COURT FILE NUMBER **Q.B. No. 1884 of 2019**

COURT OF QUEEN'S BENCH FOR SASKATCHEWAN

JUDICIAL CENTRE **SASKATOON**

**IN THE MATTER OF *THE COMPANIES' CREDITORS ARRANGEMENT ACT*, RSC 1985, c C-36, AS AMENDED (the "*CCAA*")**

**AND**

**IN THE MATTER OF A PROPOSED PLAN OF ARRANGEMENT FOR THE CREDITORS OF 101098672 SASKATCHEWAN LTD., MORRIS INDUSTRIES LTD., MORRIS SALES AND SERVICE LTD., CONTOUR REALTY INC., and MORRIS INDUSTRIES (USA) INC.**

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# BOOK OF AUTHORITIES OF 1742009 ALBERTA INC. (DBA AGRITERRA EQUIPMENT)

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# In the Matter of Section 193 of the Alberta Business Corporations Act, R.S.A. 2000, c. B-9, as amended; and in the matter of the Judicature Act, R.S.A. 2000, c. J-2, as amended,

And in the Matter of a Proposed Arrangement involving Value Creation Inc., BA Energy Inc. and the holders of common shares of Value Creation Inc.; And in the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended; and in the Matter of BA Energy Inc.

B.E. Romaine J.

Heard: June 1, 2010
Judgment: August 5, 2010 *
Docket: Calgary 0801-16292

Counsel: Chris D. Simard, Kelsey J. Drozdowski for Dresser-Rand Canada, Ltd.
David LeGeyt for Ernst & Young Inc.
Howard A. Gorman, Kyle D. Kashuba for BA Energy Inc.

Subject: Insolvency
**Related Abridgment Classifications**
Bankruptcy and insolvency
IX Proving claim
IX.4 Practice and procedure
IX.4.c Amendment of claim
**Headnote**
Bankruptcy and insolvency --- Proving claim — Practice and procedure — Amendment of claim
Debtor entered into agreement of sale with creditor for purchase of equipment — Total purchase price was US$8,577,942.39 — Debtor paid US$7,021,918 pursuant to purchase agreement before successfully applying for protection under Companies' Creditors Arrangement Act — Some equipment was still in creditor's possession at that time — Creditor filed proof of claim with monitor claiming US$1,655,477.95 secured by undelivered equipment — Monitor advised creditor it was free to sell undelivered equipment in satisfaction of its claim — Equipment was custom made and difficult to sell — Creditor filed late amended proof of claim for unsecured claim of US$1,474,161.63 and secured claim of US$177,382 — Monitor disallowed amended claim on basis that it was late — Creditor brought application for order requiring monitor to accept late amended proof of claim — Application dismissed — Amended claim was really new claim so it was properly treated as late — It would not have been fair or equitable to accept late amended proof of claim — Late amended claim was not result of inadvertence — Creditor delayed in valuing undelivered equipment — Creditor changed nature of its claim at time when all creditors would have been aware that distribution to unsecured creditors was expected to be substantial — Allowing late amended claim would have been prejudicial to debtor and other creditors — Debtor structured plan of arrangement on basis that creditor would not be affected — There were no conditions that would have alleviated relevant prejudice — Debtor was required to pay reasonable conduct money for employee of creditor who was cross-examined on his affidavit.
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Generally — referred to

*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36

Generally — referred to

APPLICATION by creditor for order requiring monitor to accept late amended proof of claim.

***B.E. Romaine J.*:**

**Introduction**

1 Dresser-Rand Canada, Inc. ("Dresser-Rand") applies for acceptance of its late amended proof of claim so that it may participate in a distribution to unsecured creditors pursuant to the plan of arrangement and reorganization of BA Energy Inc. ("BA Energy") under the *Companies' Creditors Arrangement Act.*

2 The issue is whether Dresser-Rand, having initially filed a claim which it characterized as fully secured on the basis of holding assets that it described as having a value equal to its claim, is entitled to file a late amended claim that now alleges that a large portion of the claim is unsecured.

**Facts**

3 In 2006, BA Energy had entered into an agreement of sale with Dresser-Rand for the purchase of a wet-gas compressor and ancillary equipment for use at the proposed Heartland Upgrader, a heavy oil upgrader that BA Energy was in the process of constructing at a site near Fort Saskatchewan, Alberta. The total purchase price for this compressor was USD $8,577,942.39.

4 On December 30, 2008, BA Energy was granted an initial order under the *Companies' Creditors Arrangement Act*,R.S.C. 1985, c. C-36 as amended (the "CCAA").

5 At the time of the filing under the CCAA, BA Energy had paid USD $7,021,918 pursuant to the purchase agreement, leaving a balance owing of USD $1,651.543.63. The compressor was still in the possession of Dresser-Rand at its premises in Edmonton, with the exception of some of the ancillary equipment which had been delivered to the proposed site of the Heartland Upgrader.

6 On March 9, 2009, counsel to Dresser-Rand enquired of counsel to BA Energy and counsel to the Monitor whether the balance of the purchase price would be paid, "failing which Dresser-Rand will be free to exercise its right of sale pursuant to the *Sale of Goods Act.*" On May 15, 2009, Dresser-Rand sent a Proof of Claim to the Monitor, signed by Dresser-Rand's General Manager in Canada, indicating that it had a secured claim for USD $1,655,477.95 and that "in respect of the said debt, we hold assets of the CCAA Debtor valued at $1,655,477.95 US as security". Under the Claims Procedure Order, claims were to be filed by June 15, 2009.

7 On August 26, 2009, BA Energy repudiated the purchase agreement and advised Dresser-Rand that it had a duty to mitigate its losses with respect to the terminated agreement.

8 In an email dated August 31, 2009, counsel to Dresser-Rand asked counsel to BA Energy to confirm that Dresser-Rand was free to deal with the compressor equipment in its possession and enquired whether BA Energy would return the parts in its possession. On the same day, counsel to BA Energy responded that Dresser-Rand could deal with the equipment subject to

  

any requirement to act reasonably in performing its duty to mitigate and said that he would ask his client about the equipment in its possession.

9 On September 18, 2009, the Monitor advised counsel to Dresser-Rand that, in light of the repudiation, Dresser-Rand's previous claim may have been stayed and that Dresser-Rand may have the right to file "Subsequent Claim" as set out in the Claims Procedure Order. The Monitor also told Dresser-Rand that BA Energy believed that the ancillary equipment in its possession was worth about $1 million. Counsel to Dresser-Rand responded that he did not believe his client would be interested in the equipment at that price.

10 On September 22, 2009, Dresser-Rand submitted a Subsequent Claim for USD $1,651,543.63 (taking into account a further invoice paid by BA Energy). Again, Dresser-Rand in its claim form characterized the claim as secured and, again, the claim form states that Dresser-Rand held assets of the CCAA Debtor valued at USD $1,651.543.63.

11 On December 16, 2009, the Monitor issued a Notice of Revision or Disallowance of the claim. This notice indicates that the Proof of Claim as submitted in the amount of USD $1,651,543.53 was revised and accepted at nil. The Monitor noted as follows:

> **Retained Assets**
>
> [Dresser-Rand] retained possession of certain assets as a result of the termination of the Purchase Order. In the Termination Letter the Applicant directed [Dresser-Rand] to mitigate its losses in respect of the termination of the Purchase Order. The Applicant noted in its review of [Dresser-Rand]'s Claim that the retained assets have a value in excess of the amount of [Dresser-Rand]'s Claim. Accordingly, the Applicant has revised [Dresser-Rand]'s claim to $0.00.

12 On December 18, 2009, counsel to Dresser-Rand asked to meet with counsel to BA Energy and the Monitor to discuss the reasoning behind the Notice of Revision, commenting that "(p)reviously you did not dispute our priority to the extent of what we could realize from the equipment we have in our possession." The email also notes that the compressor is custom-made equipment and that its sale may take some time.

13 On December 20, 2009, counsel to Dresser-Rand delivered a Notice of Dispute to the Monitor, with a covering letter that noted as follows:

> With respect to the enclosed Notice of Dispute, in reviewing the documentation you forwarded to Dresser-Rand Canada, Inc. in this regard, this simply may be a situation where there is misunderstanding of terminology between us. Looking at your statement about the "retained assets", you do not appear to be disputing Dresser-Rand Canada, Inc.'s right to retain the assets in question (being compressor equipment) and deal with it as it wishes. To this stage, we have always valued the retained assets as being worth as much or more than the debt that is owed by BA Energy Inc. to Dresser-Rand Canada, Inc. We do not believe that you should have put $0.00 beside the secured aspect of this claim in the Notice of Revision or Disallowance dated December 16, 2009.

14 The Notice of Dispute lists $1,651.543.63 under the designation "Reviewed Claim or Subsequent Claim as Disputed" and characterizes this amount as "Secured". It makes no claim on an unsecured basis. The Notice stipulates that "(t)his claim is fully secured. The Notice of Revision or Disallowance did not reflect this fact."

15 A without-prejudice conference call was held on January 6, 2010 among counsel to BA Energy, the Monitor and counsel to Dresser-Rand.

16 In an email dated January 11, 2010, the Monitor asked Dresser-Rand's counsel whether he had been able to determine the appropriate person for the Monitor to speak to with respect to the equipment in the possession of BA Energy. Counsel to Dresser-Rand responded that he had not and that he was "awaiting the letter [counsel to BA Energy] indicated last week you would be sending on the other point that deals more generally with the claim, etc."

17 On January 14, 2010, the Monitor sent counsel to Dresser Rand an email that attached a letter that he was asked to review, commenting: ... "let me know if it meets your needs before I finalize it."

  

18 The letter, marked "draft", reads as follows:

> As Court Appointed Monitor of BA Energy Inc. I am sending this letter to you as a follow-up to our teleconference of January 5, 2010 and to provide more clarity with respect to the Notice of Revision and Notice of Dispute between BA Energy Inc. ("BA Energy") and Dresser Rand Canada, Inc. ("DRC").
>
> As agreed on our teleconference, BA Energy does not dispute DRC's rights to retain the assets in question and deal with them as it wishes. This right means DRC shall have no claim against BA Energy given that the value of the assets are at least as much or more than the claim amount. Furthermore, I must note that DRC will accept all potential risks and rewards of its actions in dealing with the assets. For further clarity, should DRC sell the assets for an amount greater than the amount of the claim filed against BA Energy, then this excess amount benefits DRC. Should DRC sell the assets for an amount less than DRC's claim against BA Energy, DRC will not be able to claim the difference against BA Energy.
>
> *I trust this clarifies any misunderstanding between the parties.*
>
> (emphasis added)

19 Counsel to Dresser-Rand responded saying that the letter would be reviewed internally and by his client and that he would get back to the Monitor. Numerous emails ensued between counsel to Dresser-Rand and the Monitor. On January 25, 2010, counsel to Dresser-Rand advised the Monitor that "I am told that I should hear from someone in the US part of the organization tomorrow. Unfortunately, many people have become involved within my client and has made it more complex for me to get instructions."

20 In an email dated January 27, 2010, counsel to Dresser Rand advised the Monitor that:

> ...my people as of yesterday were still assessing their position, including what can be done with the part of the compressor they have and those parts which BA has in its position. Unfortunately, these machines are very custom made for a particular customer and are not readily saleable or useable for anyone else. They [sic] inquiries out to see what they can do and hope to get back to me this week.

21 On February 19, 2010 counsel to Dresser-Rand left a voice mail for the Monitor. The recording was not preserved. Counsel to Dresser-Rand in an email to his client said that in the voice mail, he enquired if BA Energy was interested in making an offer to Dresser-Rand for the compressor "with the concept being that if an acceptable cash offer was made to [Dresser-Rand] for that equipment, [Dresser Rand] would forego any further claim against [BA Energy] for the balance owing." The Monitor in an email to BA Energy said that in the voice mail, counsel to Dresser-Rand was enquiring whether BA Energy would like to acquire the compressor for an unnamed price and that "if [BA Energy] acquired this equipment then Dresser-Rand would withdraw their claim".

22 On February 23, 2010, BA Energy advised the Monitor that it did not wish to purchase the compressor. On the same day, the Monitor filed its Ninth Report with the Court and served it on the parties on the service list. The report states that BA Energy anticipated filing a plan of arrangement which would result in a recovery that would be better than a liquidation, and that it was expected that the plan would be brought to the Court for approval in mid to late March, 2010. During this time period, the Monitor and BA Energy were finalizing the sale of a key asset necessary to fund the plan and were in the course of structuring the plan.

23 On March 15, 2010, BA Energy filed and served its Notice of Motion for approval to circulate a plan of arrangement and hold a meeting of creditors. Dresser-Rand was not listed either as an affected or unaffected creditor nor was it mentioned on the list of disputed claims.

24 Apparently, counsel to Dresser-Rand had not yet been added to the service list at this time and did not receive a copy of the Ninth Report until it was posted on the Monitor's web-site on March 16, 2010. Counsel to Dresser-Rand received a copy of the plan motion materials on March 17, 2010 and requested to be put on the service list on that date. The Monitor also informed

  

counsel to Dresser-Rand on March 17, 2010 that BA Energy was not interested in purchasing the compressor from Dresser-Rand and that it took the position that the Dresser-Rand claim had been satisfied.

25 On March 18, 2010, the Court approved the circulation of the plan of arrangement to creditors.

26 On March 26, 2010, Dresser-Rand submitted a late amended proof of claim in which it stated it had an unsecured claim of USD $1,474,161.63 and a secured claim of USD $177,382.

27 On April 5, 2010, the Monitor issued a Notice of Revision or Disallowance relating to Dresser-Rand's amended proof of claim, with a revised claim amount of zero. The Monitor set out the following as reasons for disallowance:

> Dresser-Rand's Late Amended proof of claim dated March 26, 2010, claiming an unsecured claim in the amount of $1,474,161.63 USD and a secured claim in the amount of $177,382.00 USD (the "Late Amended Claim") is barred and extinguished pursuant to the claims procedure order dated April 29, 2009 (the "Claims Procedure Order"). The Late Amended Claim is in essence the same as the Initial Claim (as defined below) submitted by Dresser-Rand, which claim has been resolved as described below.
>
> Dresser-Rand was aware of and participated in the claims process established under the Claims Procedure Order. Dresser-Rand's initial proof of claim was received by the Monitor on or about May 15, 2009, as amended to a Subsequent Claim (as defined in the Claims Procedure Order) on September 22, 2009 (the "Initial Claim") following BA Energy's repudiation of the purchase order. The Initial Claim by Dresser-Rand was for $0.00 unsecured and Dresser-Rand acknowledged it held equipment or collateral of a value equal to its claim.
>
> On December 16, 2009, the Monitor issued a notice of revision or disallowance thereby disallowing the total claim amount listed by Dresser-Rand in its Initial Claim (the "NOR"). The reason for the disallowance in the NOR was that Dresser-Rand acknowledged that it retained possession of the collateral equipment that it held in full satisfaction of the Initial Claim amounts (the "POC Satisfaction"), therefore, Dresser-Rand had no claim against BA Energy. Dresser-Rand did respond by issuing a notice of dispute on December 21, 2009 (the "NOD"); however, the NOD served to only address a "misunderstanding of terminology" on the part of Dresser-Rand regarding the classification of the claim amounts and not a dispute as to or the rejection of the POC Satisfaction. After further discussions between the parties, the Monitor sent draft correspondence to Dresser-Rand's solicitors dated January 13, 2010 affirming the POC Satisfaction, that Dresser-Rand was retaining the equipment in full satisfaction of its claim and that it had the risk and benefit of any potential recovery. Throughout the process leading up to the Late Amended Claim, Dresser-Rand valued the collateral equipment as being worth as much or more than the debt owed by the Applicant.
>
> BA Energy and the Monitor relied upon the proofs of claim as filed in the claims process, including the Initial Claim, in calculating the dividend in the BA Energy Plan of Arrangement filed March 10, 2010 (the "Plan"). The inclusion of the Late Amended Claim would have significantly affected BA Energy's/the Monitor's calculations and provisions contained in the Plan, and the subsequent BA Energy creditor review, consideration and implementation of the Plan.
>
> The Dresser-Rand filing of the Late Amended Claim occurred only after distribution of the Plan proposing a 55% dividend. Allowance of the Amended Proof of Claim would: (i) circumvent the *Companies' Creditor Arrangement Act* (Canada) process, the Claims Procedure Order and provide Dresser-Rand an unjustified and improper advantage, and (ii) prejudice BA Energy and/or BA Energy's creditors generally in the pro rata or total distribution under the Plan.

28 Dresser-Rand filed a Notice of Dispute on April 8, 2010, submitting that there was no resolution of its claim as asserted by the Monitor, that it was "prudent and reasonable" for it to amend its claim on March 26, 2010 and that not accepting the claim would be prejudicial to Dresser-Rand and not prejudicial to BA Energy or its creditors. Dresser-Rand filed a Notice of Motion with respect to its claim on April 12, 2010 and served the service list.

  

29 The meeting of creditors was held on April 15, 2010. Only one creditor appeared in person: the rest voted by proxy. No-one voted against the plan. Counsel to Dresser-Rand read a prepared statement indicating that it had filed an amended proof of claim that may impact the other creditors if ultimately validated.

**Analysis**

30 Dresser-Rand submits that the amended proof of claim it filed on March 26, 2010 is not a "late claim", but merely an amendment to the September, 2009 proof of claim which was filed in a timely manner in compliance with the Claims Procedure Order. I cannot agree with this submission. The amended proof of claim purports to assert an unsecured claim for the first time, a claim that would qualify as an affected claim under the plan as opposed to the fully-secured claim previously asserted. It changes the nature of the original claim to such a degree that it must be considered a new claim and not a mere amendment.

31 Dresser-Rand initially filed its claim on the basis that it was in possession of assets of such a value as to satisfy its claim and that it was secured by its possession of such assets. It maintained that position for approximately eight months, leading the debtor and the Monitor to believe, not unreasonably, that Dresser-Rand would not be an affected creditor in a plan of arrangement. BA Energy structured its plan on that assumption. Dresser-Rand changed its approach and amended its claim to file in large part as an affected unsecured creditor at a time when it would have been clear to creditors that the distribution to unsecured creditors under a plan would be substantial, albeit prior to a formal vote by unsecured creditors on the plan.

32 While this application involves a determination of whether Dresser-Rand's late amended claim should be accepted, it is neither a clear case of a creditor "lying in the weeds" nor is it clearly the kind of late claim reviewed by Wittmann, J. A. (as he then was) in *Blue Range Resource Corp., Re*, 2000 ABCA 285 (Alta. C.A.), the leading authority on the assessment of late claims. However, the principles set out in *Blue Range* are relevant to the application.

33 Wittmann, J. A. set out the following as appropriate criteria for a court to apply to the assessment of late claims:

> 1. Was the delay caused by inadvertence and if so, did the claimant act in good faith?
>
> 2. What is the effect of permitting the claim in terms of the existence and impact of any relevant prejudice caused by the delay?
>
> 3. If relevant prejudice is found, can it be alleviated by attaching appropriate conditions to an order permitting late filing?
>
> 4. If relevant prejudice is found which cannot be alleviated, are there any other considerations which may nonetheless warrant an order permitting late filing?

34 In identifying these criteria and applying them to specific late claims, Wittmann, J. A. favoured a "blended approach", taking into consideration both the standards set out under the *Bankruptcy and Insolvency Act*. and the U.S. Bankruptcy Rules, and informed by concepts drawn from the approaches taken in a variety of areas of law when dealing with late notice or delays in process. It is clear from the nature of the criteria that the question of whether a late claim should be accepted is an equitable consideration, taking into account the specific circumstances of each case.

***A. Inadvertence and Good Faith***

35 Wittmann, J.A. noted that "inadvertence" in the context of the first criterion includes carelessness, negligence or accident and is unintentional.

36 BA Energy submits that Dresser-Rand's conduct in this case cannot be described as careless, negligent or accidental, but arose from a deliberate intent to reframe its claim as an unsecured claim when it became apparent that there would be a distribution to unsecured creditors of approximately $0.55 per dollar of claim.

  

37 It is clear that Dresser-Rand was aware of BA Energy's process under the CCAA from shortly after the initial order and had retained counsel active on its behalf as early as March, 2009. It filed its initial proof of claim in a timely manner in May, 2009. It was aware from August, 2009 that BA Energy had repudiated the agreement but it was also clear that from March, 2009, Dresser-Rand took the position that it was free to exercise a right of sale of the equipment in its possession. I agree that it cannot be said that Dresser-Rand's amended proof of claim arose from inadvertence.

38 BA Energy alleges that Dresser-Rand has acted in bad faith in putting forth its recharacterized and amended claim only when it became apparent that it may do better as an unsecured creditor, given the level of distribution to unsecured creditors anticipated by the successful monetization of assets.

39 While there is insufficient evidence to reach the conclusion that Dresser-Rand acted in bad faith, it is true that it would have been clear to creditors in the relevant time period that a successful plan with an acceptable distribution to unsecured creditors was a strong possibility. At the least, Dresser-Rand delayed approximately eight months before taking any substantial or meaningful steps to value the assets in its possession in order to come to a valuation of its security. While Scott Kaffka, an employee of a U.S. affiliate of Dresser-Rand, suggests in his affidavits that Dresser-Rand was investigating the possibility of remarketing the equipment before January, 2010, it is also clear from the affidavits and cross-examination on them that relatively little was done in that regard until Mr. Kaffka became involved and contacted an equipment dealer to obtain an estimate of value for the compressor on January 28, 2010, some eleven months after counsel for Dresser-Rand first stated that it took the position that it was entitled to sell the equipment. It is noteworthy that on January 27, 2010, counsel to Dresser-Rand advised the Monitor that Dresser-Rand was still assessing its position, and that the opinion as to of value that Dresser-Rand relies upon was not formally prepared until March 19, 2010.

40 The consequences of the delay in adequately investigating the value of the assets it held as security for its claim, which accounts for most of the delay in filing the amended claim, must be borne by Dresser-Rand. The question of the resale value of the compressor was a question within the reasonable control of Dresser-Rand to determine.

41 The objective of a claims procedure order is to attempt to ensure that all legitimate creditors come forward on a timely basis. A claims procedure order provides the debtor and the Monitor with the information necessary to fashion a plan that may prove acceptable to the requisite majority of creditors given the financial circumstances of the debtor and that may be sanctioned by the court. The fact that accurate information relating to the amount and nature of claims is essential for the formulation of a successful plan requires that the specifics of a claims procedure order should generally be observed and enforced, and that the acceptance of a late claim should not be an automatic outcome. The applicant for such an order must provide some explanation for the late filing and the reviewing court must consider any prejudice caused by the delay.

