Court of Queen's Bench of Alberta

Citation: Access Mortgage Investment Corporation v Arres Capital Inc, 2021 ABQB 307

Date:
Docket: 1401 12431
Registry: Calgary

Between:

Access Mortgage Investment Corporation

Applicant

- and -

Arres Capital Inc.

Respondent

Reasons for Decision
of the
Honourable Madam Justice B.E. Romaine

I. Introduction

[1] The Receiver for Arres Capital Inc. applies for a distribution order of the remaining funds in this receivership. In a related application, investors in Kenzie Financial Investments Ltd., supported by Arres Capital's Inspector in bankruptcy, take the position that certain funds that had originally been paid into court pursuant to earlier litigation, and were later released to the Receiver, should not be construed as part of the Arres Capital estate. The Kenzie investors submit that they are entitled to the funds, subject only to deduction for the Receiver's expenses actually incurred in respect of dealing with any competing claims to them.

II. Facts

[2] Bankruptcy proceedings in this matter were commenced in 2011. After protracted litigation, which is not necessary to describe in detail for the purpose of this application, the Court granted a bankruptcy order with respect to the estate of Arres Capital Inc. on July 29, 2017. On the same date, Alvarez and Marsal Canada Inc., the trustee in bankruptcy, was appointed Receiver of Arres Capital pursuant to the *Civil Enforcement Act*, R.S.A. 2000, c. C-15. That order was amended and restated on October 23, 2017.

[3] The bankruptcy and receivership proceedings are in their final stages. This application involves priority to a fund of approximately $235,000.

[4] The Kenzie investors claim this fund, which was originally paid into court pursuant to a partial summary judgment that they obtained against Arres Capital in July, 2013.

[5] The amount of the judgment was $228,965.45, inclusive of costs. As Arres Capital appealed the judgment, the sum of $235,000 was paid into court in the summary judgment matter pursuant to a consent order dated February 11, 2014.

[6] The appeal was dismissed on April 16, 2014. Before the Kenzie investors were able to access the funds paid into court, Terrapin Mortgage Corporation made a successful application to be granted intervenor status in the litigation between Arres Capital and the Kenzie investors, and in litigation between Arres Capital and Graybriar Land Company Ltd. and Graybriar Greens Inc., a foreclosure action.

[7] The Kenzie investors applied to have the funds paid out of court to them. Terrapin opposed the application on the basis of a mortgage that it had obtained against four condominiums units that were part of the foreclosure proceedings involving the Graybriar companies. Registration of the mortgage had been stayed by order obtained by the Kenzie investors, who submitted that this was an attempt to mortgage trust property of Graybriar, and that the funds from the mortgage had been advanced before registration.

[8] Terrapin claimed an equitable mortgage over the Graybriar assets, or alternatively, an interest in the funds paid into court by Arres Capital on the basis that Terrapin was essentially the party that provided the funds.

[9] The Kenzie investors took the position at the time, and continue to take the position, that Arres Capital had no further claim over those funds going forward as the issue was between the Kenzie investors and Terrapin.

[10] In July, 2014, Strekaf, J (as she then was) directed that the Kenzie application to access the funds be adjourned sine die pending a determination of a stay order in the Graybriar actions. The Court of Appeal allowed the Graybriar stay order to remain in place.

[11] On July 26, 2017, while the Graybriar foreclosure matters were continuing to unfold, Arres Capital was placed into receivership. On June 4, 2018, I heard an application by the Receiver for an order directing that funds held in court from the Graybriar sales and funds held in court arising from the Kenzie investors' action be paid to the Receiver to enable the Receiver to conduct a claims process and be subject to the Receiver's Charge and the Receiver's Borrowing Charge. I identified the issue in that application as being whether the Receiver's Charge was able to be prioritized over property subject to the trust claims. I found that the Court may impose such a charge where it is satisfied that the Receiver's Charge would secure the

administration of a claims process that represents the only method "of breaking out of the current quagmire in respect to the Graybriar funds".

[12] I directed that the funds paid into court in the Kenzie litigation (the "Court Funds") were to be paid to the Receiver, together with the funds derived from the sale of six Graybriar condominium units.

[13] The June 4, 2018 Order arising from the application provides that the sales proceeds and the funds that had been paid into court are subject to the Receiver's Charge and the Receiver's Borrowing Charge as a first charge in priority to all other security interests, trusts, liens, charges and encumbrances, statutory or otherwise, subject to certain sections of the *Bankruptcy and Insolvency Act*, and that the Receiver was authorized "to apply the Funds against current or future indebtedness owing on either the Receiver's Charge or the Receiver's Borrowing Charge."

