished to file an affidavit in response and to adjourn the motion for further cross examinations. The affidavits were for the most part affidavits concerning the calculation of the bonus with supporting financial material. In the result, I admitted all of the affidavit material but I did not grant an adjournment. Nothing in this decision turns on the material in those affidavits as Mr. Cuervo-Lorens advised me in argument that he was only pursuing payment in of $180,000.00.

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DEL EQUIPMENT INC.
Applicant

Court File No. CV-19-629552-00CL

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BOOK OF AUTHORITIES OF THE RESPONDING PARTY, GIN-COR INDUSTRIES INC.
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