42 The claims procedure process was developed to give creditors a level playing field with respect to their claims and to discourage tactics that would give some creditors an unjustified advantage. Situations that give rise to concerns of improper manipulation of the process by a creditor must be carefully considered.

43 Dresser-Rand was offered an opportunity to amend its claim after the purchase agreement with BA Energy was formally repudiated, and did so on September 22, 2010, confirming its initial claim with only a slight variation in amount claimed. As late as December 21, 2009, Dresser-Rand characterized its claim as a fully-secured claim its Notice of Dispute and concedes that it believed at least to this point in time that the compressor was worth at least as much as its claim. Dresser-Rand submits that there was delay by the Monitor in responding to the amended claim, but a three-month delay in the circumstances of a large restructuring with many claims is not unusual. Dresser-Rand also submits that the Monitor should have reacted more quickly to its February 19, 2010 suggestion that it was open to accepting an unspecified cash offer from BA Energy to settle its claim. While the Monitor did not respond for roughly a month, it is clear that the Monitor was involved in preparing and filing a key report on the restructuring with the Court and also involved in a major monetization of BA Energy's assets that would subsequently fund the plan.

***B. Prejudice Caused by the Delay***

  

44 BA Energy, in consultation with the Monitor, prepared its plan in the early months of 2010 without making any provision for an unsecured deficiency claim from Dresser-Rand. Given what had been communicated among the parties with respect to Dresser-Rand's claim at this point of time, this was not unreasonable.

45 It is difficult to determine what the effect Dresser-Rand's late amended claim may have had on the decisions of creditors with respect to whether to approve the plan. All but one creditor voted on the plan by proxy, and some of those proxies were authorized before Dresser-Rand served other creditors with a Notice of Motion with respect to its revised claim on April 12, 2010. Dresser-Rand states in its brief that 16 out of 30 proxies were submitted after April 7, 2010. Therefore, roughly half of the creditors in number had already voted on the plan several days prior to receiving notice of Dresser-Rand's late claim.

46 With respect to the materiality of the claim, it would if accepted comprise approximately 5.4% of the total pool of affected creditors and, if paid from plan proceeds, would reduce the amount available to unsecured creditors from 55 cents per dollar of a claim to 53 cents per dollar of claim. The Dresser-Rand claim therefore is not as insignificant as the late claims accepted by the Court in *Blue Range*.

47 As noted in *Blue Range* at paragraph 40, the fact that creditors may receive less money if a late claim is accepted is not prejudice relative to the second criterion. The test is whether creditors by reason of the late claim lost a realistic opportunity to do anything that they otherwise might have done. In this case, it is not possible to determine if any of the proxy votes cast in favour of the plan would have been affected by knowledge of the late claim. It is only apparent that a significant number of creditors were not aware of the claim when they decided how to vote.

48 During the sanction hearing of April 16, 2010, BA Energy indicated that, instead of reducing the distribution to other creditors if Dresser-Rand's late claim was accepted by the Court, BA Energy would find another way to pay the required distribution to Dresser-Rand.

49 Consideration of prejudice is not restricted to prejudice to other creditors. The second criterion also requires consideration of prejudice to the debtor company or other interested parties: *Blue Range* at paras. 14 and 18. The timing of the late claim with respect to the stage of proceedings is a key consideration in determining whether there has been prejudice: *Blue Range* at para. 36.

50 The parties prejudiced by this late amended claim are BA Energy and its parent Value Creation, BA Energy's largest secured creditor. Value Creation refrained from requiring BA Energy to pay all of the proceeds of the assets it had monetized on Value Creation's secured claim and allowed BA Energy to use a portion of those proceeds to distribute to other creditors under the plan. While there is no doubt that Value Creation benefits from BA Energy's restructuring under the CCAA as a continuing entity with surviving assets, the postponement of a portion of Value Creation's secured claim was arrived at in consideration of the status of creditor claims as they had been filed, without Dresser-Rand's late amended claim.

51 It is not surprising that BA Energy did not attempt to alter its plan after having received notice of Dresser-Rand's amended proof of claim. Given the negotiations that necessarily proceed a vote on the plan, the status of proxy voting and the limited time to the creditors' meeting, BA Energy did not have a realistic opportunity to amend its plan to include Dresser-Rand without the risk of losing support from other creditors and jeopardizing the plan.

52 In *Lindsay v. Transtec Canada Ltd.* (1994), 28 C.B.R. (3d) 110 (B.C. S.C.) at para. 74, Huddart, J. held, in a case where there would have been no effect on other creditors if a late claim was accepted as it would be paid from post-arrangement revenue, that it was fair to refuse to grant leave to the late creditor to commence an action against the debtor company for a number of reasons, noting that "(a) CCAA proceeding is not a stage for an individual creditor to try to ensure the best possible position for himself ... As in bankruptcy proceedings, it is not unfair that a creditor who attempts to gain an advantage for himself should find himself disentitled to recover anything."

53 While the facts of this case are distinguishable from the facts before the Court in *Lindsay*, Dresser-Rand filed a very late revised claim after months of relative lack of diligence with respect to the value of its security, at a time when it had become

  

apparent that the distribution to unsecured creditors under a proposed plan would be substantial. Dresser-Rand's recovery would be improved considerably by its very late recharacterization of claim if Dresser-Rand's new submissions with respect to the resale value of the compressor is accepted.

54 Dresser-Rand submits that, from its perspective, the Monitor's draft letter of January 14, 2010 was a "proposed resolution" of the claim, and that thus BA Energy and the Monitor should have been aware from early 2010 that the Dresser-Rand claim was unresolved and that Dresser-Rand would be claiming a deficiency in value as an unsecured claim. While the letter is marked "draft" and the Monitor requested a response before it was finalized, it refers to an agreement reached in the teleconference and the clarification of a misunderstanding arising from the Notice of Revision. While the Monitor was advised that this letter was being reviewed by Dresser-Rand, and Dresser-Rand invited a proposal for settlement on February 19, 2010, it was not until March 26, 2010, ten months after the expiry of the initial claims bar date that Dresser-Rand made its revised position clear to the debtor and the Monitor.

55 Mr. Kaffka states in his affidavits that Dresser-Rand received a verbal estimate of value from an equipment dealer on January 28, 2010. It may well be that Dresser-Rand did not wish to disclose the low resale value it was now alleging for the compressor at a point in time when it was hoping that BA Energy would make an offer to purchase the compressor, but this was a strategic decision by Dresser-Rand, and, again, the risk of further delay in clearly communicating its revised estimate of value because of this strategic decision must be borne by Dresser-Rand.

56 Dresser-Rand also submits that it would have filed its amended claim sooner had the Monitor advised it sooner that BA Energy was not interested in purchasing the compressor. It is true that Dresser-Rand may have been able to file its amended claim at the end of February, 2010 instead of at the end of March, 2010 had the Monitor responded earlier to Dresser-Rand's suggestion that BA Energy may wish to make an offer on the equipment, but it should be noted that Dresser-Rand's "proposal" was merely an invitation to BA Energy to make a settlement offer, and not a proposal specifying an acceptable price for the compressor that may have alerted the Monitor to its importance. The Monitor in the Thirteenth Report to the Court dated April 30, 2010 explained that it did not place a high priority on its response to the voice-mail enquiry as it thought that it was one of several enquiries that Dresser-Rand was making to potential purchasers to of the compressor.

57 Dresser-Rand submits that BA Energy knew as early as January 14, 2010 (the date of the Monitor's draft letter) that Dresser-Rand may have been in the position of recovering less than it was owed if it sold the equipment. While this was anticipated as a possibility in the January 14, 2010 letter, the responsibility for valuing the equipment Dresser-Rand claimed as its security cannot be transferred to the debtor or the Monitor. Dresser-Rand is in the business of manufacturing and marketing the equipment, and had as late as September 22, 2009 made the formal representation in its revised proof of claim that the equipment was worth the amount of its claim. It appears that in January 2010, an officer of BA Energy enquired of the Monitor whether BA Energy could recover any surplus proceeds from Dresser-Rand's sale of the compressor, further indicating that there is no evidence that either the debtor or the Monitor anticipated Dresser-Rand's late change of position on value.

***C. Other Considerations***

58 Dresser-Rand submits that equity favours its application, as it is a wronged party with a legitimate claim that has been compromised by the CCAA proceedings. While if Dresser-Rand's current position with respect to value is accepted, it may suffer a deficiency in its claim of roughly $1.6 million still owing on the purchase price of roughly $8 million for the compressor, Dresser-Rand has possession of the compressor and current estimates of a deficiency are still speculative. There is no overwhelming equitable consideration that would counter-balance relevant prejudice to BA Energy of the late claim.

59 Dresser-Rand submits that the situation is similar to that described in *Look Communications Inc., Re* (2005), 21 C.B.R. (5th) 265 (Ont. S.C.J. [Commercial List]). However, this is not a situation where BA Energy was aware at all times of the applicant's claim and did not object, nor is it a case where, had court approval of the claim been sought prior to plan approval, it would be clear that such approval would be granted as a matter of course. No assumptions can be made about the outcome if this amended claim had been brought in a timely way and disputed.

  

***D. Conclusion on a Late Claim***

60 It would not be fair or equitable to accept this late amended claim. Given the facts of this case, there are no conditions that would alleviate relevant prejudice.

61 If I am wrong in my assessment of whether the late revised claim should be accepted, I would agree with BA Energy that the claim should not in any event be accepted as set out in the Amended Proof of Claim, but should be remitted to the Monitor to allow a proper consideration of value. BA Energy and the Monitor have not been given an opportunity to test the allegations made as to the resale value of the compressor as would occur in the normal course of a claim, given the timing of the late claim in relation to the plan and its sanctioning. While the parties may not have discussed this in advance of the application, it is clear that this was not a normal claims dispute, but was restricted to the issue of whether the claim should be accepted.

***E. Conduct Money***

62 In support of this application, Dresser-Rand filed and relied upon affidavits sworn by Mr. Kaffka, who resides in New York. Mr. Kaffka was cross-examined on these affidavits. Dresser-Rand submits that BA Energy should be required to pay conduct money for Mr. Kaffka's attendance at cross-examination.

63 BA Energy objects to paying conduct money for Mr. Kaffka's cross-examination because he is not an employee of Dresser-Rand Canada Inc., because he had no involvement with the issues prior to January, 2010 and because Dresser-Rand has employees in Alberta who could have provided an affidavit, including Bill Colpitts, its recently-retired General Manager who was involved with the matter and signed the first Proof of Claim.

64 Dresser-Rand submits that Mr. Kaffka was an appropriate affiant because he was primarily responsible for Dresser-Rand's mitigation efforts after January, 2010 and because he was the individual who determined the market value of the compressor.

65 While Mr. Kafka's evidence of pre-2010 efforts by Dresser-Rand to mitigate and to assess value was of necessity hearsay, he was involved in 2010 mitigation efforts. He was not so clearly an inappropriate witness that Dresser-Rand is disentitled to reasonable conduct money. I direct that BA Energy be required to pay reasonable conduct money for Mr. Kaffka's attendance.

***F. Costs***

66 This is not an appropriate case to depart from the usual practice with respect to costs in commercial insolvency applications, and therefore both Dresser-Rand and BA Energy will bear their own costs.

*Application dismissed.*

Footnotes

* A corrigendum issued by the court on August 13, 2010 has been incorporated herein.

**Most Negative Treatment:** Check subsequent history and related treatments.

2000 ABCA 285
Alberta Court of Appeal

Blue Range Resource Corp., Re

2000 CarswellAlta 1145, 2000 ABCA 285, [2000] A.J. No. 1232, [2001] 2 W.W.R. 477, 100 A.C.W.S. (3d) 956, 193 D.L.R. (4th) 314, 234 W.A.C. 138, 271 A.R. 138, 87 Alta. L.R. (3d) 352

# In the matter of the Companies' Creditors Arrangement Act, R.S.C. 1985 c. C-36, as amended; and in the matter of Blue Range Resources Corporation; Enron Canada Corp., and the Creditor's Committee (Appellants/Appellants) and National Oil-well Canada Ltd. et al. (Respondents/Respondents)

Russell, Sulatycky, Wittmann JJ.A.

Heard: June 15, 2000
Judgment: October 24, 2000
Docket: Calgary Appeal 99-18564, 99-18565, 99-18566, 99-18567, 99-18568, 99-18569, 99-18570, 99-18571, 99-18802

Proceedings: affirmed *Blue Range Resource Corp., Re* (1999), 1999 CarswellAlta 1053, 251 A.R. 1 (Alta. Q.B.)

Counsel: *A. Robert Anderson* and *Scott J. Burrell*, for Enron Canada Corp. and Creditors' Committee.
*S. Collins*, for TransAlta Utilities Corporation.
*D.W. Dear*, for Rigel Oil & Gas Ltd.
*D. Mann*, for Barrington Petroleum Ltd. and PetroCanada Oil & Gas.
*K.E. Staroszik*, for Founders Energy Ltd.
*J.N. Thom*, for National-Oilwell Canada Ltd. and Campbell's Industrial Supply Ltd.

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

**Related Abridgment Classifications**

Bankruptcy and insolvency
XIX Companies' Creditors Arrangement Act
XIX.3 Arrangements
XIX.3.b Approval by court
XIX.3.b.iv Miscellaneous
Bankruptcy and insolvency
XIX Companies' Creditors Arrangement Act
XIX.5 Miscellaneous

**Headnote**

Corporations --- Arrangements and compromises — Under Companies' Creditors Arrangement Act — Miscellaneous issues
Monitor appointed by court obtained order establishing procedure to determine claims of creditors of corporation — Claims bar date was set during which creditors could prove claims — Notices of claim filed after claims bar date by certain creditors were disallowed by monitor — Partial distribution was made by court — Late-filing creditors applied to court for permission to file or amend claims after expiry of claims bar date — Applications were allowed on basis that same test should apply to late-filing creditors under Companies' Creditors Arrangement Act (CCAA) as under Bankruptcy and Insolvency Act (BIA) — Creditor EC Corp. and creditors committee appealed — Appeal dismissed — Claims bar orders setting out claims procedure ought not to purport to extinguish debt, but simply set deadline for obtaining remedy — Inadvertence alone can be basis for permitting late filing, provided claimant can show it acted in good faith and not in effort to manipulate its position — Any prejudicial effect of

  

permitting claim is relevant factor, as is availability of means to alleviate prejudice — All creditors had acted in good faith and existing creditors suffered no prejudice as result of late filings or amendments — Existing creditors were aware of potential for further claims and that these might be permitted by court — No evidence existed to suggest that existing creditors would have voted differently on plan of arrangement had late-filing creditors filed in time — Value of claims of late-filing creditors was less than one per cent of total of claims filed in time — Fact that existing creditors might receive less money if late claims allowed did not constitute prejudice, since policy of CCAA depends on all legitimate creditors being able to participate in available proceeds — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 — Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36.

Corporations --- Arrangements and compromises — Under Companies' Creditors Arrangement Act — Arrangements — Approval by Court — Miscellaneous issues

Monitor appointed by court obtained order establishing procedure to determine claims of creditors of corporation — Claims bar date was set during which creditors could prove claims — Notices of claim filed after claims bar date by certain creditors were disallowed by monitor — Partial distribution was made by court — Late-filing creditors applied to court for permission to file or amend claims after expiry of claims bar date — Applications were allowed on basis that same test should apply to late-filing creditors under Companies' Creditors Arrangement Act (CCAA) as under Bankruptcy and Insolvency Act (BIA) — Creditor EC Corp. and creditors committee appealed — Appeal dismissed — Claims bar orders setting out claims procedure ought not to purport to extinguish debt, but simply set deadline for obtaining remedy — Inadvertence alone can be basis for permitting late filing, provided claimant can show it acted in good faith and not in effort to manipulate its position — Any prejudicial effect of permitting claim is relevant factor, as is availability of means to alleviate prejudice — All creditors had acted in good faith and existing creditors suffered no prejudice as result of late filings or amendments — Existing creditors were aware of potential for further claims and that these might be permitted by court — No evidence existed to suggest that existing creditors would have voted differently on plan of arrangement had late-filing creditors filed in time — Value of claims of late-filing creditors was less than one per cent of total of claims filed in time — Fact that existing creditors might receive less money if late claims allowed did not constitute prejudice, since policy of CCAA depends on all legitimate creditors being able to participate in available proceeds — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 — Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36.

**Table of Authorities**

**Cases considered by *Wittmann J.A.*:**

*Allen v. Sir Alfred McAlpine & Sons Ltd.*, [1968] 2 Q.B. 229, [1968] 1 All E.R. 543 (Eng. C.A.) — applied

*Cohen, Re* (1956), 19 W.W.R. 14, 3 D.L.R. (2d) 528, 36 C.B.R. 21 (Alta. C.A.) — considered

*Hogan v. Kolisnyk*, [1983] 3 W.W.R. 481, 25 Alta. L.R. (2d) 17, 43 A.R. 17 (Alta. Q.B.) — considered

*Kuziw v. Kucheran Estate*, 2000 ABCA 226 (Alta. C.A.) — considered

*Lethbridge Motors Co. v. American Motors (Can.) Ltd.* (1987), 53 Alta. L.R. (2d) 326, 20 C.P.C. (2d) 11, 79 A.R. 321, 40 D.L.R. (4th) 544 (Alta. C.A.) — considered

*Lindsay v. Transtec Canada Ltd.* (1994), 28 C.B.R. (3d) 110, 5 C.C.P.B. 219, [1995] 2 W.W.R. 404, 99 B.C.L.R. (2d) 73 (B.C. S.C.) — distinguished

*Mount James Mines (Que.) Ltd., Re* (1980), 28 O.R. (2d) 271, 33 C.B.R. (N.S.) 227, 110 D.L.R. (3d) 80 (Ont. Bktcy.) — considered

*Pacific National Lease Holding Corp., Re* (1992), 72 B.C.L.R. (2d) 368, 19 B.C.A.C. 134, 34 W.A.C. 134, 15 C.B.R. (3d) 265 (B.C. C.A. [In Chambers]) — considered

*Pioneer Investment Services Co. v. Brunswick Associates Ltd. Partnership* (1993), 507 U.S. 380, 113 S. Ct. 1489 (U.S. Tenn.) — considered

*Smoky River Coal Ltd., Re*, 175 D.L.R. (4th) 703, 237 A.R. 326, 197 W.A.C. 326, 71 Alta. L.R. (3d) 1, [1999] 11 W.W.R. 734, 12 C.B.R. (4th) 94 (Alta. C.A.) — considered

*Specialty Equipment Cos. Inc., Re* (1993), 159 B.R. 236 (U.S. Bankr. N.D. Ill.) — considered

*W. Schoeler Trucking Ltd. v. Markel Insurance Co. of Canada* (1979), 9 Alta. L.R. (2d) 232, 19 A.R. 196, [1980] I.L.R. 1-1210 (Alta. Dist. Ct.) — considered

*312630 British Columbia Ltd. v. Alta Surety Co.*, 30 C.C.L.I. (2d) 165, 10 B.C.L.R. (3d) 84, [1995] 10 W.W.R. 100, 23 C.L.R. (2d) 273, 61 B.C.A.C. 208, 100 W.A.C. 208 (B.C. C.A.) — applied

**Statutes considered:**

*Bankruptcy Code*, 11 U.S.C. 1982

  

Chapter 11 — referred to
*Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3
Generally — considered
*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36
Generally — considered

s. 6 — considered

s. 12(2)(a)(iii) — referred to
*Insurance Act*, R.S.A. 1980, c. I-5
s. 205 — referred to

s. 211 — referred to

s. 385 — referred to

**Rules considered:**
*Alberta Rules of Court*, Alta. Reg. 390/68
Generally — considered

R. 244(4) [en. Alta. Reg. 234/94] — considered
*Federal Rules of Bankruptcy Procedure (U.S.)*
Generally — referred to

R. 9006(b)(1) — considered

APPEAL by creditor EC Corp. and creditors committee from judgment reported at (1999), 251 A.R. 1 (Alta. Q.B.), permitting creditors to file notices of claim, or amended claims, after expiry of claims bar date.

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

**Introduction**

1 The *Companies' Creditors Arrangement Act*, R.S.A. 1985, c. C-36, as amended ("*CCAA*"), permits the compromise and resolution of claims of creditors against an insolvent corporation. In this appeal, as part of the ongoing resolution of the insolvency of Blue Range Resources Corporation ("Blue Range"), this Court has been asked to state the applicable criteria in considering whether to allow late claimants to file claims after a stipulated date in an order ("claims bar order").

2 In his decision below, the chambers judge determined that in the circumstances of this case it was appropriate to allow the respondents ("late claimants") to file their claims thus entitling them to participate in the *CCAA* distribution.

**Facts**

3 Blue Range sought and received court protection from its creditors under the *CCAA* on March 2, 1999. The claims procedure established by PriceWaterhouse Coopers Inc. ("the Monitor"), and approved by the court in a claims bar order, fixed a date of May 7, 1999 at 5:00 p.m. by which all claims were to be filed. Due to difficulties in obtaining the appropriate records, the date was extended in a second order to June 15, 1999 at 5:00 p.m., for the joint venture partners. The relevant orders stated that claims not proven in accordance with the set procedures "shall be deemed forever barred" (A.B.P.01, A.B.P.06). Under this procedure $270,000,000 in claims were filed.

4 The respondent creditors in this appeal fall into two categories: first, those who did not file their Notices of Claim before the relevant dates in the claims bar orders, and second, those who filed their initial claims in time but sought to amend their claims after the relevant dates. All of these creditors applied to the chambers judge for relief from the restriction of the date in the claims bar orders and to have their late or amended claims accepted for consideration by the Monitor.

  

5 The chambers judge allowed the late and amended claims to be filed. The appellants, Enron Capital Corp. ("Enron") and the Creditor's Committee, seek to have that decision overturned. I granted leave to appeal on January 14, 2000 on the following question:

> What criteria in the circumstances of these cases should the Court use to exercise its discretion in deciding whether to allow late claimants to file claims which, if proven, may be recognized, notwithstanding a previous claims bar order containing a claims bar date which would otherwise bar the claim of the late claimants, and applying the criteria to each case, what is the result? (A.B.928).

**Judgment Below**

6 The chambers judge found that the applicable section of the *CCAA*, s. 12(2)(iii) did not mandate a claims procedure. He stated that preserving certainty in the *CCAA* process was not a sufficient reason to deny the late claimants a second chance. In his view, taking a strict reading of the claims bar orders would have the effect of denying creditors, who have a logical explanation for their non- compliance with the order, any recovery. While the chambers judge noted that compromise is required by creditors in a *CCAA* proceeding, he did not think it fair that these late claimants be required to compromise 100 per cent of their legitimate claims. In addition, the chambers judge was of the view that process required flexibility and should avoid pitting creditors against one another.