[14] I made the following comment during the hearing of the application:

> I am going to allow the order, but on the understanding that the funds are to be used to determine the priority of claims against the Graybriar funds and the Kenzie funds only, and not with respect to the other projects that might be in the receivership. If the Receiver determines that it wishes to proceed with those other projects, it must give notices to the parties here today so that there can be some determination of whether that is appropriate.

[15] Counsel for the Receiver immediately reminded the Court after this comment that the claims process "is only in relation to the Graybriar funds". I apologized for the error. Counsel for the Receiver then indicated that:

> ...I think it speaks to your point because this is how we are ... - you want things segregated and - ... we are proposing to segregate, so the Kenzie funds will fall into the general administration of the estate and the parties can make claims [to] them through the bankruptcy process. We don't need an independent process on them.

[16] Counsel for Kenzie investors questioned that comment. He submitted that his position was that use of the Court Funds:

> ...should be limited only to investigations and determinations of priority of competing claims, vis-à-vis those funds and that if the Receiver determines that there is no other competing claims that would disrupt the judgment creditors' otherwise entitlement to those funds, then those investors, those judgment creditors can make an application or can otherwise come back to the court to have those funds released back to that group, rather than being just general money in the receivership to the benefit of all potential creditors, so I want to make sure we are clear on that.

[17] After discussion among counsel and the Court, during which counsel for the Receiver indicated his view that the Court Funds were not trust funds, I noted that "even if it is in the general administration of the estate, you are only going to use it to investigate claims and priority with respect to that amount, is that correct?". The Receiver through counsel indicated that there was a significant portion of the fees outstanding, and that:

> ... you will see in your order that you are, you know, saying that we have first charge on both the Graybriar funds and the Court Funds. With that understanding, and we will have to come back and get fees approved at a later date and that's part of what we are doing today. That's fine to the Receiver. As long as we have the priority, we are happy then to adjudicate claims to the 235 based on entitlement...

[18] I questioned whether the fees of the Receiver outstanding at the time were incurred with respect to the determination of the claims with respect to the two funds of money. Counsel for the Receiver confirmed that the vast majority of the fees incurred fit that description but there was also “the usual general administration”. He later indicated that he did "not want to be entirely hamstrung with the [$235,000] in the general estate" with respect to fees.

[19] Again, counsel for the Kenzie investors questioned this. After discussion, the Receiver agreed to segregate the outstanding fees between the Graybriar matter and the Kenzie matter, which was acceptable to counsel for the Kenzie investors “as long as we can see that segregation both looking back and going forward”.

[20] Finally, counsel for Terrapin submitted that her client wanted the Court Funds segregated "to preserve any trust claims that we have", and asked that the funds not be commingled. Counsel for the Receiver responded that "[a]s long as the charge ranks in priority on them, we will be able to deal with allocation at the end of the piece", and that "... we are happy to have them in two separate accounts at Alvarez".

[21] As a result of this order, the Court Funds in the amount of $241,800 were released to the Receiver.

[22] The Kenzie investors take the position that this indicates that the Receiver agreed to segregate the Court Funds from the general assets of Arres Capital realized during the course of the bankruptcy and receivership, and to utilize those funds only for the Receiver's expenses incurred to deal with any competing claims of creditors (essentially Terrapin) against those funds but that the Court Funds were not otherwise to be available for the general expenses of the bankruptcy and receivership of Arres Capital.

[23] Subsequently, Jones, J. dismissed Terrapin's claim of an equitable mortgage with respect to the four Graybriar condominium units in the receivership proceedings of Arres Capital. Terrapin has confirmed that it is no longer making any claim against the Court Funds, and takes no position on the current application.

[24] Entitlement to the Graybriar funds referred to in the June 4, 2018 hearing has now been resolved by order of August 13, 2019. On that date, the Court authorized distribution of the Graybriar funds to various investors, authorized the payment of certain professional fees incurred by the investors who had been represented in the Graybriar litigation and approved the fees of the Receiver and its counsel to that date.

[25] As of August 21, 2020, the receivership maintained a cash balance of approximately $210,000.00, with an expected GST refund of approximately $11,500 to come. Exigible assets which the Receiver had not been able to monetize, mainly in the form of litigation assets, remain in the receivership, and the Receiver is of the view that, for a number of reasons, it is in the best interest of Arres Capital, its creditors and other stakeholders that it be discharged. Any interest in the remaining exigible assets would vest in the Trustee in bankruptcy.

[26] Receipts and disbursements to discharge are estimated at approximately $113,000, leaving approximately $109,000 in available funds.