7 Having decided that flexibility in the process was required, the chambers judge then considered an appropriate test for allowing the filing of late claims. Although encouraged by the appellants to adopt an approach similar to that contained in the *United States Bankruptcy Code*, *Federal Rules of Bankruptcy Procedure*, for Chapter 11 Reorganization Cases, ("*U.S. Bankruptcy Rules*") the chambers judge chose to incorporate the test in place under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"). Specifically, he found that because the situation of Blue Range was essentially a liquidation, the approach used in the *BIA* was appropriate. Under the *BIA*, late claims are permitted under almost any circumstance provided no injustice is done to other creditors. A late filing creditor under the *BIA* may only share in undistributed assets. Therefore, the chambers judge found that the creditors should be allowed to file late claims, or to amend existing claims late.

**Standard of Review**

8 It has been recently held by this court that decisions of a *CCAA* supervising judge should only be interfered with in clear cases. Deference to a *CCAA* supervising judge is generally appropriate where the questions before the court deal with management issues and are of necessity matters which must be decided quickly. This issue was addressed by Macfarlane, J.A. in *Pacific National Lease Holding Corp., Re* (1992), 15 C.B.R. (3d) 265 (B.C. C.A. [In Chambers]) (cited with approval by Hunt, J.A. in *Smoky River Coal Ltd., Re* (1999), 237 A.R. 326 (Alta. C.A.)) as follows at 272:

> ...I am of the view that this court should exercise its powers sparingly when it is asked to intervene with respect to questions which arise under the CCAA. The process of management which the Act has assigned to the trial court is an ongoing one. In this case a number of orders have been made...
>
> ...
>
> Orders depend on a careful and delicate balancing of a variety of interests and of problems. In that context appellate proceedings may well upset the balance, and delay or frustrate the process under the CCAA.

The chambers judge was exercising his discretion under the *CCAA* in granting an extension of the claims bar dates. However, the criteria upon which that discretion is to be exercised is a matter of legal principle, and therefore on that issue, the standard of review is correctness.

**Analysis**

  

9 As a preliminary matter I wish to comment on the nature of the order granted and the notices sent out to the individual creditors. The order dated April 6, 1999 stated in paragraph 2:

> Claims not proven in accordance with the procedures set out in Schedules "A" and "B" shall be deemed forever barred and may not thereafter be advanced as against Blue Range in Canada or elsewhere. (A.B.P.01)

The first page of Schedule "A" stated in part:

> A Claims' Bar Date of 5:00 p.m. Calgary time on May 7, 1999 has been set by the Alberta Court of Queen's Bench. All claims received by the monitor or postmarked after the Claims' Bar Date will be forever extinguished, barred and will not participate in any voting or distributions in the CCAA proceedings.
>
> [Emphasis added] (A.B.P.03).

The language used in Schedule "A" goes beyond the text of the order. Although it may not be of practical significance, barring the right of a claimant to a remedy is fundamentally different from erasing the debt. The court under the *CCAA* has powers to compromise and determine, but only in accordance with the process prescribed in the statute.

10 It was urged before the court in oral argument by counsel for the appellants that the purpose of the wording of the claims bar orders was to "smoke out" the creditors. I am dubious that the severe wording of the claims bar orders is effective to "smoke out" the creditor who may otherwise lie dormant. The objective of making certain that all legitimate creditors come forward on a timely basis has to be balanced against the integrity and respect for the court process and its orders. Courts should not make orders that are not intended to be enforced in accordance with their terms. All counsel conceded that the court had authority to allow late filing of claims, and that it was merely a matter of what criteria the court should use in exercising that power. It necessarily follows that a claims bar order and its schedule should not purport to "forever bar" a claim without a saving provision. That saving provision could be simply worded with a proviso such as "without leave of the court", which appears to be not only what was contemplated, but what in fact occurred here.

**The Appropriate Criteria**

11 The appellants advocated the adoption of the criteria under the *U.S. Bankruptcy Rules*, Chapter 11, while the respondents favoured either the application of the tests under the *BIA* or some blending of the two standards.

12 Rule 9006 of the *U.S. Bankruptcy Rules* deals with the extension of time in these circumstances. The relevant portion of the Rule states:

> 9006 (b)(1) ... when an act is required or allowed to be done at or within a specified period by these rules or by a notice given thereunder or by order of court, the court for cause shown may at any time in its discretion (1) with or without motion or notice order the period enlarged if the request is made before the expiration of the period originally prescribed or as extended by a previous order or (2) on motion made after the expiration of the specified period permit the act to be done where the failure to act was the result of excusable neglect.

The key phrase in this section is "excusable neglect". In *Pioneer Investment Services Co. v. Brunswick Associates Ltd. Partnership*, 507 U.S. 380, 113 S. Ct. 1489 (U.S. Tenn. 1993) the U.S. Supreme Court dealt with the interpretation of this phrase. In *Pioneer*, the creditor's attorney, due to disruptions in his legal practice and confusion over the form of notice, failed to file a Notice of Claim in time. The U.S. Supreme Court noted that excusable neglect may extend to "inadvertent delays" (at pg 391) and went on to identify the relevant considerations when determining whether or not a delay is excusable. The Court said at 395:

> Because Congress has provided no other guideposts for determining what sorts of neglect will be considered "excusable", we conclude that the determination is at bottom an equitable one, taking account of all relevant circumstances surrounding the party's omission. These include, as the Court of Appeals found, the danger of prejudice to the debtor, the length of

  

> the delay and its potential impact on judicial proceedings, the reason for the delay, including whether it was within the reasonable control of the movant, and whether the movant acted in good faith.

The American authorities also seem to reflect that the burden of meeting all of these elements, including showing the absence of prejudice, lies with the party seeking to file the late claim: e.g. *Specialty Equipment Cos. Inc., Re*, 159 B.R. 236 (U.S. Bankr. N.D. Ill. 1993).

13 The Canadian approach under the *BIA* has been somewhat different. Canadian courts have been willing to allow the filing of late or amended claims under the *BIA* when the claims are delayed due to inadvertence, (which would include negligence or neglect), or incomplete information being available to the creditors, see: *Mount James Mines (Que.) Ltd., Re* (1980), 110 D.L.R. (3d) 80 (Ont. Bktcy.). The Canadian standard under the *BIA* is, therefore, less arduous than that applied under the *U.S. Bankruptcy Rules*.

14 I accept that some guidance can be gained from the *BIA* approach to these types of cases but I find that some concerns remain. An inadvertence standard by itself might imply that there need be almost no explanation whatever for the failure to file a claim in time. In my view inadvertence could be an appropriate element of the standard if parties are able to show, in addition, that they acted in good faith and were not simply trying to delay or avoid participation in *CCAA* proceedings. But I also take some guidance from the *U.S. Bankruptcy Rules* standard because I agree that the length of delay and the potential prejudice to other parties must be considered. To this extent, I accept a blended approach, taking into consideration both the *BIA* and *U.S. Bankruptcy Rules* approaches, bolstered by the application of some of the concepts included in other areas, such as late reporting in insurance claims, and delay in the prosecution of a civil action.

15 In *Lindsay v. Transtec Canada Ltd.* (1994), 28 C.B.R. (3d) 110 (B.C. S.C.), the applicant was an unsecured creditor of Alberta Pacific Terminals Ltd. ("APCL"). Transtec Canada Ltd. was indebted to the applicant and APCL had guaranteed the obligation. APCL sought protection under the *CCAA*. Through oversight, the applicant Lindsay was not sent the relevant *CCAA* materials by APCL and was not included in the *CCAA* proceedings. He did not, therefore, have the opportunity to vote on the plan of arrangement. It is clear, however, that Lindsay at some point during the *CCAA* proceedings became aware of them, and at various stages had his lawyers contact APCL's lawyers to inquire about the process. Despite this knowledge he did not pursue the matter. Lindsay then came to the court seeking permission to sue APCL as a guarantor, potentially recovering considerably more than those creditors who participated in the *CCAA* process.

16 After reviewing all of the facts, Huddart, J. found that "Lindsay (or solicitors on his behalf) made considered, deliberate, decisions not to notify Alberta-Pacific of his claim until after the approval order and then not until after the closing of the share purchase agreement" (para 19). She then went on to conclude that Lindsay preferred not to participate in the *CCAA* process and chose to take his chances later on.

17 In deciding how to exercise her discretion, Huddart, J. applied the following factors: "the extent of the creditor's actual knowledge and understanding of the proceedings; the economic effect on the creditor and debtor company; fairness to other creditors; the scheme and purpose of the *CCAA* and the terms of the plan" (para 56). On these criteria, Huddart, J. found that it would not be equitable to allow Lindsay to pursue a claim as he was well aware of what was going on in the *CCAA* proceedings, chose not to participate, and his late action would cause serious prejudice both to the debtor company and to the other creditors.

18 While *Lindsay* is clearly distinguishable on its facts from the within appeal, the case does highlight the issues of the conduct of the late claimants and the potential prejudice to other creditors and the debtor. Lindsay was the classic creditor "lying in the weeds", waiting for the appropriate moment to pounce. He did not act in good faith and his conduct was potentially prejudicial to other creditors and the debtor company. By avoiding the *CCAA* proceedings, Lindsay was attempting to gain an advantage not available to other creditors.

19 There is further support for a blended approach in several other areas of the law where courts have had to deal with the impact of delays and late filings. In particular, I have considered the courts' treatment of delays in the prosecution of actions and the late filing of notices of claim to insurers.

  

20 In *Lethbridge Motors Co. v. American Motors (Can.) Ltd.* (1987), 53 Alta. L.R. (2d) 326 (Alta. C.A.) the court had to decide whether or not to allow an action to continue where no steps had been taken by the plaintiff for five years. In deciding that the action could continue, Laycraft, C.J.A. relied on the following test from the English Court of Appeal in *Allen v. Sir Alfred McAlpine & Sons Ltd.*, [1968] 1 All E.R. 543 (Eng. C.A.) where Salmon L.J. said at 561:

> In order for the application to succeed the defendant must show:
>
> (i) that there has been inordinate delay. It would be highly undesirable and indeed impossible to attempt to lay down a tariff - so many years or more on one side of the line and a lesser period on the other. What is or is not inordinate delay must depend on the facts of each particular case. These vary infinitely from case to case, but it should not be too difficult to recognise inordinate delay when it occurs.
>
> (ii) that this inordinate delay is inexcusable. As a rule, until a credible excuse is made out, the natural inference would be that it is inexcusable.
>
> (iii) that the defendants are likely to be seriously prejudiced by the delay. This may be prejudice at the trial of issues between themselves and the plaintiff, or between each other, or between themselves and the third parties. In addition to any inference that may properly be drawn from the delay itself, prejudice can sometimes be directly proved. As a rule, the longer the delay, the greater the likelihood of serious prejudice at the trial.

Relying on this test, as well as additional refinements, the Court found that the fundamental rule was that it was "necessary for a defendant to show serious prejudice before the court will exercise its jurisdiction to strike out an action for want of prosecution" (at pg. 331). The onus of showing serious prejudice has now been substantially altered as the result of amendments to the *Alberta Rules of Court* in 1994. Rule 244(4) now states that proof of inordinate and inexcusable delay constitutes *prima facie* evidence of serious prejudice: *Kuziw v. Kucheran Estate*, 2000 ABCA 226 (Alta. C.A.).

21 Similar questions can arise in an insurance context where an insured is required to file a proof of loss or other notice of claim within a certain time period under a contract of insurance. For example, s. 205 of the *Insurance Act*, R.S.A. 1980, c. I-5 states:

> 205 [w]here there has been imperfect compliance with a statutory condition as to the proof of loss to be given by the insured or other matter or thing required to by done or omitted by the insured with respect to the loss and the consequent forfeiture or avoidance of the insurance in whole or in part and the Court considers it inequitable that the insurance should be forfeited or avoided on that ground, the Court may relieve against forfeiture or avoidance on such terms as it considers just.

22 Similar wording is also found in ss. 211 and 385 of the *Insurance Act* and similar legislation exists throughout the common law provinces.

23 When deciding whether to grant relief from forfeiture in an insurance context the Alberta courts have generally adopted a two part test, see: *Hogan v. Kolisnyk* (1983), 25 Alta. L.R. (2d) 17 (Alta. Q.B.). In *Hogan* the court found it appropriate to look first at the conduct of the insured to determine whether the insured is guilty of fraud or wilful misconduct. Second, the court considered whether the insurer had been seriously prejudiced by the imperfect compliance with the statutory provision (at 35). The "noncomplying" party can show that there was no prejudice by showing that the innocent party had actual knowledge of the events in question and was thereby able to investigate the situation.

24 Considering whether the insurer has suffered any prejudice, the court in *Hogan* quoted from a decision of Stevenson, D.C.J. in *W. Schoeler Trucking Ltd. v. Markel Insurance Co. of Canada* (1979), 9 Alta. L.R. (2d) 232 (Alta. Dist. Ct.) at 237 where Stevenson, D.C.J. said "[t]he root of the question is whether or not it (the insurer) would have acted any differently if it had been given notice of the loss when it should have been given notice". In *312630 British Columbia Ltd. v. Alta Surety Co.* (1995), 10 B.C.L.R. (3d) 84 (B.C. C.A.) the B.C. Court of Appeal set out a more recent formulation of the test, namely whether the insurer by reason of the late notice had lost a realistic opportunity to do anything that it might otherwise have done.

 

25 These authorities arise in a clearly different context from that which I am dealing with in this case, but they demonstrate that there is a somewhat consistent approach in a variety of areas of the law when dealing with the impact of late notice or delays in particular processes.

26 Therefore, the appropriate criteria to apply to the late claimants is as follows:

1. Was the delay caused by inadvertence and if so, did the claimant act in good faith?

2. What is the effect of permitting the claim in terms of the existence and impact of any relevant prejudice caused by the delay?

3. If relevant prejudice is found can it be alleviated by attaching appropriate conditions to an order permitting late filing?

4. If relevant prejudice is found which cannot be alleviated, are there any other considerations which may nonetheless warrant an order permitting late filing?

27 In the context of the criteria, "inadvertent" includes carelessness, negligence, accident, and is unintentional. I will deal with the conduct of each of the respondents in turn below and then turn to a discussion of potential prejudice suffered by the appellants.

**National-Oilwell Canada Ltd. ("National")**

28 National, and National as the successor in interest to Dosco Supply, a division of Westburne Industrial Enterprises Ltd. ("Dosco") indicate that their claims were filed late due to the unexpected illness and resulting lengthy absence of their credit manager who was in charge of the Blue Range accounts receivable. National submitted the National and Dosco notices of claims on June 7, 1999 (AB V, pgs 538 and 542). National's claim is $58,211.00 and Dosco's claim is $390,369.13. National and Dosco clearly acted in good faith and provided the Notices of Claim as soon as the relevant personnel became aware of the situation.

**Campbell's Industrial Supply Ltd. ("Campbell's")**

29 Campbell's initial claim in the amount of $14,595.22 was filed prior to the date in the relevant claims bar order. Campbell's then amended its claim on June 25, 1999 and again on July 8, 1999 to $23,318.88. The claim was amended after the relevant date as a result of a representative from Blue Range informing Campbell's that its claim should include invoices sent to Trans Canada Midstream, Berkley Petroleum, Big Bear Exploration and Blue Range Resources Corporation (A.B. 495-496). In addition, there appears to have been some delay due to the Notices of Claim not being sent to the correct Campbell's office. Campbell's acted in good faith throughout and it is in fact arguable that any delay in the proper filing of its claims was actually due to errors on the part of Blue Range rather than its own doing.

**TransAlta Utilities Corporation ("TransAlta")**

30 TransAlta did not comply with the dates in the claims bar orders. It contends that it did not receive the claims package prior to the relevant dates. It is apparent from the evidence that the claims package was sent to TransAlta at its accounts receivable office, rather than the registered office for service (A.B.432-434). TransAlta was permitted to file its total claim of $120,731.00 by order of the chambers judge dated September 7, 1999. There is no evidence that TransAlta was attempting to circumvent the *CCAA* process. On the contrary, as soon as the appropriate personnel became aware of the situation, TransAlta took the necessary steps to have its Notice of Claim filed.

**Petro-Canada Oil and Gas ("PCOG")**

31 PCOG filed extensive claims material with the Monitor prior to the relevant dates showing several unsecured claims. The Monitor's draft third interim report indicated that four of PCOG's claims should properly have been classified as secured. The mistake by PCOG was the result of a misapprehension of how operator's liens functioned under the CAPL Operating Procedures

 

incorporated into the contracts giving rise to the claims. PCOG then sought to amend its claims and have them changed from unsecured to secured status (A.B. 554), on July 7, 1999. The change in status would result in claims of $137,981.30 being amended from unsecured to secured. There was no lack of good faith.

**Barrington Petroleum Ltd. ("Barrington")**

32 Barrington was acquired by Sunoma Energy Corp ("Sunoma") in about September, 1998. An affidavit filed by Sunoma's controller indicates that the financial records of Barrington were found to have been in complete disarray. Barrington's initial Notice of Claim in the amount of $223,940.06 was submitted prior to the relevant date. Barrington received a Notice of Dispute of Claim which approved the claim to the extent of $57,809.37, but disputed the remainder. On reviewing the issue, Barrington's controller determined that Blue Range was correct, but at the same time she identified additional invoices of which she had been unaware (A.B.549-551). On discovering the additional invoices, Barrington then submitted an amended Notice of Claim on July 22, 1999 and an objection to the Notice of Dispute of Claim. Barrington acted in good faith.

**Rigel Oil & Gas Ltd. ("Rigel")**

33 The full amount of Rigel's Notice of Claim was $146,429.68. This Claim was filed prior to the relevant date and the amount was approved by Blue Range. After the relevant date, on August 12, 1999, Rigel moved to amend and to allege that, despite Blue Range's claims to the contrary, its claim was secured, rather than unsecured. The only issue for Rigel on appeal is if their claim is properly secured can it be accepted because it was not claimed as secured until August 12, 1999.

**Halliburton Group Canada Inc. ("Haliburton")**

34 Halliburton was in the process of attempting to collect on accounts receivable owed by Big Bear Exploration Ltd. through May and June, 1999. They subsequently became aware, after the relevant date, that a claim in the amount of $11,309.90 was in fact against Blue Range, and should properly have been filed as a Notice of Claim in the *CCAA* proceedings (A.B. 497-499). On making this discovery, Halliburton wrote to the Monitor on July 14, and July 26, 1999 requesting that its claim be included in the *CCAA* proceeding. The Monitor disputed this claim as having been filed too late (A.B. 498). It appears that Halliburton acted in good faith.

**Founders Energy Ltd. ("Founders")**

35 Founders filed its claim prior to the relevant date, but, due to an oversight, claimed as an unsecured rather than a secured creditor. After filing its initial Notice of Claim, Founders received a Notice of Dispute from Blue Range. Within the 15 day appeal period, but outside the claims bar date, Founders then filed an amended Notice of Claim claiming a secured interest in the sum of $365,472.39, on July 26, 1999.

**Prejudice**

36 The timing of these proceedings is a key element in determining whether any prejudice will be suffered by either the debtor corporation or other creditors if the late and late amended claims are allowed. The total of all late and amended claims of the late claimants, secured and unsecured, is approximately $1,175,000. As set out above, in the initial claims bar order, the relevant date was 5:00 p.m. May 7, 1999. This date was extended for joint venture partners to 5:00 p.m. on June 15, 1999. The Plan of Arrangement, sponsored by Canadian Natural Resources Ltd. ("CNRL"), was voted on and passed on July 23, 1999. Status as a creditor, the classification as secured or unsecured, and the amount of a creditor's claim, are relevant to voting: s.6 *CCAA*.

37 Enron and the Creditor's Committee claim that they would be prejudiced if the late claims were allowed because, had they known late claims might be permitted without rigorous criteria for allowance, they might have voted differently on the Plan of Arrangement. Enron in particular submits that it would have voted against the CNRL Plan of Arrangement, thus effectively vetoing the plan, if it had known that late claims would be allowed. This bald assertion after the fact was not sufficient to compel the chambers judge to find this would in fact have been Enron's response. Nowhere else in the evidence is there any indication that late claimants being allowed would have impacted the voting on the different proposed Plans of Arrangement. In addition,

  

materiality is relevant to the issue of prejudice. The relationship of $1,175,000 (which is the total of late claims) to $270,000,000 (which is the total of claims filed within time) is .435 per cent.

38 Also, the contrary is indicated in the Third Interim Report of the Monitor where it is shown in Schedule D-1 (A.B.269) that $2 million was held as an estimate of unsecured disputed claims. Therefore, when considering which Plan of Arrangement to vote for, Enron, and all of the creditors, would have been aware that $2 million could still be legitimately allowed as unsecured claims, and would have been able to assess that potential effect on the amount available for distribution.

39 Further, the late claimants were well known to the Monitor and all of the other creditors. The evidence discloses that officials at Enron received an e-mail from the Monitor on May 18, 1999 indicating that there were several creditors who had filed late, after the first deadline of May 7, and the Monitor thought that even though they were late the court would likely allow them (A.B.1040). Finally, all of the late claimants were on the distribution list as having potential claims. (A.B. 9-148). It cannot be said that these late claimants were lying in the weeds waiting to pounce. On the contrary, all parties were fully aware of who had potential claims, especially Enron and the Creditors Committee.

40 In a *CCAA* context, as in a *BIA* context, the fact that Enron and the other Creditors will receive less money if late and late amended claims are allowed is not prejudice relevant to this criterion. Re-organization under the *CCAA* involves compromise. Allowing all legitimate creditors to share in the available proceeds is an integral part of the process. A reduction in that share can not be characterized as prejudice: *Cohen, Re* (1956), 36 C.B.R. 21 (Alta. C.A.) at 30-31. Further, I am in agreement with the test for prejudice used by the British Columbia Court of Appeal in *312630 British Columbia Ltd*. It is: did the creditor(s) by reason of the late filings lose a realistic opportunity to do anything that they otherwise might have done? Enron and the other creditors were fully informed about the potential for late claims being permitted, and were specifically aware of the existence of the late claimants as creditors. I find, therefore, that Enron and the Creditors will not suffer any relevant prejudice should the late claims be permitted.

**Summary of Criteria**

41 In considering claims filed or amended after a claims bar date in a claims bar order, a *CCAA* supervising judge should proceed as follows:

1. Was the delay caused by inadvertence and if so, did the claimant act in good faith?

2. What is the effect of permitting the claim in terms of the existence and impact of any relevant prejudice caused by the delay?

3. If relevant prejudice is found can it be alleviated by attaching appropriate conditions to an order permitting late filing?

4. If relevant prejudice is found which cannot be alleviated, are there any other considerations which may nonetheless warrant an order permitting late filing?

**Conclusion**

42 Applying the criteria established, I find that the conclusion reached by the chambers judge ought not to be disturbed, and the late claims filed by the respondents should be permitted under the *CCAA* proceedings. The appeal is dismissed.

*Appeal dismissed.*

**Most Negative Treatment:** Check subsequent history and related treatments.

2011 ONCA 160
Ontario Court of Appeal

Credifinance Securities Ltd., Re

2011 CarswellOnt 1218, 2011 ONCA 160, [2011] O.J. No. 894,
198 A.C.W.S. (3d) 578, 277 O.A.C. 377, 74 C.B.R. (5th) 161

# In the Matter of the Bankruptcy of Credifinance Securities Limited, of the City of Toronto, in the Province of Ontario

Deloitte & Touche Inc., in its Capacity as Trustee in Bankruptcy of Credifinance Securities Limited (Appellant) and DSLC Capital Corp. (Respondent)

S.T. Goudge, Robert Sharpe, H.S. LaForme JJ.A.

Heard: January 7, 2011
Judgment: March 2, 2011
Docket: CA C51766

Proceedings: affirming *Credifinance Securities Ltd., Re* (2010), 2010 CarswellOnt 830, 2010 ONSC 984, 63 C.B.R. (5th) 250 (Ont. S.C.J. [Commercial List])

Counsel: Catherine Francis for Appellant
Gregory Sidlofsky for Respondent

Subject: Insolvency; Civil Practice and Procedure; Estates and Trusts

**Related Abridgment Classifications**

Bankruptcy and insolvency
IX Proving claim
IX.2 Disallowance of claim
IX.2.c Appeal from disallowance
IX.2.c.ii Grounds
Bankruptcy and insolvency
XVII Practice and procedure in courts
XVII.8 Costs
XVII.8.d Award of costs
XVII.8.d.iii Payable by trustee personally

**Headnote**

Bankruptcy and insolvency --- Proving claim — Disallowance of claim — Appeal from disallowance — Grounds

C Ltd. made assignment in bankruptcy in August 2009 — D Corp. filed proof of claim in amount of $400,000 in September 2009 — D Corp. maintained that sum of $310,500 in C Ltd.'s possession was its property; trustee denied claim in full — D Corp. successfully appealed, claiming to be victim of fraud and alleging that $310,500 amount was directly traceable to $400,000 loan — Trial judge held that L, representative of D Corp., was deceived by B, of C Ltd. — B did not inform L of contingent liabilities when, to B's knowledge, there was outstanding investigation which could potentially result in charges against C Ltd. — In addition, there was outstanding U.S. lawsuit in which plaintiffs were seeking millions from defendants, one of which was C Ltd. — Trial judge found that L would not have entered into agreement but for deceit and would not have loaned C Ltd. $400,000 — Evidence showed that $310,500 was traceable to $400,000 and funds should be subject of constructive trust in favour of D Corp. in order to prevent further unjust enrichment of C Ltd — Trustee appealed; D Corp. cross-appealed seeking leave to

  

appeal decision not to award costs — Appeals dismissed — Constructive trust in bankruptcy proceedings can be ordered to remedy injustice; Prerequisite is that bankrupt obtained property through misconduct — Appeal judge made relevant findings which demonstrated why case at bar was somewhat exceptional — But for deceit, L would not have entered into any agreement concerning C Ltd., would not have loaned it money, and C Ltd. would not have had $310,500 in its bank account — Importantly, only creditors of C Ltd. impacted by appeal judge's order were B and his lawyers — Enriching B with windfall and depriving D Corp. of its interest in $310,500 would have been fundamentally unjust — Constructive trust was just.

Bankruptcy and insolvency --- Practice and procedure in courts — Costs — Award of costs — Payable by trustee personally

**Table of Authorities**

**Cases considered by *H.S. LaForme J.A.*:**

*Ascent Ltd., Re* (2006), 2006 CarswellOnt 116, 9 P.P.S.A.C. (3d) 176, 18 C.B.R. (5th) 269 (Ont. S.C.J.) — considered

*Charlestown Residential School, Re* (2010), 2010 ONSC 4099, 70 C.B.R. (5th) 13, 2010 CarswellOnt 5343 (Ont. S.C.J.) — referred to

*Elez, Re* (2010), 54 E.T.R. (3d) 31, 2010 ONSC 1052, 2010 CarswellOnt 874 (Ont. S.C.J.) — considered

*Farm Mutual Financial Services Inc., Re* (2010), 66 C.B.R. (5th) 85, 2010 CarswellOnt 2147, 2010 ONSC 2184 (Ont. S.C.J. [Commercial List]) — referred to

*Galaxy Sports Inc., Re* (2004), 2004 BCCA 284, 2004 CarswellBC 1112, 20 R.P.R. (4th) 1, 240 D.L.R. (4th) 301, 1 C.B.R. (5th) 20, 29 B.C.L.R. (4th) 362, 200 B.C.A.C. 184 (B.C. C.A.) — referred to

*Katz, Re* (2005), 2005 CarswellOnt 3995, 14 C.B.R. (5th) 193 (Ont. S.C.J.) — referred to

*McNaughton Automotive Ltd. v. Co-operators General Insurance Co.* (2008), 95 O.R. (3d) 365, 2008 ONCA 597, 2008 CarswellOnt 7384, 298 D.L.R. (4th) 86, 250 O.A.C. 252, 62 C.P.C. (6th) 196 (Ont. C.A.) — considered

**Statutes considered:**

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

Generally — referred to

s. 81 — considered

s. 197(1) — considered

s. 197(3) — considered

**Rules considered:**

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

R. 45.02 — referred to

APPEAL by trustee from judgment reported at *Credifinance Securities Ltd., Re* (2010), 2010 CarswellOnt 830, 2010 ONSC 984, 63 C.B.R. (5th) 250 (Ont. S.C.J. [Commercial List]), granting claimant constructive trust over what remained of loan to bankrupt; CROSS-APPEAL by claimant from decision not to award costs.

***H.S. LaForme J.A.*:**

**Introduction**

1 Credifinance Securities Limited ("Credifinance") made an assignment in bankruptcy. DSLC Capital Corp. ("DSLC") filed a proof of claim in the amount of $400,000. In its proof of claim, DSLC maintained that the sum of $310,500 in the possession of Credifinance was its property. Deloitte & Touche Inc., as Trustee of Credifinance (the "Trustee"), denied the claim in full. DSLC appealed that decision in the Superior Court.

2 The appeal judge found that DSLC had been defrauded into loaning Credifinance the $400,000. The appeal judge granted DSLC a constructive trust over what remained of the loan — $310,500 — and determined that it did not form part of the bankrupt estate. The Trustee appeals this decision.

3 DSLC cross-appeals, seeking leave to appeal the decision of the appeal judge not to award costs to DSLC. If leave is granted, DSLC is seeking an award of costs against the Trustee personally.

  

**Background**

4 There is a good deal more to the factual background of this case than what I propose to set out. What I intend to do is simply provide that background that I believe is necessary to give context to my analysis and ultimate conclusions.

***The lawsuit***

5 On February 6, 2009, DSLC issued a notice of action against Credifinance, Georges Benarroch (who controlled Credifinance) and others and obtained an *ex parte* Mareva injunction.

6 On March 6, 2009, DSLC filed a statement of claim seeking damages, an Order winding up Credifinance, oppression remedy relief, and the appointment of a receiver. DSLC did not assert a constructive trust claim; rather, it alleged that Credifinance had failed to repay the $400,000 loan.

7 On April 2, 2009 DSLC amended its claim seeking an Order rescinding the Subscription Agreement and the Share Purchase Agreement (the agreements related to the loan and the relationship between DSLC and Credifinance) on the basis of the alleged "dishonest and fraudulent conduct of the defendants". DSLC repeated its allegation that Credifinance had refused to repay the $400,000 loan.

8 On April 20, 2009, the Mareva injunction was dismissed as against the defendants other than Credifinance. However, the motion judge ordered that $310,500 be preserved pursuant to r. 45.02 of the *Rules of Civil Procedure*, whereupon the injunction would be dissolved against Credifinance. He found that, of the $460,000 that had been frozen in Credifinance's bank accounts, $310,500 on deposit with the National Bank could be identified as remaining from the $400,000 loan.

9 On July 23, 2009, Credifinance's motion for leave to appeal the order of the motion judge was dismissed. On August 24, 2009 Benarroch assigned Credifinance into bankruptcy. Credifinance has never paid the $310,500 into court.

10 The only creditors of Credifinance are DSLC, Benarroch — directly and through a corporation — and Benarroch's lawyers. Benarroch and his company Credifinance Capital Corp. allege that they are secured creditors owed $127,032.07. The lawyers who represent the defendants including Benarroch claim to be owed a total of $128,546.25.

***The trustee proceedings***

11 Before setting out the basic facts of this part of the background, I think it will be useful to set out the provisions of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (BIA) that are at the core of this appeal. Section 81 provides in part:

> 81. (1) Where a person claims any property or interest therein, in the possession of a bankrupt at the time of the bankruptcy, he shall file with the trustee a proof of claim verified by affidavit giving the grounds on which the claim is based and sufficient particulars to enable the property to be identified.
>
> (2) The trustee with whom a proof of claim is filed under subsection (1) shall within 15 days after the filing of the claim or within 15 days after the first meeting of creditors, whichever is the later, either admit the claim and deliver possession of the property to the claimant or send notice in the prescribed manner to the claimant that the claim is disputed, with the trustee's reasons for disputing it, and, unless the claimant appeals the trustee'[s] decision to the court within 15 days after the sending of the notice of dispute, the claimant is deemed to have abandoned or relinquished all his or her right to or interest in the property to the trustee who may then sell or dispose of the property free of any right, title or interest of the claimant.

12 On September 9, 2009, pursuant to this section, DSLC filed a property proof of claim with the trustee claiming a property interest in the $310,500 that remained on deposit in Credifinance's bank account. In the proof of claim, DSLC outlined the basic facts relied upon, including the allegation of fraudulent misrepresentations made by Credifinance, and asserted that "the $310,500 are trust funds belonging to DSLC".

  

13 In its notice of dispute of this claim dated September 25, 2009, the Trustee refused to consider the merits of DSLC's fraud allegations and denied DSLC's property claim. In doing so, and among other things, it responded with this: "The allegations of fraudulent misrepresentation made by DSLC, even if they could be established, are incapable at law of elevating DSLC's subordinate unsecured claim to the status of a property claim with priority over the Trustee or other creditors of the bankrupt."

14 DSLC appealed the Trustee's decision and by agreement, the matter was placed on the Commercial List to be heard by a judge of the Superior Court. The procedure to be followed for the hearing was agreed upon by counsel for the parties and reflected in a case conference order. As set out in the order, the parties agreed to file and rely on affidavits and transcripts from the civil proceeding and DSLC would also call *viva voce* evidence. Counsel for the Trustee declined to call witnesses as she expressly intended to rely only on the affidavit and transcript evidence from the civil proceeding.

15 The appeal judge conducted what he called a hearing *de novo* and, as I noted earlier, allowed DSLC's appeal. He awarded DSLC a constructive trust over the $310,500. He made no order as to costs — he held that, given the result of his order on the estate would mean it has "virtually no assets".

***The position of the Trustee***

16 The Trustee's position is that the appeal judge erred in determining DSLC's fraud allegations in the context of an appeal from a disallowance. It says that these issues were not properly before the court. Rather, the issue before the court was whether DSLC could, at law, establish a property claim to the funds in priority to the interests of the Trustee.

17 The Trustee decided that DSLC could not establish a property claim to the funds and that the loan advance was not required to be held in trust. Accordingly, it disallowed DSLC's proof of claim. This was, it argues, based upon well-established legal principles and admissions from DSLC's own representatives that DSLC's interest in the funds was subordinate to the interests of Credifinance's other creditors.

***The position of DSLC***

18 DSLC asserts that the hearing before the appeal judge proceeded as a hybrid trial of an issue. It submits that the procedure adopted for the hearing was agreed to by the parties and was the appropriate means to determine the issues. That is, by agreement of counsel, the Trustee and DSLC each filed and relied on various affidavits and transcript evidence from a related civil proceeding. DSLC also called *viva voce* evidence at the hearing in support of its fraud allegations.

19 The issue for the appeal judge, DSLC argues, was whether DSLC was defrauded into loaning the $400,000 to Credifinance — the appeal judge's finding of fraud is a finding of fact supported by the evidence.

20 I would dismiss the appeal. I conclude that both the process followed by the appeal judge and the issues he decided were, in the circumstances of this case, correct in law. I also conclude that the appeal judge committed no errors in either his decision or his analysis. Finally, I would not grant DSLC leave to appeal the issue of costs. This is not an obvious case where leave should be granted.

**Discussion**

21 The Trustee essentially disputes the factual and jurisdictional basis for the appeal judge's remedy under the statutory regime of the BIA. The essence of the Trustee's appeal to this court, and the answer to it, I believe, is bound up in two questions. First, did the Trustee agree to the process and the issue to be decided? Second, was it within the jurisdiction of the court to proceed in the fashion it did and to decide the issue it did? I find that the answer to both is "yes", and I conclude that the appeal should be dismissed.

***(1) The process***

  

22 By way of brief summary, under the BIA the Chief Justice of the Ontario Superior Court of Justice designates judicial officers who sit as part of Ontario's Bankruptcy Court. Appeals from a decision made by a Trustee in bankruptcy proceedings are most often made to a Registrar of the Ontario Bankruptcy Court. From time to time, however, appeals are heard by judges of the Superior Court.

23 It seems that in Ontario the usual course for appeals under the BIA may be to proceed by way of *viva voce* evidence. This includes appeals under s. 81 of the BIA of a Notice of Dispute of property claims. Occasionally the court permits these appeals to proceed by way of affidavit evidence or partly by way of affidavit evidence and partly by way of *viva voce* evidence: *Katz, Re* (2005), 14 C.B.R. (5th) 193 (Ont. S.C.J.) at paras. 4 and 5.

24 At the very least, the practice seems to be that an appeal court, when considering a Notice of Disallowance, will first decide the issue of whether the matter proceeds as a true appeal or as a hearing *de novo*. The test that has evolved seems to be that a hearing *de novo* will occur if the court decides that to proceed otherwise would result in an injustice to the creditor: *Charlestown Residential School, Re* (2010), 70 C.B.R. (5th) 13 (Ont. S.C.J.) at paras. 1 and 18.

25 I note that this practice is not used uniformly across the country. For example, in British Columbia an appeal under s. 81 of the BIA is not intended to be a trial *de novo* but rather a true appeal: *Galaxy Sports Inc., Re* (2004), 1 C.B.R. (5th) 20 (B.C. C.A.) at para. 40. The policy rationale is that trustees in bankruptcy should be regarded as having experience and expertise in the area of business financing, restructurings and insolvency.

26 This BC approach makes sense because, if evidence that was not before a Trustee were to be presented on an appeal as a matter of course, much of the efficiency in the operation of the bankruptcy scheme would be lost. Creditors who neglected to file a proof of claim in compliance with the requirements of the scheme would be at an advantage because they could expect to enhance their proof on appeal. This, it seems to me, would impact on the objective implicit in the BIA, which is to enable parties to have their rights and claims determined in an expeditious fashion, and add unwanted expense, delay and formality: *Galaxy Sports* at para. 41.

27 However, since counsel before us did not raise the issue of the correctness of this practice, I do not intend to comment on it further. This is not the case that requires this court to consider the merits of the Ontario practice. I would add that the practice appears to have been developed mainly through decisions of Ontario's Bankruptcy Court.

28 The procedure adopted for the hearing of the appeal in this case was agreed to by the parties and was, in their view, the appropriate means to determine the issues. On that there is no dispute. There is, however, a dispute that the Trustee describes as this: the Trustee did not seek a trial of DSLC's fraud allegations against Benarroch, nor was it the Trustee's understanding that such allegations were supposed to have been tried before the appeal judge.

29 There is no doubt that DSLC's appeal of the Trustee's Notice of Dispute was focused entirely on its allegation of fraud. That was the very issue it sought to have decided by the appeal judge. At para. 2 of his reasons, the appeal judge describes DSLC's position on the appeal this way:

> [T]hat it is the victim of a fraud at the hands of Georges Benarroch and that, as a result of that fraud, it loaned $400,000 to Credifinance Securities Limited. According to DSLC Capital Corp., the $310,500 is directly traceable to that $400,000 loan and, therefore, should be impressed with a constructive trust in favour of DSLC Capital Corp.

30 It was DSLC's appeal. It framed the issue to be heard by the appeal judge, and all parties agreed to the process to be followed. While the Trustee may have disagreed with what issue was to be decided, the appeal judge was required to address the issue put forward by DSLC. I fail to see where he committed any error in doing so. There is no merit to this submission.

***(2) The fraud issue***

31 Before the appeal judge, counsel for the Trustee — who is also counsel on this appeal — took two positions that demonstrate that the Trustee was fully engaged in the issue of fraud that she now asserts the appeal judge had no jurisdiction to

  

decide. First, she argued that, even if there was a fraudulent misrepresentation, it would not allow DSLC to bypass the BIA. Her view was — as it continues to be — that in bankruptcy proceedings, there is no special status accorded to a victim of a fraud.

32 Second, she fairly conceded — again as she does here — that constructive trust principles can be applied in bankruptcy proceedings, however, those principles are applied only in the most extraordinary cases. She relies on *Ascent Ltd., Re* (2006), 18 C.B.R. (5th) 269 (Ont. S.C.J.) as illustrating such a case. Indeed, in her oral submissions, counsel conceded that a trustee could, albeit in extraordinary circumstances, find a *de facto* constructive trust by allowing the property claim, or otherwise refer the issue for a hearing before a Bankruptcy Registrar or judge of the Superior Court.

33 There is no question that the remedy of constructive trust is expressly recognized in bankruptcy proceedings. Both the case law and authors of texts make this clear, although the test for proving the existence of a constructive trust in a bankruptcy setting is high: L.W. Houlden & Geoffrey Morawetz, *Houlden and Morawetz Bankruptcy and Insolvency Analysis* (Toronto: WL Can, 2011) at F§5(1). The authors add this at F§5(8): "A constructive trust will ordinarily be imposed on property in the hands of a wrongdoer to prevent him or her from being unjustly enriched by profiting from his or her wrongful conduct" (citations omitted).

34 *Ascent*, a case decided by an Ontario Registrar in Bankruptcy, is a case that demonstrates the type of circumstances that can make a case extraordinary. I found this case to be very instructive.

35 The Registrar in *Ascent* held that in its role as the arbiter of commercial morality, the Bankruptcy Court can rely on equitable principles, "even at the expense of the formulaic aspects of the BIA scheme of distribution": para. 17.

36 An example of commercial immorality is described in *Ascent* as being where a bankrupt and its creditors benefit from misconduct by the bankrupt which was the basis upon which the property was obtained. The Registrar held that to permit an estate to retain the property in such circumstances amounts to an unjust enrichment, and the court can impose a constructive trust on an estate's assets to remedy the injustice. Furthermore, "it matters not which assets are consumed to remedy this": para. 18.

37 Thus, a constructive trust in bankruptcy proceedings can be ordered to remedy an injustice; for example, where permitting the creditors access to the bankrupt's property would result in them being unjustly enriched. The prerequisite is that the bankrupt obtained the property through misconduct. The added necessary feature is that it would be unjust to permit the bankrupt and creditors to benefit from the misconduct.

38 A Trustee in bankruptcy is an officer of the court and must act in an equitable manner. Enriching creditors with a windfall and depriving another of its interest in property, has been held to be an offence to natural justice. As Karakatsanis J. (as she then was) held at para. 14 in *Elez, Re* (2010), 54 E.T.R. (3d) 31 (Ont. S.C.J.), "The court will not allow the trustee, as an officer of the court, to stand on his legal rights if to do so would offend natural justice" (citations omitted).

39 Some of the relevant findings of the appeal judge, which demonstrate why this case is somewhat exceptional, bear repeating:

> [23] I am also satisfied, on a balance of probabilities, that, but for the deceit, Mr. Lorenzo [the director of DSLC who negotiated with Benarroch] would not have entered into any agreement concerning Credifinance Securities Limited, would not have lent Credifinance Securities Limited $400,000, and Credifinance would not have $310,500 in its bank account.
>
> [24] At present, it appears that Georges Benarroch and a company he controls, Credifinance Capital Corp., have filed secured claims in the bankruptcy of Credifinance Securities Limited. It appears that the other creditors are lawyers who acted for Credifinance Securities Limited in the litigation against DSLC Capital Corp and its attempts to recover the $400,000 and in the IDA [Investment Dealers Association] investigations. In this regard, it is also a fact that Georges Benarroch, through his company, Donabo Inc., has guaranteed the fees of the Trustee.

40 Thus, as the appeal judge found, DSLC was the victim of a fraud perpetrated by Credifinance and Benarroch. Importantly, the only creditors of Credifinance impacted by the appeal judge's order are Benarroch and his lawyers. Enriching Benarroch, therefore, with a windfall and depriving DSLC of its interest in the $310,500 would be fundamentally unjust.

  

41 The constructive trust granted by the appeal judge was just in the circumstances of this case and did not unjustly deprive creditors of their rights under the BIA. In the words of the appeal judge at para. 34, "those funds should be the subject of a constructive trust in favor of DSLC Capital Corp. in order to prevent the unjust enrichment of Credifinance Securities Limited."

42 It was within the appeal judge's jurisdiction to grant the remedy he did. Furthermore, there was ample evidence upon which the appeal judge could rely to make the findings he did, and they are reasonable and entitled to deference from this court. I would, therefore, reject this argument.

43 Before leaving this issue, I believe it is important to make a final observation. The appeal judge's reasons should not be interpreted to suggest that once a civil fraud by the bankrupt on the claimant, whose claim was disallowed by the trustee, is proven, and that is coupled with a loss and an ability to trace the consequences of the fraud, then a constructive trust will always be imposed. That, in my view, is too broad.

44 Constructive trust is a discretionary remedy. In a bankruptcy there are other interests to consider besides those of the defrauder and the defraudee: there are other creditors. Thus, the exercise of remedial discretion must be informed by additional considerations than in a civil fraud trial. The appeal judge in our case clearly understood this, considered the claims of the creditors, found them to be tainted by Benarroch's misconduct, and concluded that a rigid formulaic approach, relying strictly on the letter of the BIA would produce an unjust result.

**The Cross-Appeal**

45 The appeal judge's decision on costs is explained in full in his reasons at para. 35: "Having regard to the fact that the effect of my ruling means that the Estate of Credifinance Securities Limited has virtually no assets, there will be no order concerning costs." DSLC in its cross-appeal asserts that this was an error and the appeal judge's decision is not entitled to deference. I disagree.