[27] The Receiver takes the position that:

a) the Court Funds are not trust property, and are available for distribution to general creditors of the debtors;
b) the Court funds are subject to the priority claims of the Receiver's Charge and the Receiver's Borrowing Charge; and
c) whether or not claim to the Court Funds is a trust claim, the Receiver's professional fees and the fees of its counsel for the period from appointment to June 30, 2019 have been approved by the order of the Court on August 13, 2019.

[28] As there will remain a shortfall on the Receiver's Borrowing Charge, the Receiver does not view it necessary to determine any claims, trust or otherwise, to the Court Funds.

III. Position of the Parties

[29] The Receiver seeks court approval for its fees and disbursements and those of its counsel for the period from July 1, 2019 to July 31, 2020 in the amount of $15,542, and estimated fees and costs to complete the receivership of $50,000, which includes fees and costs incurred but not paid.

[30] The Kenzie investors submit that the Court Funds were to be segregated from other assets of Arres Capital and were only to be used to cover the Receiver's costs and expenses to sort out any contest to entitlement to those funds between the Kenzie plaintiffs and Terrapin. Since Terrapin no longer has a claim against the funds, and therefore the Receiver does not have to incur costs to determine such a claim, the funds should be paid to the Kenzie investors.

[31] The Kenzie investors submit that this was agreed among counsel for the Receiver, counsel for Terrapin and counsel for both Graybriar and the Kenzie investors, despite the provisions of the June 4, 2018 order. They do not rely on, or give evidence of, anything but the record of the June, 2018 hearing with respect to this submission.

IV. Analysis

[32] As noted previously, the transcript of the discussions at the hearing, and the provisions of the June 4, 2018 Order do not support either a direction of the Court or an agreement of counsel as described by the Kenzie investors. While I initially commented that the understanding was that the funds would only be used to determine the priority of claims against the two funds, I was swiftly corrected by counsel for the Receiver, who made it plain that the Kenzie funds would fall into general administration and that the Receiver's application was to obtain priority for the Receiver's Charge and the Receiver's Borrowing Charge over the Court Funds. This priority was reflected in the Order, and confirmed in the Fourth Report of the Receiver in 2019.

[33] In response to my further comment with respect to the use of the funds, counsel for the Receiver indicated that there was already a significant amount of fees outstanding and that "[a]s long as we have the priority, we are happy then to adjudicate claims to the [$235,000] based on entitlement". The Receiver agreed to segregate outstanding fees between the Graybriar matter and the Kenzie matter. It was counsel for Terrapin that wanted assurance that the Kenzie Court

Funds be segregated, to which counsel for the Receiver replied that, as long as the Receiver's charges had priority over them, the Receiver would be able to deal with allocation at the end of the piece, and that the funds would be held in two separate accounts by the Receiver.

[34] That is essentially what the Receiver did: the Graybriar funds were held in an account separate from the Court Funds which were held in the general account.

[35] If there was any misunderstanding about what the Receiver had agreed to do with respect to segregation, that misunderstanding should have been cleared up at the time of the Receiver's Fourth Report dated August 2, 2019. Under the heading "Interim Receipts and Disbursements - July 26, 2012 [the commencement of the receivership] to August 2, 2019", the Receiver discloses that the Court Funds were deposited in the general account and were included with other "receipts" of the receivership, subject to disbursements for professional fees and general and administrative costs.

[36] The Fourth Report also indicates that, in the Receiver's view, the Court Funds "are not trust property for the benefit of any Persons and therefore are available for distribution to general creditors of the Debtor". Ultimately, any distribution to general creditors is unlikely, and in fact there will be a shortfall to cover the Receiver's Borrowing Charge. The Fourth Report indicates that persons who wish to assert a trust or other claim to the assets "are able to do so in the receivership proceedings".

[37] The Fourth Report discloses specifically that:

> Because the Receiver is administering separate classes of assets that will be distributed for the benefit of separate classes of creditors, the Receiver has been careful to segregate professional fee charges and disbursements between the separate asset classes. Since May 2018, the Receiver and its legal counsel have separately recorded and charged their fees and disbursements to "Graybriar" (when performing work related to the Graybriar Funds) and to "General" (when performing work related to the general assets) so as to ensure that allocation of cost is fair and accurate.

[38] While the August, 2019 hearing dealt with distribution to the Graybriar investors and payment of their legal costs, the Court also approved the conduct of the Receiver as reported in the Fourth Report, the payment of the Receiver's general fees and expenses for the period from the inception of the receivership to June 30, 2019, and the payment of the Receiver's fees and expenses specific to the Graybriar issue.

[39] As noted by the Receiver, the interests of the Graybriar investors and those of the Kenzie investors were adverse at the time of the August, 2019 hearing. However, the Kenzie investors had notice of and were represented at the hearing by the same counsel as the Graybriar investors, and the order was not appealed.

[40] In the result, nothing can be done to claw-back distributions from the Graybriar investors, or the payment of their litigation costs. While there may have been a misunderstanding arising from the June, 2018, hearing, there was no breach by the Receiver of the June 4, 2018 Order or what was discussed and agreed to at the hearing.

[41] Although the Kenzie investors do not formally allege a trust with respect to the Court Funds, they submit that the funds were "earmarked" for them, and cite ***Stone Sapphire Ltd. v***

Transglobal Communications Group Inc., 2008 ABQB 575, upheld on appeal, 2009 ABCA 125.

[42] However, the claimant in that case, in similar circumstances as the Kenzie investors, was not able to establish priority over a secured creditor's claim. Topolniski, J. distilled principles relating to priority disputes over money paid into court at para. 11 of that decision:

1. To trump a trustee's priority to funds paid into court under a garnishee or as a condition of opening up a default judgment, the judgment creditor must have completed execution.
2. An order permitting payment out of monies paid into court on obtaining a further order is insufficient to trump the trustee's priority to the funds.
3. A judgment creditor is not elevated to the status of secured creditor by virtue of a payment into court, whether that payment is to advance an appeal or as security for costs.
4. A judgment creditor may trump a trustee's priority to funds paid into court if the funds are sufficiently 'earmarked' and the creditor has 'done all that it could' to access the funds. (***Careen Estate v Quinlan Brothers Ltd.*** (2004), 2004 NLSCTD 132 (CanLII), 2 C.B.R. (5th) 102 (Nfld. S.C.)).
5. A secured creditor trumps a trustee's priority to funds paid into court if the monies are the subject of valid security.

[43] The Court in ***Stone Sapphire*** noted the unusual facts of the ***Careen Estate*** case: money had been paid into court by Careen Estate pending disposition of a trial.

[44] When judgment was awarded against it, counsel for Careen Estate informed the trial judge that his client intended to make an assignment into bankruptcy that day. The trial judge ordered immediate payment out of the funds in court to the plaintiff, but when the defendant's counsel sought payment of the funds, courthouse staff informed him that the court needed to confirm the payment and issue a certificate in accordance with the *Rules of Court*, which could not be accomplished by the close of business that day. Within an hour of that happening, Careen Estate made an assignment into bankruptcy. Thus, only a bureaucratic error prevented the plaintiff from completing execution.

[45] With respect to the concept of "earmarked funds" generally, Topolniski, J. indicated at para 36 that the proposition offends the underlying premise of the *BIA* concerning distribution of a bankrupt's property among creditors, and the specific language of section 70 of the *BIA*. She noted that she was not satisfied that a 2013 decision that found otherwise remained good law in light of the Supreme Court's decision in ***T.E. Cleary Drilling Co. (Trustee of) v Beaver Trucking Ltd***., [1939] S.C.R. 317.

[46] I agree with the Court's reasoning in ***Stone Sapphire***, and find that the Kenzie investors have not established entitlement to priority over the Receiver's charges by reason of the funds being earmarked.

[47] The Kenzie investors submit that there was no basis going forward from the July, 2014 order of Strekaf, J. pursuant to which Arres Capital could have applied back to court to have the Court Funds paid out to it. However, that is essentially what the Receiver did in the July, 2018 application, and was successful.

[48] Finally, the Kenzie investors submit that it is unfair that they are unable to claim the Court Funds, since they have been working since 2014 to execute on their judgment, but were side-lined by the Terrapin claim.

[49] Their frustration is understandable, but the Court Funds have not been paid to another creditor in this case, but have been, and will be, subsumed by the Receiver's Charge and the Receiver's Borrowing Charge in this complex and litigious matter.

V. Conclusion

[50] I allow the Receiver's applications, and dismiss the application of the Kenzie investors for payment of the Court Funds.

[51] If the parties are unable to agree on costs, they may make written submissions.

Dated at Calgary, Alberta this 19th day of April, 2021.

B.E. Romaine
J.C.Q.B.A.

Appearances:

Walker W. MacLeod and Pantelis Kyriakakis
for the Receiver, Alvarez & Marsal Canada Inc.

Jeffrey L. Oliver
for Access Mortgage Corporation (2004) Limited

Loran V. Halyn
for the Kenzie Investors