46 The general rule in these types of proceedings is found in the provisions of the BIA. Section 197(1) provides that the costs of and incidental to any proceedings in court under the BIA are in the discretion of the court. Section 197(3) provides that where an action or proceeding is brought by or against a trustee, or where a trustee is made a party to any action or proceeding, he is not personally liable for costs unless the court otherwise directs.

47 As this court held in *McNaughton Automotive Ltd. v. Co-operators General Insurance Co.* (2008), 95 O.R. (3d) 365 (Ont. C.A.) at paras. 23-26, leave to appeal a costs decision is granted sparingly and only in obvious cases. This is because decisions as to costs are highly discretionary and are accorded a very high degree of deference. Generally, they will only be interfered with where it can be demonstrated that the decision maker is plainly wrong or has made an error in principle.

48 While trustees in bankruptcy are not exempt from liability for costs, the jurisprudence in the field suggests that they will only be liable in limited circumstances: see *Farm Mutual Financial Services Inc., Re* (2010), 66 C.B.R. (5th) 85 (Ont. S.C.J. [Commercial List]). I fail to see any such limited circumstances in this case. DSLC has not met its heavy burden and has not satisfied me that this is an obvious case.

49 Accordingly, I would deny DSLC leave to appeal the award of costs.

**Disposition**

50 For the reasons herein I would dismiss the Trustee's appeal. I would deny DSLC leave to appeal the costs order of the appeal judge.

51 Although DSLC was unsuccessful on its cross-appeal, it was wholly successful in the main appeal. After factoring this into my analysis, I would award DSLC its costs in this court fixed in the amount of $20,000, inclusive of disbursements and taxes, paid from the estate.

  

***S.T. Goudge J.A.*:**

I agree

***Robert Sharpe J.A.*:**

I agree

*Appeals dismissed.*

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# Foskett v. McKeown and Others [2000] UKHL 29; [2000] 3 All ER 97 (18th May, 2000)

**HOUSE OF LORDS**

Lord Browne-Wilkinson Lord Steyn Lord Hoffmann Lord Hope of Craighead Lord Millett

**OPINIONS OF THE LORDS OF APPEAL FOR JUDGMENT IN THE CAUSE**

*FOSKETT*
*(SUING ON HIS OWN BEHALF AND ON BEHALF OF ALL OTHER PURCHASERS OF PLOTS OF LAND AT MOUNT EDEN, HERRADODO CERRO ALTO DIOGO, MARTINS, ALGARVE, PORTUGAL)*
*(ORIGINAL APPELLANT AND CROSS-RESPONDENT)*

*v.*

*MCKEOWN*
*(ORIGINAL RESPONDENT) AND OTHERS (A.P.)*
*(ORIGINAL RESPONDENTS AND CROSS-APPELLANTS)*

***ON 18 MAY 2000***

**LORD BROWNE-WILKINSON**

My Lords,

There are many cases in which the court has to decide which of two innocent parties is to suffer from the activities of a fraudster. This case, unusually, raises the converse question: which of two innocent parties is to benefit from the activities of the fraudster. In my judgment, in the context of this case the two types of case fall to be decided on exactly the same principles, viz. by determining who enjoys the ownership of the property in which the loss or the unexpected benefit is reflected.

On 6 November 1986, Mr. Murphy effected a whole-life policy ("the policy") with Barclays Life Assurance Co. Ltd. ("the insurers") in the sum of £1m. at an annual premium of £10,220. The policy (which was issued on 27 January 1987) provided that on the death of Mr. Murphy a specified death benefit became payable, such benefit

being the greater of (1) the sum assured (£1m.) and (2) the aggregate value of units notionally allocated under the terms of the policy to the policy at their bid price on the day of the receipt by the Insurers of a written notice of death. The policy stated that "in consideration of the first premium already paid and of the further premiums payable and subject to the conditions of this policy the company will on the death of the life assured pay to the policy holder or his successors in title ("the policy holder") the benefits specified."

Although primarily a whole-life policy assuring the sum assured of £1m., the policy had an additional feature, viz. a notional investment content which served three purposes. First, it determined the surrender value of the policy. Second, it determined the alternative calculation of the death benefit if the value of the notionally allocated units exceeded the sum assured of £1m. Third, the investment element was used to pay for the cost of life cover after the payment of the second premium in November 1987. By condition 4 of the policy, units were notionally allocated to the policy upon receipt of the second and all subsequent premiums. By condition 6 of the policy, upon receipt of each premium resulting in the notional allocation of units under condition 4, the Insurers cancelled sufficient units to meet the cost of life cover for the next year. Condition 10 provided for conversion of the policy into a paid-up policy: units would thereafter continue to be cancelled under condition 6 so long as there were units available for that purpose. As soon as there were no units available, no death benefit or surrender value was to be available under the policy. Sir Richard Scott V.-C., [1998] Ch. 265, 275, summarised the position as follows:

> ". . . if a premium is not paid, then (provided at least two years' premiums have been paid) the policy is converted into a paid-up policy and units that have been allocated to the policy are applied annually in meeting the cost of life insurance until all the allocated units have been used up. Only at that point will the policy lapse."

Five premiums were paid, in November 1986, 1987, 1988, 1989 and 1990. The 1986 and 1987 premiums were paid by Mr. Murphy out of his own resources. The 1989 and 1990 premiums were paid out of moneys misappropriated by Mr. Murphy from the plaintiffs. The source of the 1988 premium is disputed: unconditional leave to defend on issues relating to this premium has been granted.

The policy was directed to be held on trusts. On 15 March 1989 the policy was irrevocably appointed to be held in trust for Mr. Murphy absolutely. On 16 March 1989 he settled the policy on trust for his wife and his mother but subject to a power for him to appoint to members of a class which included his wife, his mother and his children but which excluded Mr. Murphy himself. By a deed of appointment dated 1 December 1989 Mr. Murphy appointed the policy and all moneys payable thereunder upon trust (in the events which happened) as to one-tenth for Mrs. Brigette Murphy and as to nine-tenths for his three children equally.

I turn then to consider the source of the moneys which constituted the fourth and fifth premiums. In 1988 Mr. Murphy, together with an associate of his, Mr. Deasy, acquired control of an English company which itself owned and controlled a Portuguese company. Those two companies between them marketed plots of land forming part of a site in the Algarve in Portugal to be developed and sold by them to purchasers. Each prospective purchaser entered into a contract with one of the companies for the purchase of his plot. The contract required each purchaser to pay the purchase price to Mr. Deasy, to be held by him upon the trusts of a trust deed ("the Purchasers trust deed") under which the purchasers' money was to be held in a separate bank account until either the plot of land was transferred to him or a period of two years had expired, whichever first happened. If after two years the plot had not been transferred to the purchaser the money was to be repaid with interest. Some 220 prospective purchasers entered into transactions to acquire plots on the building estate and paid some £2,645,000 to Mr. Deasy to be held by him on the terms of the purchasers trust deed. However, the land in Portugal was never developed. When the time came for the money to be refunded to the purchasers it was found that it had been dissipated and that £20,440 of those funds had been used to pay the fourth and fifth premiums due under the policy.

Mr. Murphy committed suicide on 9 March 1991. On 6 June 1991 the insurers paid £1,000,580-04 to the two surviving trustees of the policy. Mrs. Murphy has been paid her one-tenth share. The dispute, for the rest, lies between Mr. Murphy's three children (as beneficiaries under the policy trust) and the purchasers of the plots in Portugal, from whose money £20,440 has been applied in breach of the trusts of the purchasers trust deed in paying the fourth and fifth premiums. The purchasers allege that, at a minimum, 40 per cent. of the premiums on the policy have been paid out of their moneys and that having traced their moneys through the policy into the policy moneys,

they are entitled to 40 per cent. of the policy moneys. On the other side, the children contend that the purchasers are not entitled to any interest at all or at most only to the return of the sum misappropriated to pay the premiums, viz. £20,440 plus interest. The Court of Appeal, by a majority (Sir Richard Scott V.-C. and Hobhouse L.J., Morritt L.J. dissenting) [1998] Ch. 265, held that the purchasers were entitled to be repaid the amount of the fourth and fifth premiums together with interest but were not entitled to a pro-rata share of the policy proceeds.

The purchasers appeal to your Lordships claiming that the policy moneys are held in trust for the children and themselves pro rata according to their respective contributions to the premiums paid out of the purchasers' moneys on the one hand and Mr. Murphy personally on the other, i.e. they claim that a minimum of 40 per cent. (being two out of the five premiums) is held in trust for the purchasers. The children, on the other hand, seek to uphold the decision of the majority of the Court of Appeal and, by cross-appeal, go further so as to claim that the purchasers are entitled to no rights in the policy moneys.

As to the cross-appeal, I have read in draft the speech of my noble and learned friend Lord Hope of Craighead. For the reasons which he gives I would dismiss the cross-appeal.

As to the appeal, at the conclusion of the hearing I considered that the majority of the Court of Appeal were correct and would have dismissed the appeal. However, having read the draft speech of Lord Millett I have changed my mind and for the reasons which he gives I would allow the appeal. But, as we are differing from the majority of the Court of Appeal I will say a word or two about the substance of the case and then deal with one minor matter on which I do not agree with my noble and learned friend Lord Millett.

The crucial factor in this case is to appreciate that the purchasers are claiming a proprietary interest in the policy moneys and that such proprietary interest is not dependent on any discretion vested in the court. Nor is the purchasers claim based on unjust enrichment. It is based on the assertion by the purchasers of their equitable proprietary interest in identified property.

The first step is to identify the interest of the purchasers: it is their absolute equitable interest in the moneys originally held by Mr. Deasly on the express trusts of the purchasers trust deed. This case does not involve any question of resulting or constructive trusts. The only trusts at issue are the express trusts of the purchasers trust deed. Under those express trusts the purchasers were entitled to equitable interests in the original moneys paid to Mr. Deasy by the purchasers. Like any other equitable proprietary interest, those equitable proprietary interests under the purchasers trust deed which originally existed in the moneys paid to Mr. Deasy now exist in any other property which, in law, now represents the original trust assets. Those equitable interests under the purchasers trust deed are also enforceable against whoever for the time being holds those assets other than someone who is a bona fide purchaser for value of the legal interest without notice or a person who claims through such a purchaser. No question of a bona fide purchaser arises in the present case: the children are mere volunteers under the policy Trust. Therefore the critical question is whether the assets now subject to the express trusts of the purchasers trust deed comprise any part of the policy moneys, a question which depends on the rules of tracing. If, as a result of tracing, it can be said that certain of the policy moneys are what now represent part of the assets subject to the trusts of the purchasers trust deed, then as a matter of English property law the purchasers have an absolute interest in such moneys. There is no discretion vested in the court. There is no room for any consideration whether, in the circumstances of this particular case, it is in a moral sense "equitable" for the purchasers to be so entitled. The rules establishing equitable proprietary interests and their enforceability against certain parties have been developed over the centuries and are an integral part of the property law of England. It is a fundamental error to think that, because certain property rights are equitable rather than legal, such rights are in some way discretionary. This case does not depend on whether it is fair, just and reasonable to give the purchasers an interest as a result of which the court in its discretion provides a remedy. It is a case of hard-nosed property rights.

Can then the sums improperly used from the purchaser's moneys be traced into the policy moneys? Tracing is a process whereby assets are identified. I do not now want to enter into the dispute whether the legal and equitable rules of tracing are the same or differ. The question does not arise in this case. The question of tracing which does arise is whether the rules of tracing are those regulating tracing through a mixed fund or those regulating the position when moneys of one person have been innocently expended on the property of another. In the former case (mixing of funds) it is established law that the mixed fund belongs proportionately to those whose moneys were

mixed. In the latter case it is equally clear that money expended on maintaining or improving the property of another normally gives rise, at the most, to a proprietary lien to recover the moneys so expended. In certain cases the rules of tracing in such a case may give rise to no proprietary interest at all if to give such interest would be unfair: see *In Re Diplock* [1948] Ch. 465, 548.

Both the Vice-Chancellor and Hobhouse L.J. considered that the payment of a premium on someone else's policy was more akin to an improvement to land than to the mixing of separate trust moneys in one account. Hobhouse L.J. was additionally influenced by the fact that the payment of the fourth and fifth premiums out of the purchasers' moneys conferred no benefit on the children: the policy was theirs and, since the first two premiums had already been paid, the policy would not have lapsed even if the fourth and fifth premiums had not been paid.

Cases where the money of one person has been expended on improving or maintaining the physical property of another raise special problems. The property left at the end of the day is incapable of being physically divided into its separate constituent assets, i.e. the land and the money spent on it. Nor can the rules for tracing moneys through a mixed fund apply: the essence of tracing through a mixed fund is the ability to re-divide the mixed fund into its constituent parts pro rata according to the value of the contributions made to it. The question which arises in this case is whether, for tracing purposes, the payments of the fourth and fifth premiums on a policy which, up to that date, had been the sole property of the children for tracing purposes fall to be treated as analogous to the expenditure of cash on the physical property of another or as analogous to the mixture of moneys in a bank account. If the former analogy is to be preferred, the maximum amount recoverable by the purchasers will be the amount of the fourth and fifth premiums plus interest: if the latter analogy is preferred the children and the other purchasers will share the policy moneys pro rata.

The speech of my noble and learned friend Lord Millett demonstrates why the analogy with moneys mixed in an account is the correct one. Where a trustee in breach of trust mixes money in his own bank account with trust moneys, the moneys in the account belong to the trustee personally and to the beneficiaries under the trust rateably according to the amounts respectively provided. On a proper analysis, there are "no moneys in the account" in the sense of physical cash. Immediately before the improper mixture, the trustee had a chose in action being his right against the bank to demand a payment of the credit balance on his account. Immediately after the mixture, the trustee had the same chose in action (i.e. the right of action against the bank) but its value reflected in part the amount of the beneficiaries' moneys wrongly paid in. There is no doubt that in such a case of moneys mixed in a bank account the credit balance on the account belongs to the trustee and the beneficiaries rateably according to their respective contributions.

So in the present case. Immediately before the payment of the fourth premium, the trust property held in trust for the children was a chose in action i.e. the bundle of rights enforceable under the policy against the insurers. The trustee, by paying the fourth premium out of the moneys subject to the purchasers trust deed, wrongly mixed the value of the premium with the value of the policy. Thereafter, the trustee for the children held the same chose in action (i.e. the policy) but it reflected the value of both contributions. The case, therefore, is wholly analogous to that where moneys are mixed in a bank account. It follows that, in my judgment, both the policy and the policy moneys belong to the children and the trust fund subject to the purchasers trust deed rateably according to their respective contributions to the premiums paid.

The contrary view appears to be based primarily on the ground that to give the purchasers a rateable share of the policy moneys is not to reverse an unjust enrichment but to give the purchasers a wholly unwarranted windfall. I do not myself quibble at the description of it being "a windfall" on the facts of this case. But this windfall is enjoyed because of the rights which the purchasers enjoy under the law of property. A man under whose land oil is discovered enjoys a very valuable windfall but no one suggests that he, as owner of the property, is not entitled to the windfall which goes with his property right. We are not dealing with a claim in unjust enrichment.

Moreover the argument based on windfall can be, and is, much over-stated. It is said that the fourth and fifth premiums paid out of the purchasers' moneys did not increase the value of the policy in any way: the first and second premiums were, by themselves, sufficient under the unusual terms of the policy to pay all the premiums falling due without any assistance from the fourth and fifth premiums: even if the fourth and fifth premiums had not been paid the policy would have been in force at the time of Mr. Murphy's death. Therefore, it is asked, what value

has been derived from the fourth and fifth premiums which can justify giving the purchasers a pro rata share. In my judgment this argument does not reflect the true position. It is true that, *in the events which have happened*, the fourth and fifth premiums were not required to keep the policy on foot until the death of Mr. Murphy. But at the times the fourth and fifth premiums were paid (which must be the dates at which the beneficial interests in the policy were established) it was wholly uncertain what the future would bring. What if Mr. Murphy had not died when he did? Say he had survived for another five years? The premiums paid in the fourth and fifth years would in those events have been directly responsible for keeping the policy in force until his death since the first and second premiums would long since have been exhausted in keeping the policy on foot. In those circumstances, would it be said that the purchasers were entitled to 100 per cent. of the policy moneys? In my judgment, the beneficial ownership of the policy, and therefore the policy moneys, cannot depend upon how events turn out. The rights of the parties in the policy, one way or another, were fixed when the relevant premiums were paid when the future was unknown.

For these reasons and the much fuller reasons given by Lord Millett, I would allow the appeal and declare that the policy moneys were held in trust for the children and the purchasers in proportion to the contributions which they respectively made to the five premiums paid.

There is one small point on which my noble and learned friends Lord Millett and Lord Hoffmann disagree, namely, whether the pro rata division should take account of the notional allocation of units to the policy and to the fact that contributions were made at different times, i.e. when the various premiums were paid. I agree that, for the reasons given by Lord Hoffmann, it is not necessary to complicate the calculation of the pro rata shares by taking account of these factors and would therefore simply divide the policy moneys pro rata according to the contributions made to the payment of the premiums.

**LORD STEYN**

My Lords,

This is a dispute between two groups of innocent parties about the rights to a death benefit of about £1m. paid by insurers pursuant to a whole life policy. The first group are individuals who contracted between June 1989 and January 1991 to purchase plots of land in Portugal which were intended to be developed as an estate with villas and a golf and country club. Mr. Timothy Murphy was the dominant figure behind the development project. He obtained over £2.6m. from the purchasers. With effect from November 1987 he took out a whole life policy at an annual premium of £10,200. The policy had an investment content, which served various purposes. It determined the surrender value of the policy. It determined the alternative calculation of the death benefit if the value of notionally allocated units exceeded the sum assured (i.e. £1m.) The investment element was to be used to pay for the cost of life cover after the payment of the second premium. Mr. Murphy used his own money to pay the premiums for 1986 and 1987. The value of the units allocated to the policy after the payment of the 1987 premium was more than enough to pay for the life element in the next three years. Mr. Murphy in fact paid the premium for 1988. It is still unclear where he got the money from. But he undoubtedly paid the premiums for 1989 and 1990 with money stolen from the purchasers. On 9 March 1991 Mr. Murphy committed suicide. On 6 June 1991 the insurers paid a sum of about £1 million as a death benefit under the policy. The children are express beneficiaries of the trusts of the policy. The purchasers claimed a proportionate part of the policy moneys. The issue concerns the respective rights of the purchasers and the children to the policy moneys. By a majority the Court of Appeal reversed the trial judge's decision in favour of the purchasers and decided that the purchasers are only entitled to recover the money stolen from them and used to pay the 1989 and 1990 premiums together with interest: *Foskett v. McKeown* [1998] Ch. 265. On appeal to the House of Lords the primary case of the purchasers was that they are entitled to share in the policy moneys in the same proportion as the amount of the premiums paid out of the purchasers' moneys bear to the total amount of the premiums paid i.e. a two-fifths share. I will explain my reasons for concluding that the purchasers have no rights to the policy moneys. There is, however, an anterior point. On the appeal to the House of Lords counsel for the children argued that by resorting to other remedies the purchasers made a binding election which preclude them from advancing their present claim. In my view there was in truth no inconsistency between the remedies to which the purchasers resorted.

The purchasers put forward a proprietary claim. They allege that they are equitable co-owners in the policy moneys: specifically their claim is that they are entitled to 40 per cent. and the children to 60 per cent. of the policy moneys. The purchasers point out that they can trace the stolen money (£20,440) through various bank accounts into payments in respect of the 1989 and 1990 premiums. Given that a total of five premiums were paid the purchasers assert that they are entitled to equitable proprietary rights to 40 per cent. of the sum assured. The purchasers argued that the proceeds of the policy were purchased out of a common fund to which the purchasers and the children contributed and that on equitable principles the purchasers are entitled to a proportionate part of the proceeds. Counsel for the purchasers observed in his printed case that it is not an area of the law where the House is constrained by previous authority. Accordingly, he argued, wider considerations of policy must be taken into account.

There are four considerations which materially affect my approach to the claim of the purchasers. First the relative moral claims of the purchasers and the children must be considered. The purchasers emphasise that their claim is the result of the deliberate wrongdoing of Mr. Murphy. This is a point in favour of the purchasers. Moreover the case for the children is not assisted by the fact that Mr. Murphy sought to make provision for his family. The legal question would be the same if the beneficiary under the express trust was a business associate of Mr. Murphy. On the other hand, it is an important fact that the children were wholly unaware of any wrongdoing by their father. Secondly, it is clear that in the event the premiums paid in 1989 and 1990 added nothing of value to the policy. The policy was established and the children acquired vested interests (subject to defeasance) before Mr. Murphy pursuant to the rights acquired by the children before 1989. The entitlement of the children was not in any way improved by payment of the 1989 and 1990 premiums. Thirdly, the purchasers have no claim in unjust enrichment in a substantive sense against the children because the payment of the 1989 and 1990 premiums conferred no additional benefit on the children. They were not enriched by the payment of those premiums: they merely received their shares of the sum assured in accordance with their pre-existing entitlement. The fourth point is that the children, as wholly innocent parties, can cogently say that, if they had become aware that Mr. Murphy planned to use trust money to pay the fourth and fifth premiums, they would have insisted that he did not so pay those premiums, with the result that they would still have received the same death benefit. (The relvance of such a factor is helpfully explained by *Professor Hayton*, "*Equity's Identification Rules,*" Chapter 1 in *P. Birks* (ed) *Laundering and Tracing* (Oxford, 1995), p. 11-12 and *Charles Mitchell*, *Tracing Trust Funds Into Insurance Proceeds*, [1997] L.M.C.L.Q. 465, 472.)

In arguing the merits of the proprietary claim counsel for the purchasers from time to time invoked "the rules of tracing." By that expression he was placing reliance on a *corpus* of supposed rules of law, divided into common law and equitable rules. In truth tracing is a process of identifying assets: it belongs to the realm of evidence. It tells us nothing about legal or equitable rights to the assets traced. In a crystalline analysis *Professor Birks* (*The Necessity of a Unitary Law of Tracing, essay in Making Commercial Law, Essays in Honour of Roy Goode,* (1997), pp. 239-258) explained that there is a unified regime for tracing and that "it allows tracing to be cleanly separated from the business of asserting rights in or in relation to assets successfully traced": at p. 257. Applying this reasoning Professor Birks concludes at p. 258:

> ". . . that the modern law is equipped with various means of coping with the evidential difficulties which a tracing exercise is bound to encounter. The process of identification thus ceases to be either legal or equitable and becomes, as is fitting, genuinely neutral as to the rights exigible in respect of the assets into which the value in question is traced. The tracing exercise once successfully completed, it can then be asked what rights, if any, the plaintiff can, on his particular facts, assert. It is at that point that it become relevant to recall that on some facts those rights will be personal, on others proprietary, on some legal, and on others equitable."

I regard this explanation as correct. It is consistent with orthodox principle. It clarifies the correct approach to so-called tracing claims. It explains what tracing is about without providing answers to controversies about legal or equitable rights to assets so traced.

There is no difficulty in tracing the stolen moneys. Moreover, it is self-evident that there must be a right to recover the moneys stolen and used for the payment of the 1989 and 1990 premiums. Equity's method of achieving the necessary result is to impose a lien or charge over the stolen money. The formal assertion to the contrary on behalf of the children, which is the subject of a cross appeal, is without substance. The question is whether the

purchasers have equitable proprietary rights to the sum assured which was paid in terms of the policy. This brings me back to the distinctive feature of the case, namely that the fourth and fifth premiums did not contribute or add to the sum received by the children. Sir Richard Scott, V.-C., observed, [1998] Ch. 265, 282:

> ". . . If a trustee used trust money to improve or maintain his house, the beneficiaries would, in my view, be entitled to a charge on the house to recover their money. But unless it appeared that the improvements had increased the value of the house there would be no basis for a claim to a pro rata share in the house and no reason for the imposition of a constructive trust. There would, in such a case, be no benefit acquired by the use of the trust money for which the trustee would be accountable. Similar reasoning applies, in my opinion, in the present case. . . . They did not, in my opinion, become entitled to a pro rata share in the policy either via a constructive trust route or via a resulting trust route."

On this point Hobhouse L.J. (now Lord Hobhouse of Woodborough) apparently took a similar view: at p. 291E-F. I am in respectful agreement with this reasoning of the majority on this aspect. The Vice-Chancellor and Hobhouse L.J. further concluded that the misapplied trust funds were not used to acquire the policy, or the death benefit of £1m. nor any share in either. On appeal to the House counsel for the purchasers while not formally conceding anything observed that the improvement argument is "a wholly unrealistic argument." He argued that the proceeds of the policy were purchased out of a common fund to which both the purchasers and the children had contributed. This was the primary issue on the appeal to the House.

The argument of the purchasers is supported by the carefully reasoned dissenting judgment of Morritt L.J. He relied on the analogies of the cases where (1) an asset is bought with a mixed fund composed of trust money and the trustees own money, and is then passed to an innocent volunteer, and (2) a trustee mixes money from one trust with that of another, and uses the mixed fund to purchase an asset. Morritt L.J. pointed to longstanding authorities to the effect that in such situations beneficiaries may be entitled to a pro rata share of the purchased asset: at p. 301G-302B. But it is clear that this reasoning of Morritt L.J. is critically dependent on the relative closeness of the two analogies. On balance I have been persuaded that the analogies cited by Morritt L.J., and strongly relied on by counsel for the purchasers, are not helpful in the circumstances of the present case.

There is in principle no difficulty about allowing a proprietary claim in respect of the proceeds of an insurance policy. If in the circumstances of the present case the stolen moneys had been wholly or partly causative of the production of the death benefit received by the children there would have been no obstacle to admitting such a proprietary claim. But those are not the material facts of the case. I am not influenced by hindsight. The fact is that the rights of the children had crystallised by 1989 before any money was stolen and used to pay the 1989 and 1990 premiums. Indeed Morritt L.J. expressly accepts that "in the event, the policy moneys would have been the same if the later premiums had not been paid:" at p. 302F. Counsel for the purchasers accepted that as a matter of primary fact this was a correct statement. But he argued that there was nevertheless a causal link between the premiums paid with stolen moneys and the death benefit. I cannot accept this argument. It would be artificial to say that all five premiums produced the policy moneys. The purchasers' money did not "buy" any part of the death benefit. On the contrary, the stolen moneys were not causally relevant to any benefit received by the children. The 1989 and 1990 premiums did not contribute to a mixed fund in which the purchasers have an equitable interest entitling them to a rateable division. It would be an innovation to create a proprietary remedy in respect of an asset (the death benefit) which had already been acquired at the date of the use of the stolen moneys. Far from assisting the case of the purchasers the impact of wider considerations of policy in truth tend to undermine the case of the purchasers. One needs to consider the implication of a holding in favour of the purchasers in other cases. Suppose Mr. Murphy had surrendered the policy before going bankrupt. Assume Mr. Murphy had partly used his own money and partly used money stolen from the purchasers to pay premiums. The hypothesis is that the stolen money did not in any way increase the surrender value of the policy. Justice does not support the creation to the prejudice of trade creditors of a new proprietary right in the surrender value of the policy: compare *Roy Goode, Proprietary Restitutionary Claims, essay in Restitution: Past Present and Future,* ed. Cornish, Nolan, O'Sullivan, and Virgo, p. 63 et seq. For these reasons I differ from the analysis of Morritt L.J. and reject the argument of the purchasers.

There is one final matter of significance. In a critical final passage in his judgment Morritt L.J. observed, at p. 303A:

". . . In my view . . . common justice requires that the purchasers should have the right to participate in that which has followed from the use of their money together with the other moneys, taking their share out of that joint and common stock."

The purchasers do not assert that they suffered any loss. They cannot assert that the children would be unjustly enriched if the purchasers' claim fails. In these circumstances my perception of the justice of the case is different from that of Morritt L.J. If justice demanded the recognition of such a proprietary right to the policy moneys, I would have been prepared to embark on such a development. Given that the moneys stolen from the purchasers did not contribute or add to what the children received, in accordance with their rights established before the theft by Mr. Murphy, the proprietary claim of the purchasers is not in my view underpinned by any considerations of fairness or justice. And, if this view is correct, there is no justification for creating by analogy with cases on equitable interests in mixed funds a new proprietary right to the policy moneys in the special circumstances of the present case.

My Lords, for these reasons, as well as the reasons given by Lord Hope of Craighead, I would dismiss both the appeal by the purchasers (the appellants) and the cross appeal by the children (the cross appellants.)

**LORD HOFFMANN**

My Lords,

I have had the advantage of reading in draft the speech of my noble and learned friend Lord Millett. I agree with him that this is a straightforward case of mixed substitution (what the Roman lawyers, if they had had an economy which required tracing through bank accounts, would have called confusio). I agree with his conclusion that Mr. Murphy's children, claiming through him, and the trust beneficiaries whose money he used, are entitled to share in the proceeds of the insurance policy in proportion to the value which they respectively contributed to the policy. This is not based upon unjust enrichment except in the most trivial sense of that expression. It is, as my noble and learned friend says, a vindication of proprietary right.

The only point on which I differ from my noble and learned friend is the calculation of the proportions. The policy was a complicated chose in action which contained formulae for the calculation of different amounts which would become payable on different contingencies. One such formula (which, in the event, was irrelevant to the calculation of the amount payable) was by reference to notional units in a notional fund of notional investments. My noble and learned friend considers that these units should be treated as if they were real and that they formed separate property which some part of each premium had been used to buy. In my opinion, that overcomplicates the matter. The units were merely part of the formula for calculating what would be payable. They cannot be regarded as separate property or even some kind of internal currency. It would not in my view have mattered whether the formula for calculating the amount payable had been by reference to the movements of the heavenly bodies. The policy was a single chose in action under which some amount would fall due for payment in consideration of the premiums which had been paid. Immediately before Mr. Murphy's suicide, it was owned by the children and the beneficiaries in proportion to the value of their contributions to that consideration. The fact that the contingency which made the money payable was the death of Mr. Murphy cannot affect the proprietary interests in the chose in action and therefore in its proceeds: see *D'Avigdor-Goldsmid v. Inland Revenue Commissioners* [1953] A.C. 347. In the case of contributions which are made at different times to the consideration for a single item of property such as the chose in action in this case, I can see an argument for saying that the value of earlier payments is greater than that of later payments. A pound today is worth more than the promise of a pound in a year's time. So there may be a case for applying some discount according to the date of payment. But no such argument was advanced in this case and I do not think that your Lordships should impose it upon the parties. I therefore agree with Morritt L.J. that the fund should be held simply in proportion to the contributions which the parties made to the five premiums.

**LORD HOPE OF CRAIGHEAD**

My Lords,

This is a competition between two groups of persons who claim to be entitled to participate in the same fund. The fund consists of the death benefit paid by the insurers under a policy of life assurance to the trustees of the policy following the death of the life assured, Timothy Murphy, by suicide. The amount of the death benefit was £1m., to which a small sum was added as interest from the date of the death until payment. At the date of death the policy was held in trust for the children of the life assured and for his mother, who is also now deceased. The mother's share of the sum paid under the policy was distributed to her before her death. The trustees have made certain payments from the balance of that sum for the maintenance of the children. The remainder has been retained and invested by them, and it is that sum which forms the amount now in dispute. The third, fourth and fifth respondents, who are the children of the life assured, claim to be entitled to payment of the whole of that amount as the remaining beneficiaries under the trusts of the policy.

There would have been no answer to the claim by the children had it not been for the fact that the last two of five annual premiums (and possibly a portion of the previous year's premium - the facts have yet to be established by evidence) were paid by the life assured out of money which, dishonestly and in breach of trust, he had misappropriated. The facts have been set out fully by my noble and learned friend Lord Browne-Wilkinson and I do not need to repeat them here. It is sufficient to say that it is not disputed that these premiums were paid from money which had been deposited with the life assured and his business associate Mr. Deasey by the purchasers of plots of land in Portugal. This money was to be held in trust on their behalf upon the trusts of a trust deed pending the carrying out by a company controlled by the life assured of a scheme for the development of the land. In the event the company did not carry out the development and the purchasers' money was misappropriated from the bank accounts into which it had been deposited. The purchasers' claim is to a share of the proceeds of the life insurance policy, on the ground that the rights under the policy had been paid for in part with money which was taken from them without their agreement and in breach of trust to pay the premiums.

In the Court of Appeal it was held by a majority (Sir Richard Scott V.-C. and Hobhouse L.J., Morritt L.J. dissenting) that the purchasers were not entitled to participate in the proceeds of the policy except to the extent of such of their money, with interest thereon, as could be traced into the premiums: [1998] Ch. 265. Morritt L.J. would have granted a declaration to the effect that the proceeds were to be shared between the children and the purchasers. He held that they should be distributed between them in the same proportions as the life assured's own money and that which he took from the purchasers bore to the total amount paid to the insurers by way of premium during the lifetime of the policy. The purchasers have appealed against that judgment on the broad ground that common justice requires that the children should share the proceeds with them commensurately with the premiums which were paid by the life assured from his own money and the purchasers' money respectively. The children have cross-appealed on two grounds. The first is that the purchasers, having elected to take the benefit of other remedies, are precluded from pursuing any claim against the proceeds of the policy. The second is that the purchasers cannot trace their money into any part of the proceeds, because the right to payment of the sum of £1m. paid by the insurers as death benefit had already been acquired before the purchasers' money was used to pay the premiums.

I shall deal first with the childrens' cross-appeal. Mr. Kaye for the children based his argument on election upon the purchasers' receipt of compensation for the breach of trust in other proceedings brought on their behalf. The appellant obtained a declaration in 1994 that the shares in the company and the land in Portugal which was to be developed by it were held in trust for the purchasers. He also obtained for them £600,000 under a compromise in 1997 with Lloyds Bank, with whom the purchasers' money had been deposited and from whose bank accounts it had been misappropriated to pay the 1990 premium. Mr. Kaye submitted that, as the purchasers had elected to recover their plots of land in specie and had received monetary compensation in satisfaction of their claims for the misappropriation of the deposit moneys, they were barred by that election from pursuing any claim against the proceeds of the policy. He maintained that the purchasers, by pursuing these remedies, had obtained all that they had bargained for when they paid their money to the developers. They no longer had any proprietary base from which they could trace, and they had already been fully compensated as they were now in a position to complete the development. As the entire original purpose of the deposits had been fulfilled, they had lost nothing. They were in no need of any further relief by way of any proprietary or equitable remedy.

In my opinion the claims which were made against the developers and the bank and the claim now made against the proceeds of the policy are two wholly unrelated remedies. The purchasers were not put to any election when they were seeking to recover from the developers and the bank what they lost when, in breach of trust, their money was

misappropriated. Had the claim which they are now making been one by way of damages, the relief which they have already obtained in the other proceedings would have been taken into account in this action in the assessment of their loss. That would not have been because they were to be held to any election, but by applying the rule that a party who is entitled to damages cannot recover twice over for the same loss. But in this action they are claiming a share of the proceeds of the policy on the ground that the money which was taken from them can be traced into the proceeds. The amount, if any, to which they are entitled as a result of the tracing exercise does not require any adjustment on account of the compensation obtained by pursuing other remedies. This is because the remedy which they are now seeking to pursue is a proprietary one, not an award of damages. The purpose of the remedy is to enable them to vindicate their claim to their own money. The compensation which they have obtained from elsewhere may have a bearing on their claim to a proportionate share of the proceeds. But it cannot deprive them of their proprietary interest in their own money. For these reasons I would reject this argument.

Mr. Kaye then said in support of the cross-appeal that, if his argument on election were to be rejected, the purchasers were nevertheless unable to trace into any part of the policy moneys. He submitted that the majority of the Court of Appeal were wrong to hold that the purchasers were entitled to repayment of such amounts of their money as could be shown to have been expended by the life assured on the payment of the premiums. This was because the purchasers could not show that there was any proprietary or causal link between their money and the asset which they claimed, which was the death benefit paid under the policy. A contingent right to the payment of that sum was acquired at the outset when the first premium was paid by the life assured out of his own money. The purchasers' money did not add anything of value to what had already been acquired on payment of that premium. The sum payable on the death remained the same, and the rights under the policy were not made more valuable in any other respect by the payment of the additional premiums.

I do not think that there is any substance in this argument. One possible answer to it is that given by Sir Richard Scott V.-C. [1998] Ch. 265, 277C-D, who said that the statements of principle by Fry L.J. in *In re Leslie: Leslie v. French* (1883) 23 Ch.D. 552, 560 supported the right of the purchasers to trace their money into the proceeds of the policy. On his analysis the life assured, as a trustee of the policy, was prima facie entitled to an indemnity out of the trust property in respect of the payments made by him to keep the policy on foot, and the purchasers can by subrogation pursue that remedy.

I am, with great respect, not wholly convinced by this line of reasoning. It seems to me that the circumstances of this case are too far removed from those which Fry L.J. had in mind when he said a lien might be created upon the moneys secured by a policy belonging to someone else by the payment of the premiums. He referred, in his description of the circumstances, to the right of trustees to an indemnity out of the trust property for money which they had expended in its preservation, and to the subrogation to this right of a person who at their request had advanced money for its preservation to the trustees. In this case the life assured was a trustee of the policy, but he was also the person who had effected the policy and had set up the trust. When he paid the premiums, he did so not as a trustee - not because the person who was primarily responsible for their payment had failed to pay and it was necessary to take steps to preserve the trust - but because he was the person primarily responsible for their payment. The trust was one which he himself had created. He was making a further contribution towards the property which, according to his own declaration, was to be held in trust for the beneficiaries. In that situation it is hard to see on what ground the trustees of the policy could be said to be under any obligation to refund to him the amount of his expenditure. The general rule is that a man who makes a payment to maintain or improve another person's property, intentionally and not in response to any request that he should do so, is not entitled to any lien or charge on that property for such payment: *Falcke v. Scottish Imperial Insurance Co.* (1886) 34 Ch.D. 234, *per* Cotton L.J. at p. 241. A further difficulty about the subrogation argument is that it cannot be said that it was at the purchasers' request that the life assured used their money to pay the premiums.

On the other hand I consider that there is no difficulty, on the facts of this case, as to the purchasers' right on other grounds to reimbursement of the money which was taken from them by the life assured. Mr. Kaye's argument was that the purchasers could not trace their money into the proceeds of the policy because no causative link could be established between the proceeds which had been paid out by way of death benefit and the relevant premiums. In my opinion the answer to this point is to be found in the terms of the policy. It states that "in consideration of the payment of the first premium already made and of the further premiums payable and subject to the conditions of this policy" the insurer was, on the death of the life assured, to pay to the policy holder the benefits specified. The

purchasers' claim that they have a right to a proportionate share of the proceeds raises more complex issues, for the resolution of which it will be necessary to look more closely at the terms of the policy. But their right to the reimbursement of their own money seems to me to depend simply upon it being possible to follow that money from the accounts where it was deposited into the policy when the premiums were paid, and from the policy into the hands of the trustees when the insurers paid to them the sum of £1m. by way of death benefit.

On the agreed facts it is plain that the purchasers can trace their money through the premiums which were paid with it into the policy. When the insurers paid out the agreed sum by way of death benefit, the sum which they paid to the trustees of the policy was paid in consideration of the receipt by them of all the premiums. As *Professor Lionel Smith, The Law of Tracing* (1997), p. 235, has explained, the policy proceeds are the product of a mixed substitution where the value being traced into a policy of life assurance has provided a part of the premiums. In my opinion that is enough to entitle the purchasers, if they cannot obtain more, at least to obtain reimbursement of their own money with interest from the proceeds of the policy. There can be no doubt as to where the equities lie on the question of their right to recover from the proceeds the equivalent in value of that which they lost when their money was misappropriated. I would dismiss the cross-appeal.

There remains however the principal issue in this appeal, which is whether the purchasers can go further and establish that they are entitled to a much larger sum representing a proportionate share of the proceeds calculated by reference to the amount of their money which was used to pay the premiums. The purchasers' argument was presented by Mr. Mawrey on two grounds. The first was that they were entitled as a result of the tracing exercise to a proprietary right of part ownership in the proceeds which, on the application of common justice, enabled them to claim a share of them proportionate to the contribution which their money had made to the total sum paid to the insurers by way of premium. The second, which was developed briefly in the alternative and, I thought, very much by way of a subsidiary argument, was that the law of unjust enrichment would provide them with a remedy.

It seems to me that two quite separate questions arise in regard to the first of these two arguments. The first question is simply one of evidence. This is whether, if the purchasers can show that their money was used to pay any of the premiums, they can trace their money into the proceeds obtained by the trustees from the insurers in virtue of their rights under the policy. The second question is more difficult, and I think that it is the crucial question in this case. As I understand the question, it is whether it is equitable, in all the circumstances, that the purchasers should recover from the trustees a share of the proceeds calculated by reference to the contribution which their money made to the total amount paid to the insurers by way of premium.

I believe that I have already said almost all that needs to be said on the first question. It is agreed that the purchasers' money was used to pay the last two premiums. Whether their money was also used to pay a part of the 1988 premium, and if so, how much of it was so used will require to be resolved by evidence. But at least to the extent of the last two premiums the purchasers can trace their money into the policy. The terms of the policy provide a sufficient basis for tracing their money one step further. They show that this money can be followed into the proceeds received by the trustees of the policy by way of death benefit. It is clearly stated in the policy document that the benefits specified are to be made in consideration of the payment to the insurer of all the premiums. This is enough to show that the tracing exercise does not end with the receipt of the premiums by the insurers. They can say that they gave value for the premiums when they paid over to the trustees the sum to which they were entitled by way of death benefit. Nothing is left with the insurers, because they have given value for all that they received. That value now resides in the proceeds received by the trustees.

But the result of the tracing exercise cannot solve the remaining question, which relates to the extent of the purchasers' entitlement. It is the fact that this is a case of mixed substitution which creates the difficulty. If the purchasers' money had been used to pay all the premiums there would have been no mixture of value with that contributed by others. Their claim would have been to the whole of the proceeds of the policy. As it is, there are competing claims on the same fund. In the absence of any other basis for division in principle or on authority - and no other basis has been suggested - it must be divided between the competitors in such proportions as can be shown to be equitable. In my opinion the answer to the question as to what is equitable does not depend solely on the terms of the policy. The equities affecting each party must be examined. They must be balanced against each other. The conduct of the parties so far as this may be relevant, and the consequences to them of allowing and rejecting the purchasers' claim, must be analysed and weighed up. It may be helpful to refer to what would be done in other

situations by way of analogy. But it seems to me that in the end a judgment requires to be made as to what is fair, just and reasonable.

My noble and learned friend Lord Hoffmann states that this is a straightforward case of mixed substitution, which the Roman lawyers (if they had an economy which required tracing through bank accounts) would have called confusio. I confess that I have great difficulty in following this observation, as the relevant texts seem to me to indicate that they would have found the case far from straightforward and that it is quite uncertain what they would have made of it.

The discussion by the Roman jurists of the problems of ownership that arise where things which originally belonged to different people have been inextricably mixed with or attached to each other took place in an entirely different context. They were concerned exclusively with the ownership of corporeal property: with liquids like wine or solid things like heaps of corn, to which without any clear distinction in their use of terminology they applied what have come to be recognised as the doctrines of confusio and commixtio (*Institutes of Justinian* II.1.27 and 28), and with the application of the principle accessorium principale sequitur to corporeal property according to the type of property involved - accession by moveables to land, by moveables to moveables, by land to land and accession by the produce of land or the offspring of animals. I would have understood the application of the Roman law to our case if we had been dealing with the ownership of a collection of coins of gold or silver which had been melted down into liquids and transformed into another corporeal object such as a bracelet or a statue. That would indeed have been a problem familiar to Gaius and Justinian, which they would have recognised as being capable of being solved by the application of the doctrine of confusio. But here we are dealing with a problem about the rights of ownership in incorporeal property.

The taking of possession, usually by delivery, was the means by which a person acquired ownership of corporeal property. The doctrines of commixtio and confusio were resorted to in order to resolve problems created by the mixing together, or attaching to each other, of corporeal things owned two or more people. *Sandeman & Sons v. Tyzack and Branfoot Steamship Co. Ltd.* [1913] A.C. 680, in which Lord Moulton described the doctrines of English law which are applicable to cases where goods belonging to different owners have become mixed so as to be incapable of either being distinguished or separated, was also a case about what the Roman jurists would have classified as corporeal moveables - bales of jute in the hold of a cargo vessel which were unmarked and could not be identified as belonging to any particular consignment. But incorporeal property, such as the rights acquired under an insurance policy upon payment of the premiums, is incapable either of possession or of delivery in the sense of these expressions as understood in Roman law. Problems relating to rights arising out of payments made by the insurers under the policy would have belonged in Roman law to the law of obligations, and it is likely that the remedy would have been found in the application of an appropriate condictio. This is an entirely different chapter from that relating to the possession and ownership of things which are corporeal.

I think that, even if they had felt able to apply the doctrine of confusio to our case, it is far from clear that the Roman jurists would have reached a unanimous view as to the result. It is worth noting that even in the well-known case of the picture painted by Apelles on someone else's board or panel differing views were expressed: see *Stair's Institutions*, II.1.39. Paulus thought that the picture followed the ownership of the board as an accessory thereto (Digest, 6.1.23.3), while Gaius regarded the board as accessory to the picture (Digest, 41.1.9.2). Justinian's view, following Gaius, was that the board was accessory to the picture, as the picture was more precious (*Institutes Justinian* II.1.34). Stair expresses some surprise at this conclusion, because Justinian had previously declared that ownership of precious stones attached to cloth, although of greater value than cloth, was carried with the cloth. These differences of view are typical of the disputes between the Roman jurists which are to be found in the Digest.

In these circumstances I see no escape from the approach which I propose to follow, which is to examine the evidence about the rights which, in the events which happened, were acquired under the policy.

I turn first to the terms of the policy. In return for the payment of each premium the insured acquired a chose in action against the insurers which comprised the bundle of rights in terms of the policy which resulted from the payment of that premium. What those rights comprised from time to time must depend on the facts. If the life assured had not committed suicide at the age of 45, the policy might have remained on foot for many years. It was a contract of life assurance in which the sum assured on death was £1m. There was a unit-linked investment content in

each premium. The value of the units allocated by the insurers on receipt of each premium might in time have exceeded that sum. That would have increased the total amount payable on the death. But in the event the policy was not kept up for long enough for this to occur. The unit-linked investment content did not in fact make any contribution to the amount which was paid to the trustees of the policy. The effect of the payment of the first premium was to confer a right on the trustees of the policy as against the insurers to the payment of £1m. on the death of the life assured. The effect of the payment of the four remaining premiums up to the date of the life assured's suicide was to reduce the amount which the insured had to provide to meet this liability out by reinsurance or of its own funds. But they had no effect on the right of the trustees to the payment of the sum assured under the terms of the policy, as they did not increase the amount payable on the death.

I do not think that the purchasers can demonstrate on these facts that they have a proprietary right to a proportionate share of the proceeds. They cannot show that their money contributed to any extent to, or increased the value of, the amount paid to the trustees of the policy. A substantially greater sum was paid out by the insurers as death benefit than the total of the sums which they received by way of premium. A profit was made on the investment. But the terms of the policy show that the amount which produced this profit had been fixed from the outset when the first premium was paid. It was attributable to the rights obtained by the life assured when he paid the first premium from his own money. No part of that sum was attributable to value of the money taken from the purchasers to pay the additional premiums.

The next question is whether the equities affecting each party can assist the purchasers. The dispute is between two groups of persons, both of whom are innocent of the breach of trust which led to the purchasers' money being misappropriated. On the one hand there are the purchasers, who made a relatively modest but wholly involuntary contribution to the upkeep of the policy. On the other there are the children, who are the beneficiaries of the trusts of the policy but who made no contribution at all to its upkeep.

Mr. Mawrey submitted that a solution to precisely the same problem had been found in *Edinburgh Corporation v. Lord Advocate* (1879) 4 App. Cas. 823 where competing claims to a mixed fund had been resolved by the application of equitable principles. Central to his argument was the proposition that the asset of which the purchasers had been the part-purchasers was the policy itself, not the amount of the death benefit. They were to be seen as the involuntary purchasers of a share in the entire bundle of contractual rights under the policy. The proceeds of the policy were the product of those contractual rights. The terms of the policy made it clear that all benefits which were payable under it were to be made in consideration of the payment to the insurers of all the premiums. It followed that, as it was the product of the premiums towards the payment of which they had contributed, the amount of the death benefit was a mixed fund in which they were entitled to participate. He relied also, by way of analogy, on the observations of Ungoed-Thomas J. in *In re Tilley's Will Trusts* [1967] Ch. 1179, 1189 as to the rights of the beneficiary to participate in any profit which resulted where a trustee mixed trust money with his own money and then used it to purchase other property: see also *Scott v. Scott* (1963) 109 C.L.R. 649.

I am unable to agree with this approach to the facts of this case. In *Edinburgh Corporation v. Lord Advocate* (1879) 4 App. Cas. 823 the property in question was clearly a mixed fund, all the assets of which had contributed to the increase in the value of the funds held by the trustees. The facts of the case and the prolonged litigation which resulted from it are somewhat complicated: for a full account, see *Magistrates of Edinburgh v. McLaren* (1881) 8 R. (H.L.) 140. The essential point was that funds contributed by a benefactor of a hospital for particular trust purposes had for more than 170 years been held, administered and applied as part of the general funds of the hospital. The Court of Session had been directed by an earlier decision of the House of Lords in the same case to ascertain how much of the funds which had been managed in this way belonged to the hospital. In terms of its interlocutor of 20 July 1875 the Court of Session held that the benefactor's funds had been immixed with the funds of the hospital from an early period down to that date, and that they must therefore be held to have participated proportionately with the hospital's funds and property in the increase of value of the aggregate funds and property of the hospital during that period. Steps were then taken to ascertain and fix the amount of the whole of the aggregate funds and what the amount of the benefactor's funds was in proportion to the present value of the aggregate. When this had been done the case was appealed again to the House of Lords on the question, among others, whether it was right to treat the two funds as having been inextricably mixed up.

The decision of the Court of Session was upheld on this point, for reasons which I do not need to examine in detail as they have no direct bearing on the issues raised in this appeal. As Lord Blackburn put it at p. 835, the Court of Session solved the difficulty

> "in a way perfectly consistent with justice and good sense, and not inconsistent with any technical rule of law, and no other solution has been suggested which would be so satisfactory."

But the main relevance of the case for the purposes of the purchasers' argument lies in the following observation which he made at p. 833:

> "No other way was suggested at the bar in which the fund, if the two were inextricably mixed up, could be apportioned except that of taking the proportion which the two funds bore to each other, and dividing the mixed fund in that proportion; and I cannot myself see any other way."

I would have had no difficulty in reaching the same conclusion had I been persuaded that, on the facts, this was truly a case of two funds which had been inextricably been mixed up, each of which had contributed to the profit in the hands of the trustees. But it seems to me that it is on this point that the analogy with that case, and with the example of a lottery ticket purchased with money from two different sources which was also mentioned in argument, breaks down. It is no doubt true to say that the policy consisted of a bundle of rights against the insurers in consideration of the payment of all the premiums. But these rights have now been realised. We can see what has been paid out and why it was paid. We know that we are dealing with an amount paid to the trustees of the policy as death benefit in consequence of the life assured's suicide. In terms of the policy the right to payment of that amount of death benefit was purchased when the life assured paid the first premium. The insurers' right to decline payment in the event of the death of the life assured by suicide was lost after 12 months, when he kept the policy on foot by the payment of the second premium. Nothing that happened after that date affected in any way the right of the trustees of the policy to be paid the sum of £1m. when the life assured took his own life. The policy was kept on foot by the payment of the payment of the further premiums over the next three years. These premiums reduced the cost to the insurers of covering their liability under the policy in the event of the insured's death. But they made no difference to the rights which were exercisable against the insurers by the trustees of the policy or to the rights of the children as beneficiaries against the trustees.

The situation here is quite different from that where the disputed sum is the product of an investment which was made with funds which have already been immixed. In the case of the lottery ticket which is purchased by A partly from his own funds and partly from funds of which B was the involuntary contributor, the funds are mixed together at the time when the ticket is purchased. It is easy to see that any prize won by that lottery ticket must be treated as the product of that mixed fund. In the case of the funds administered as an aggregate fund by the hospital, the funds from each of the two sources had been mixed together from an early date before the various transactions were entered into which increased the amount of the aggregate. It was consistent with justice and common sense to regard the whole of the increase as attributable in proportionate shares to the money taken from the two sources. But in this case the right to obtain payment of the whole amount of the death benefit of £1m. had already been purchased from the insurers before they received payment of the premiums which were funded by the money misappropriated from the purchasers.

Of the other analogies which were suggested in the course of the argument to illustrate the extent of the equitable remedy, the closest to the circumstances of this case seemed to me to be those relating to the expenditure by a trustee of money held on trust on the improvement of his own property such as his dwelling house. This was the analogy discussed by Sir Richard Scott V.-C and by Hobhouse L.J. at [1998] Ch. 265, 282E-G and 289E-290H. There is no doubt that an equitable right will be available to the beneficiaries to have back the money which was misappropriated for his own benefit by the trustee. But that right does not extend to giving them an equitable right to a pro rata share in the value of the house. If the value of the property is increased by the improvements which were paid for in whole or in part out of the money which the trustee misappropriated, he must account to the trust for the value of the improvements. This is by the application of the principle that a trustee must not be allowed to profit from his own breach of trust. But unless it can be demonstrated that he has obtained a profit as a result of the expenditure, his liability is to pay back the money which he has misapplied.

In the present case the purchasers are, in my opinion, unable to demonstrate that the value of the entitlement of the trustees of the policy to death benefit was increased to any extent at all as a result of the use of their money to keep the policy on foot, as the entitlement had already been fixed before their money was misappropriated. In these circumstances the equities lie with the children and not with the purchasers. I do not need to attach any weight to the fact that the purchasers have already been compensated by the successful pursuit of other remedies. Even without that fact I would hold that it is fair, just and reasonable that the children should be allowed to receive the whole of the sum now in the hands of the trustees after the purchasers have been reimbursed, with interest, for the amount of their money which was used to pay the premiums.

There remains the question which Mr. Mawrey raised in his alternative argument, which is whether the purchasers have a remedy in unjust enrichment. Normally, where this question is raised, there are only two parties - the plaintiff is the person at whose expense the defendant is said to have been enriched and the defendant is the person who is said to have been enriched at the expense of the plaintiff. This case is an example of third party enrichment. The enrichment of the children is said to have resulted from a transaction with the insurers by the life assured, who had enriched himself by subtracting money from the purchasers. It is clear that the life assured was unjustly enriched when, in breach of trust and without their knowledge, he took the money from the purchasers. He transferred his enrichment to the insurers when he used that money to pay premiums. But the insurers can say in answer to a claim of unjust enrichment against them that they changed their position when, in ignorance of the breach of trust, they paid the sum assured to the trustees of the policy. Can the purchasers take their remedy against the children, who are entitled as beneficiaries under the trust of the policy to payment of the sum now in the hands of the trustees? And, if they can, does their remedy in unjust enrichment extend to a proportionate share of the proceeds of the policy, which far exceeds the amount of their involuntary expenditure when the life assured took from them the money which he used to make payment of the premiums?

These questions were not fully explored in the course of the argument, but I think that it is not necessary to do more than to make a few basic points in order to show why I consider that the purchasers cannot obtain what they want by invoking this remedy. If it could be shown that the children had consciously participated in the life assured's wrongdoing and that, having done so, they had profited from his subtraction from the purchasers of the money used to pay the premiums, the answer would be that the law will not allow them to retain that benefit. A remedy would lie against them in unjust enrichment for the amount unjustly subtracted from the purchasers and for any profit attributable to that amount. But in this case it is common ground that the children are innocent of any wrongdoing. They are innocent third parties to the unjust transactions between the life assured and the purchasers. In my opinion the law of unjust enrichment should not make them worse off as a result of those transactions than they would have been if those transactions had not happened.

The aim of the law is to correct an enrichment which is unjust, but the remedy can only be taken against a defendant who has been enriched. The undisputed facts of this case show that the children were no better off following payment of the premiums which were paid with the money subtracted from the purchasers than they would have been if those premiums had not been paid. This is because, for the reasons explained by Hobhouse L.J. [1998] Ch. 265, 286D-F, the insurers would have been entitled to have recourse to the premiums already paid to keep up the policy and because the premiums paid from the purchasers' money did not, in the events which happened, affect the amount of the sum payable in the event of the insured's death. The argument for a claim against them in unjust enrichment fails on causation. The children were not enriched by the payment of these premiums. On the contrary, they would be worse off if they were to be required to share the proceeds of the policy with the purchasers. It is as well that the purchasers' remedy in respect of the premiums and interest does not depend upon unjust enrichment, otherwise they would have had to have been denied a remedy in respect of that part of their claim also.

In these circumstances I cannot see any grounds for holding that the purchasers are entitled to participate in the amount of the death benefit except to the extent necessary for them to recover the premiums, with interest, which were paid from their money which had been misappropriated. So I would dismiss both the appeal and the cross-appeal.

**LORD MILLETT**

My Lords,

This is a textbook example of tracing through mixed substitutions. At the beginning of the story the plaintiffs were beneficially entitled under an express trust to a sum standing in the name of Mr. Murphy in a bank account. From there the money moved into and out of various bank accounts where in breach of trust it was inextricably mixed by Mr. Murphy with his own money. After each transaction was completed the plaintiffs' money formed an indistinguishable part of the balance standing to Mr. Murphy's credit in his bank account. The amount of that balance represented a debt due from the bank to Mr. Murphy, that is to say a chose in action. At the penultimate stage the plaintiffs' money was represented by an indistinguishable part of a different chose in action, viz. the debt prospectively and contingently due from an insurance company to its policyholders, being the trustees of a settlement made by Mr. Murphy for the benefit of his children. At the present and final stage it forms an indistinguishable part of the balance standing to the credit of the respondent trustees in their bank account.

*Tracing and following*

The process of ascertaining what happened to the plaintiffs' money involves both tracing and following. These are both exercises in locating assets which are or may be taken to represent an asset belonging to the plaintiffs and to which they assert ownership. The processes of following and tracing are, however, distinct. Following is the process of following the same asset as it moves from hand to hand. Tracing is the process of identifying a new asset as the substitute for the old. Where one asset is exchanged for another, a claimant can elect whether to follow the original asset into the hands of the new owner or to trace its value into the new asset in the hands of the same owner. In practice his choice is often dictated by the circumstances. In the present case the plaintiffs do not seek to follow the money any further once it reached the bank or insurance company, since its identity was lost in the hands of the recipient (which in any case obtained an unassailable title as a bona fide purchaser for value without notice of the plaintiffs' beneficial interest). Instead the plaintiffs have chosen at each stage to trace the money into its proceeds, viz. the debt presently due from the bank to the account holder or the debt prospectively and contingently due from the insurance company to the policy holders.

Having completed this exercise, the plaintiffs claim a continuing beneficial interest in the insurance money. Since this represents the product of Mr. Murphy's own money as well as theirs, which Mr. Murphy mingled indistinguishably in a single chose in action, they claim a beneficial interest in a proportionate part of the money only. The transmission of a claimant's property rights from one asset to its traceable proceeds is part of our law of property, not of the law of unjust enrichment. There is no "unjust factor" to justify restitution (unless "want of title" be one, which makes the point). The claimant succeeds if at all by virtue of his own title, not to reverse unjust enrichment. Property rights are determined by fixed rules and settled principles. They are not discretionary. They do not depend upon ideas of what is "fair, just and reasonable." Such concepts, which in reality mask decisions of legal policy, have no place in the law of property.

A beneficiary of a trust is entitled to a continuing beneficial interest not merely in the trust property but in its traceable proceeds also, and his interest binds every one who takes the property or its traceable proceeds except a bona fide purchaser for value without notice. In the present case the plaintiffs' beneficial interest plainly bound Mr. Murphy, a trustee who wrongfully mixed the trust money with his own and whose every dealing with the money (including the payment of the premiums) was in breach of trust. It similarly binds his successors, the trustees of the children's settlement, who claim no beneficial interest of their own, and Mr. Murphy's children, who are volunteers. They gave no value for what they received and derive their interest from Mr. Murphy by way of gift.

*Tracing*

We speak of money at the bank, and of money passing into and out of a bank account. But of course the account holder has no money at the bank. Money paid into a bank account belongs legally and beneficially to the bank and not to the account holder. The bank gives value for it, and it is accordingly not usually possible to make the money itself the subject of an adverse claim. Instead a claimant normally sues the account holder rather than the bank and lays claim to the proceeds of the money in his hands. These consist of the debt or part of the debt due to him from the bank. We speak of tracing money into and out of the account, but there is no money in the account. There is merely a single debt of an amount equal to the final balance standing to the credit of the account holder. No money

passes from paying bank to receiving bank or through the clearing system (where the money flows may be in the opposite direction). There is simply a series of debits and credits which are causally and transactionally linked. We also speak of tracing one asset into another, but this too is inaccurate. The original asset still exists in the hands of the new owner, or it may have become untraceable. The claimant claims the new asset because it was acquired in whole or in part with the original asset. What he traces, therefore, is not the physical asset itself but the value inherent in it.

Tracing is thus neither a claim nor a remedy. It is merely the process by which a claimant demonstrates what has happened to his property, identifies its proceeds and the persons who have handled or received them, and justifies his claim that the proceeds can properly be regarded as representing his property. Tracing is also distinct from claiming. It identifies the traceable proceeds of the claimant's property. It enables the claimant to substitute the traceable proceeds for the original asset as the subject matter of his claim. But it does not affect or establish his claim. That will depend on a number of factors including the nature of his interest in the original asset. He will normally be able to maintain the same claim to the substituted asset as he could have maintained to the original asset. If he held only a security interest in the original asset, he cannot claim more than a security interest in its proceeds. But his claim may also be exposed to potential defences as a result of intervening transactions. Even if the plaintiffs could demonstrate what the bank had done with their money, for example, and could thus identify its traceable proceeds in the hands of the bank, any claim by them to assert ownership of those proceeds would be defeated by the bona fide purchaser defence. The successful completion of a tracing exercise may be preliminary to a personal claim (as in *El Ajou v. Dollar Land Holdings* [1993] 3 All E.R. 717) or a proprietary one, to the enforcement of a legal right (as in *Trustees of the Property of F.C. Jones & Sons v. Jones* [1997] Ch. 159) or an equitable one.

Given its nature, there is nothing inherently legal or equitable about the tracing exercise. There is thus no sense in maintaining different rules for tracing at law and in equity. One set of tracing rules is enough. The existence of two has never formed part of the law in the United States: see *Scott The Law of Trusts* 4th. ed. (1989), pp.605-609. There is certainly no logical justification for allowing any distinction between them to produce capricious results in cases of mixed substitutions by insisting on the existence of a fiduciary relationship as a precondition for applying equity's tracing rules. The existence of such a relationship may be relevant to the nature of the claim which the plaintiff can maintain, whether personal or proprietary, but that is a different matter. I agree with the passages which my noble and learned friend Lord Steyn has cited from Professor Birks' essay *The Necessity of a Unitary Law of Tracing*, and with Dr. Lionel Smith's exposition in his comprehensive monograph *The Law of Tracing* (1997) see particularly pp. 120-130, 277-9 and 342-347.

This is not, however, the occasion to explore these matters further, for the present is a straightforward case of a trustee who wrongfully misappropriated trust money, mixed it with his own, and used it to pay for an asset for the benefit of his children. Even on the traditional approach, the equitable tracing rules are available to the plaintiffs. There are only two complicating factors. The first is that the wrongdoer used their money to pay premiums on an equity linked policy of life assurance on his own life. The nature of the policy should make no difference in principle, though it may complicate the accounting. The second is that he had previously settled the policy for the benefit of his children. This should also make no difference. The claimant's rights cannot depend on whether the wrongdoer gave the policy to his children during his lifetime or left the proceeds to them by his will; or if during his lifetime whether he did so before or after he had recourse to the claimant's money to pay the premiums. The order of events does not affect the fact that the children are not contributors but volunteers who have received the gift of an asset paid for in part with misappropriated trust moneys.

*The cause of action*

As I have already pointed out, the plaintiffs seek to vindicate their property rights, not to reverse unjust enrichment. The correct classification of the plaintiffs' cause of action may appear to be academic, but it has important consequences. The two causes of action have different requirements and may attract different defences.

A plaintiff who brings an action in unjust enrichment must show that the defendant has been enriched at the plaintiff's expense, for he cannot have been unjustly enriched if he has not been enriched at all. But the plaintiff is not concerned to show that the defendant is in receipt of property belonging beneficially to the plaintiff or its

traceable proceeds. The fact that the beneficial ownership of the property has passed to the defendant provides no defence; indeed, it is usually the very fact which founds the claim. Conversely, a plaintiff who brings an action like the present must show that the defendant is in receipt of property which belongs beneficially to him or its traceable proceeds, but he need not show that the defendant has been enriched by its receipt. He may, for example, have paid full value for the property, but he is still required to disgorge it if he received it with notice of the plaintiff's interest.

Furthermore, a claim in unjust enrichment is subject to a change of position defence, which usually operates by reducing or extinguishing the element of enrichment. An action like the present is subject to the bona fide purchaser for value defence, which operates to clear the defendant's title.

*The tracing rules*

The insurance policy in the present case is a very sophisticated financial instrument. Tracing into the rights conferred by such an instrument raises a number of important issues. It is therefore desirable to set out the basic principles before turning to deal with the particular problems to which policies of life assurance give rise.

The simplest case is where a trustee wrongfully misappropriates trust property and uses it exclusively to acquire other property for his own benefit. In such a case the beneficiary is entitled *at his option* either to assert his beneficial ownership of the proceeds or to bring a personal claim against the trustee for breach of trust and enforce an equitable lien or charge on the proceeds to secure restoration of the trust fund. He will normally exercise the option in the way most advantageous to himself. If the traceable proceeds have increased in value and are worth more than the original asset, he will assert his beneficial ownership and obtain the profit for himself. There is nothing unfair in this. The trustee cannot be permitted to keep any profit resulting from his misappropriation for himself, and his donees cannot obtain a better title than their donor. If the traceable proceeds are worth less than the original asset, it does not usually matter how the beneficiary exercises his option. He will take the whole of the proceeds on either basis. This is why it is not possible to identify the basis on which the claim succeeded in some of the cases.

Both remedies are proprietary and depend on successfully tracing the trust property into its proceeds. A beneficiary's claim against a trustee for breach of trust is a personal claim. It does not entitle him to priority over the trustee's general creditors unless he can trace the trust property into its product and establish a proprietary interest in the proceeds. If the beneficiary is unable to trace the trust property into its proceeds, he still has a personal claim against the trustee, but his claim will be unsecured. The beneficiary's proprietary claims to the trust property or its traceable proceeds can be maintained against the wrongdoer and anyone who derives title from him except a bona fide purchaser for value without notice of the breach of trust. The same rules apply even where there have been numerous successive transactions, so long as the tracing exercise is successful and no bona fide purchaser for value without notice has intervened.

A more complicated case is where there is a mixed substitution. This occurs where the trust money represents only part of the cost of acquiring the new asset. As Ames pointed out in "Following Misappropriated Property into its Product" (1906) Harvard Law Review 511, consistency requires that, if a trustee buys property partly with his own money and partly with trust money, the beneficiary should have the option of taking a proportionate part of the new property or a lien upon it, as may be most for his advantage. In principle it should not matter (and it has never previously been suggested that it does) whether the trustee mixes the trust money with his own and buys the new asset with the mixed fund or makes separate payments of the purchase price (whether simultaneously or sequentially) out of the different funds. In every case the value formerly inherent in the trust property has become located within the value inherent in the new asset.

The rule, and its rationale, were stated by Williston in "The Right to Follow Trust Property when Confused with Other Property" (1880) 2 Harvard Law Journal at p. 29:

> "If the trust fund is traceable as having furnished in part the money with which a certain investment was made, and the proportion it formed of the whole money so invested is known or ascertainable, the *cestui que trust* should be allowed to regard the acts of the trustee as done for his benefit, in the same way that he would if all the money so invested had been his; that is, he should be entitled in equity to an undivided share of the

property which the trust money contributed to purchase--such a proportion of the whole as the trust money bore to the whole money invested.

"The reason in the one case as in the other is that the trustee cannot be allowed to make a profit from the use of the trust money, and if the property which he wrongfully purchased were held subject only to a lien for the amount invested, any appreciation in value would go to the trustee."

If this correctly states the underlying basis of the rule (as I believe it does), then it is impossible to distinguish between the case where mixing precedes the investment and the case where it arises on and in consequence of the investment. It is also impossible to distinguish between the case where the investment is retained by the trustee and the case where it is given away to a gratuitous donee. The donee cannot obtain a better title than his donor, and a donor who is a trustee cannot be allowed to profit from his trust.

In *In re Hallett's Estate; Knatchbull v. Hallett* (1880) 13 Ch. D. 696, 709 Sir George Jessel M.R. acknowledged that where an asset was acquired exclusively with trust money, the beneficiary could either assert equitable ownership of the asset or enforce a lien or charge over it to recover the trust money. But he appeared to suggest that in the case of a mixed substitution the beneficiary is confined to a lien. Any authority that this dictum might otherwise have is weakened by the fact that Jessel M.R. gave no reason for the existence of any such rule, and none is readily apparent. The dictum was plainly *obiter*, for the fund was deficient and the plaintiff was only claiming a lien. It has usually been cited only to be explained away (see for example *In re Tilley's Will Trusts* [1967] Ch. 1179, 1186 *per* Ungoed-Thomas J.; *Burrows The Law of Restitution* (1993) p. 368). It was rejected by the High Court of Australia in *Scott v. Scott* (1963) 109 C.L.R. 649 (see the passage at pp. 661-2 cited by Morritt L.J. below at [1998] Ch. 265, 300-301). It has not been adopted in the United States: see the *American Law Institute, Restatement of the Law, Trusts, 2d* (1959) at section 202(h). In *Primeau v. Granfield* (1911) 184 F. 480 (S.D.N.Y.) at p. 184 Learned Hand J. expressed himself in forthright terms: "On principle there can be no excuse for such a rule."

In my view the time has come to state unequivocally that English law has no such rule. It conflicts with the rule that a trustee must not benefit from his trust. I agree with Burrows that the beneficiary's right to elect to have a proportionate share of a mixed substitution necessarily follows once one accepts, as English law does, (i) that a claimant can trace in equity into a mixed fund and (ii) that he can trace unmixed money into its proceeds and assert ownership of the proceeds.

Accordingly, I would state the basic rule as follows. Where a trustee wrongfully uses trust money to provide part of the cost of acquiring an asset, the beneficiary is entitled *at his option* either to claim a proportionate share of the asset or to enforce a lien upon it to secure his personal claim against the trustee for the amount of the misapplied money. It does not matter whether the trustee mixed the trust money with his own in a single fund before using it to acquire the asset, or made separate payments (whether simultaneously or sequentially) out of the differently owned funds to acquire a single asset.

Two observations are necessary at this point. First, there is a mixed substitution (with the results already described) whenever the claimant's property has contributed in part only towards the acquisition of the new asset. It is not necessary for the claimant to show in addition that his property has contributed to any increase in the *value* of the new asset. This is because, as I have already pointed out, this branch of the law is concerned with vindicating rights of property and not with reversing unjust enrichment. Secondly, the beneficiary's right to claim a lien is available only against a wrongdoer and those deriving title under him otherwise than for value. It is not available against competing contributors who are innocent of any wrongdoing. The tracing rules are not the result of any presumption or principle peculiar to equity. They correspond to the common law rules for following into physical mixtures (though the consequences may not be identical). Common to both is the principle that the interests of the wrongdoer who was responsible for the mixing and those who derive title under him otherwise than for value are subordinated to those of innocent contributors. As against the wrongdoer and his successors, the beneficiary is entitled to locate his contribution in any part of the mixture and to subordinate their claims to share in the mixture until his own contribution has been satisfied. This has the effect of giving the beneficiary a lien for his contribution if the mixture is deficient.

Innocent contributors, however, must be treated equally inter se. Where the beneficiary's claim is in competition with the claims of other innocent contributors, there is no basis upon which any of the claims can be subordinated to any of the others. Where the fund is deficient, the beneficiary is not entitled to enforce a lien for his contributions; all must share rateably in the fund.

The primary rule in regard to a mixed fund, therefore, is that gains and losses are borne by the contributors rateably. The beneficiary's right to elect instead to enforce a lien to obtain repayment is an exception to the primary rule, exercisable where the fund is deficient and the claim is made against the wrongdoer and those claiming through him. It is not necessary to consider whether there are any circumstances in which the beneficiary is confined to a lien in cases where the fund is more than sufficient to repay the contributions of all parties. It is sufficient to say that he is not so confined in a case like the present. It is not enough that those defending the claim are innocent of any wrongdoing if they are not themselves contributors but, like the trustees and Mr. Murphy's children in the present case, are volunteers who derive title under the wrongdoer otherwise than for value. On ordinary principles such persons are in no better position than the wrongdoer, and are liable to suffer the same subordination of their interests to those of the claimant as the wrongdoer would have been. They certainly cannot do better than the claimant by confining him to a lien and keeping any profit for themselves.

Similar principles apply to following into physical mixtures: see *Lupton v. White* (1808) 15 Ves. 442; and *Sandemann & Sons v. Tyzack and Branfoot Steamship Co. Ltd.* [1913] A.C. 680, 695 where Lord Moulton said: "If the mixing has arisen from the fault of B, A can claim the goods." There are relatively few cases which deal with the position of the innocent recipient from the wrongdoer, but *Jones v. De Marchant* (1916) 28 D.L.R. 561 may be cited as an example. A husband wrongfully used 18 beaver skins belonging to his wife and used them, together with four skins of his own, to have a fur coat made up which he then gave to his mistress. Unsurprisingly the wife was held entitled to recover the coat. The mistress knew nothing of the true ownership of the skins, but her innocence was held to be immaterial. She was a gratuitous donee and could stand in no better position than the husband. The coat was a new asset manufactured from the skins and not merely the product of intermingling them. The problem could not be solved by a sale of the coat in order to reduce the disputed property to a divisible fund, since (as we shall see) the realisation of an asset does not affect its ownership. It would hardly have been appropriate to require the two ladies to share the coat between them. Accordingly it was an all or nothing case in which the ownership of the coat must be assigned to one or other of the parties. The determinative factor was that the mixing was the act of the wrongdoer through whom the mistress acquired the coat otherwise than for value.

The rule in equity is to the same effect, as Sir William Page Wood V.-C. observed in *Frith v. Cartland* (1865) 2 H. & M. 417 at p. 418:

> ". . . If a man mixes trust funds with his own, the whole will be treated as the trust property, except so far as he may be able to distinguish what is his own."

This does not, in my opinion, exclude a pro rata division where this is appropriate, as in the case of money and other fungibles like grain, oil or wine. But it is to be observed that a pro rata division is the best that the wrongdoer and his donees can hope for. If a pro rata division is excluded, the beneficiary takes the whole; there is no question of confining him to a lien. *Jones v. De Marchant* 28 D.L.R. 561 is a useful illustration of the principles shared by the common law and equity alike that an innocent recipient who receives misappropriated property by way of gift obtains no better title than his donor, and that if a proportionate sharing is inappropriate the wrongdoer and those who derive title under him take nothing.

*Insurance policies*

In the case of an ordinary whole life policy the insurance company undertakes to pay a stated sum on the death of the assured in return for fixed annual premiums payable throughout his life. Such a policy is an entire contract, not a contract for a year with a right of renewal. It is not a series of single premium policies for one year term assurance. It is not like an indemnity policy where each premium buys cover for a year after which the policyholder must renew or the cover expires. The fact that the policy will lapse if the premiums are not paid makes no difference. The amounts of the annual premiums and of the sum assured are fixed in advance at the outset and assume the payment of annual premiums throughout the term of the policy. The relationship between them is based

on the life expectancy of the assured and the rates of interest available on long term government securities at the inception of the policy.

In the present case the benefits specified in the policy are expressed to be payable "in consideration of the payment of the first premium already made and of the further premiums payable." The premiums are stated to be "£10,220 payable at annual intervals from 6 November 1985 throughout the lifetime of the life assured." It is beyond argument that the death benefit of £1m. paid on Mr. Murphy's death was paid in consideration for *all* the premiums which had been paid before that date, including those paid with the plaintiffs' money, and not just some of them. Part of that sum, therefore, represented the traceable proceeds of the plaintiffs' money.

It is, however, of critical importance in the present case to appreciate that the plaintiffs do not trace the premiums directly into the insurance money. They trace them first into the policy and thence into the proceeds of the policy. It is essential not to elide the two steps. In this context, of course, the word "policy" does not mean the contract of insurance. You do not trace the payment of a premium into the insurance contract any more than you trace a payment into a bank account into the banking contract. The word "policy" is here used to describe the bundle of rights to which the policyholder is entitled in return for the premiums. These rights, which may be very complex, together constitute a chose in action, viz. the right to payment of a debt payable on a future event and contingent upon the continued payment of further premiums until the happening of the event. That chose in action represents the traceable proceeds of the premiums; its current value fluctuates from time to time. When the policy matures, the insurance money represents the traceable proceeds of the policy and hence indirectly of the premiums.

It follows that, if a claimant can show that premiums were paid with his money, he can claim a proportionate share of the policy. His interest arises by reason of and immediately upon the payment of the premiums, and the extent of his share is ascertainable at once. He does not have to wait until the policy matures in order to claim his property. His share in the policy and its proceeds may increase or decrease as further premiums are paid; but it is not affected by the realisation of the policy. His share remains the same whether the policy is sold or surrendered or held until maturity; these are merely different methods of realising the policy. They may affect the amount of the proceeds received on realisation but they cannot affect the extent of his share in the proceeds. In principle the plaintiffs are entitled to the insurance money which was paid on Mr. Murphy's death in the same shares and proportions as they were entitled in the policy immediately before his death.

Since the manner in which an asset is realised does not affect its ownership, and since it cannot matter whether the claimant discovers what has happened before or after it is realised, the question of ownership can be answered by ascertaining the shares in which it is owned immediately before it is realised. Where A misappropriates B's money and uses it to buy a winning ticket in the lottery, B is entitled to the winnings. Since A is a wrongdoer, it is irrelevant that he could have used his own money if in fact he used B's. This may seem to give B an undeserved windfall, but the result is not unjust. Had B discovered the fraud before the draw, he could have decided whether to keep the ticket or demand his money back. He alone has the right to decide whether to gamble with his own money. If A keeps him in ignorance until after the draw, he suffers the consequence. He cannot deprive B of his right to choose what to do with his own money; but he can give him an informed choice.

The application of these principles ought not to depend on the nature of the chose in action. They should apply to a policy of life assurance as they apply to a bank account or a lottery ticket. It has not been suggested in argument that they do not apply to a policy of life assurance. This question has not been discussed in the English authorities, but it has been considered in the United States. In a Note in 35 *Yale Law Journal* (1925) at pp. 220-227 Professor Palmer doubted the claimant's right to share in the proceeds of a life policy, and suggested that he should be confined to a lien for his contributions. Professor Palmer accepted, as the majority of the Court of Appeal in the present case did not, that the claimant can trace from the premiums into the policy and that the proceeds of the policy are the product of all the premiums. His doubts were not based on any technical considerations but on questions of social policy. They have not been shared by the American courts. These have generally allowed the claimant a share in the proceeds proportionate to his contributions even though the share in the proceeds is greater than the amount of his money used in paying the premiums: see for example *Shaler v. Trowbridge* (1877) 28 N.J. Eq. 595; *Holmes v. Gilman* (1893) 138 N.Y. 369); *Vorlander v. Keyes* (1924) 1 F. 2d. 67 (1924); *Truelsch v. Northwestern Mutual Life Insurance Co.* (1925) 202 N.W. 352 (1925); *Baxter House v. Rosen* (1967) 278 N.Y. 2d.

442; *Lohman v. General American Life Insurance Co.* (1973) 478 F. 2d. 719. This accords with Ames' and Williston's opinions in the articles to which I have referred.

The question is discussed at length in *Scott*: *The Law of Trust* in section 508.4 at pp. 574-584. Professor Scott concludes that there is no substance in the doubts expressed by Palmer. He points out that the strongest argument in favour of limiting the beneficiary's claim to a lien is that otherwise he obtains a windfall. But in cases where the wrongdoer has misappropriated the claimant's money and used it to acquire other forms of property which have greatly increased in value the courts have consistently refused to limit the claimant to an equitable lien. In any case, the windfall argument is suspect. As Professor Scott points out, a life policy is an aleatory contract. Whether or not the sum assured exceeds the premiums is a matter of chance. Viewed from the perspective of the insurer, the contract is a commercial one; so the chances are weighted against the assured. But the outcome in any individual case is unpredictable at the time the premiums are paid. The unspoken assumption in the argument that a life policy should be treated differently from other choses in action seems to be that, by dying earlier than expected, the assured provides a contribution of indeterminate but presumably substantial value. But the assumption is false. A life policy is not an indemnity policy, in which the rights against the insurer are acquired by virtue of the payment of the premiums and the diminution of the value of an asset. In the case of a life policy the sum assured is paid in return for the premiums and nothing else. The death of the assured is merely the occasion on which the insurance money is payable. The ownership of the policy does not depend on whether this occurs sooner or later, or on whether the bargain proves to be a good one. It cannot be made to await the event.

The windfall argument has little to commend it in the present case. The plaintiffs were kept in ignorance of the fact that premiums had been paid with their money until after Mr. Murphy's death. Had they discovered what had happened before Mr. Murphy died, they would have intervened. They might or might not have elected to take an interest in the policy rather than enforce a lien for the return of the premiums paid with their money, but they would certainly have wanted immediate payment. This would have entailed the surrender of the policy. At the date of his death Mr. Murphy was only 45 and a non-smoker. He had a life expectancy of many years, and neither he nor the trustees had the means to keep up the premiums. The plaintiffs would hardly have been prepared to wait for years to recover their money, paying the premiums in the meantime. It is true that, under the terms of the policy, life cover could if necessary be maintained for a few years more at the expense of the investment element of the policy (which also provided its surrender value). But it is in the highest degree unlikely that the plaintiffs would have been willing to gamble on the remote possibility of Mr. Murphy's dying before the policy's surrender value was exhausted. If he did not they would recover nothing. They would obviously have chosen to enforce their lien to recover the premiums or have sought a declaration that the trustees held the policy for Mr. Murphy's children and themselves as tenants in common in the appropriate shares. In either case the trustees would have had no alternative but to surrender the policy. In practice the trustees were able to obtain the death benefit by maintaining the policy until Mr. Murphy's death only because the plaintiffs were kept in ignorance of the fact that premiums had been paid with their money and so were unable to intervene.

*The reasoning of the Court of Appeal*

The majority of the Court of Appeal (Sir Richard Scott V.-C. and Hobhouse L.J.) held that the plaintiffs could trace their money into the premiums but not into the policy, and were accordingly not entitled to a proportionate share in the proceeds. They did so, however, for different and, in my view, inconsistent reasons which cannot both be correct and which only coincidentally led to the same result in the present case.

The Vice-Chancellor considered that Mr. Murphy's children acquired vested interests in the policy at its inception. They had a vested interest (subject to defeasance) in the death benefit at the outset and before any of the plaintiffs' money was used to pay the premiums. The use of the plaintiffs' money gave the plaintiffs a lien on the proceeds of the policy for the return of the premiums paid with their money, but could not have the effect of divesting the children of their existing interest. The children owned the policy; the plaintiffs' money was merely used to maintain it. The position was analogous to that where trust money was used to maintain or improve property of a third party.

The Vice-Chancellor treated the policy as an ordinary policy of life assurance. It is not clear whether he thought that the children obtained a vested interest in the policy because Mr. Murphy took the policy out or because he paid

the first premium, but I cannot accept either proposition. Mr. Murphy was the original contracting party, but he obtained nothing of value until he paid the first premium. The chose in action represented by the policy is the product of the premiums, not of the contract. The trustee took out the policy in all the recorded cases. In some of them he paid all the premiums with trust money. In such cases the beneficiary was held to be entitled to the whole of the proceeds of the policy. In other cases the trustee paid some of the premiums with his own money and some with trust money. In those cases the parties were held entitled to the proceeds of the policy rateably in proportion to their contributions. It has never been suggested that the beneficiary is confined to his lien for repayment of the premiums because the policy was taken out by the trustee. The ownership of the policy does not depend on the identity of the party who took out the policy. It depends on the identity of the party or parties whose money was used to pay the premiums.

So the Vice-Chancellor's analysis can only be maintained if it is based the fact that Mr. Murphy paid the first few premiums out of his own money before he began to make use of the trust money. Professor Scott records only one case in which it has been held that in such a case the claimant is confined to a lien on the ground that the later premiums were not made in acquiring the interest under the policy but merely in preserving or improving it: see *Thum v. Wolstenholme* (1900) 21 Utah 446, 537. The case is expressly disapproved by Scott (loc. cit.) at section 516.1, where it is said that the decision cannot be supported, and that the claimant should be entitled to a proportionate share of the proceeds, regardless of the question whether some of the premiums were paid wholly with the claimant's money and others wholly with the wrongdoer's money and regardless of the order of the payments, or whether the premiums were paid out of a mingled fund containing the money of both.

In my opinion there is no reason to differentiate between the first premium or premiums and later premiums. Such a distinction is not based on any principle. Why should the policy belong to the party who paid the first premium, without which there would have been no policy, rather than to the party who paid the last premium, without which it would normally have lapsed? Moreover, any such distinction would lead to the most capricious results. If only four annual premiums are paid, why should it matter whether A paid the first two premiums and B the second two, or B paid the first two and A the second two, or they each paid half of each of the four premiums? Why should the children obtain the whole of the sum assured if Mr. Murphy used his own money before he began to use the plaintiffs' money, and only a return of the premiums if Mr. Murphy happened to use the plaintiffs' money first? Why should the proceeds of the policy be attributed to the first premium when the policy itself is expressed to be in consideration of all the premiums? There is no analogy with the case where trust money is used to maintain or improve property of a third party. The nearest analogy is with an instalment purchase.

Hobhouse L.J. adopted a different approach. He concentrated on the detailed terms of the policy, and in particular on the fact that in the event the payment of the fourth and fifth premiums with the plaintiffs' money made no difference to the amount of the death benefit. Once the third premium had been paid, there was sufficient surrender value in the policy, built up by the use of Mr. Murphy's own money, to keep the policy on foot for the next few years, and as it happened Mr. Murphy's death occurred during those few years. But this was adventitious and unpredictable at the time the premiums were paid. The argument is based on causation and as I have explained is a category mistake derived from the law of unjust enrichment. It is an example of the same fallacy that gives rise to the idea that the proceeds of an ordinary life policy belong to the party who paid the last premium without which the policy would have lapsed. But the question is one of attribution not causation. The question is not whether the same death benefit would have been payable if the last premium or last few premiums had not been paid. It is whether the death benefit is attributable to all the premiums or only to some of them. The answer is that death benefit is attributable to all of them because it represents the proceeds of realising the policy, and the policy in turn represents the product of all the premiums.

In any case, Hobhouse L.J.'s analysis of the terms of the policy does not go far enough. It is not correct that the last two premiums contributed nothing to the sum payable on Mr. Murphy's death but merely reduced the cost to the insurers of providing it. Life cover was provided in return for a series of internal premiums paid for by the cancellation of units previously allocated to the policy. Units were allocated to the policy in return for the annual premiums. Prior to their cancellation the cancelled units formed part of a mixed fund of units which was the product of all the premiums paid by Mr. Murphy, including those paid with the plaintiffs' money. On ordinary principles, the plaintiffs can trace the last two premiums into and out of the mixed fund and into the internal premiums used to provide the death benefit.

It is true that the last two premiums were not needed to provide the death benefit in the sense that in the events which happened the same amount would have been payable even if those premiums had not been paid. In other words, with the benefit of hindsight it can be seen that Mr. Murphy made a bad investment when he paid the last two premiums. It is, therefore, superficially attractive to say that the plaintiffs' money contributed nothing of value. But the argument proves too much, for if the plaintiffs cannot trace their money into the proceeds of the policy, they should have no proprietary remedy at all, not even a lien for the return of their money. But the fact is that Mr. Murphy, who could not foresee the future, did choose to pay the last two premiums, and to pay them with the plaintiffs' money; and they were applied by the insurer towards the payment of the internal premiums needed to fund the death benefit. It should not avail his donees that he need not have paid the premiums, and that if he had not then (in the events which happened) the insurers would have provided the same death benefit and funded it differently.

In the case of an ordinary life policy which lapses if the premiums are not paid, the Vice-Chancellor's approach gives the death benefit to the party whose money was used to pay the first premium, and Hobhouse L.J.'s approach gives it to the party whose money was used to pay the last premium. In the case of a policy like the present, Hobhouse L.J.'s approach also produces unacceptable and capricious results. The claimant must wait to see whether the life assured lives long enough to exhaust the amount of the policy's surrender value as at the date immediately before the claimant's money was first used. If the life assured dies the day before it would have been exhausted, the claimant is confined to his lien to recover the premiums; if he dies the day after, then the claimant's premiums were needed to maintain the life cover. In the latter case he takes at least a proportionate share of the proceeds or, if the argument is pressed to its logical conclusion, the whole of the proceeds subject to a lien in favour of the trustees of the children's settlement. This simply cannot be right.

Hobhouse L.J.'s approach is also open to objection on purely practical grounds. It must, I think, be unworkable if there is an eccentric pattern of payment; or if there is a fall in the value of the units at a critical moment. Like the Vice-Chancellor's approach, it prompts the question: why should the order of payments matter? It is true that the premiums paid with the plaintiff's money did not in the event increase the amount payable on Mr. Murphy's death, but they increased the surrender value of the policy and postponed the date at which it would lapse if no further premiums were paid. Why should it be necessary to identify the premium the payment of which (in the events which happened) prevented the policy from lapsing? Above all, this approach makes it impossible for the ownership of the policy to be determined until the policy matures or is realised. This too cannot be right.

The trustees argued that such considerations are beside the point. It is not necessary, they submitted, to consider what the plaintiffs' rights would have been if the policy had been surrendered, or if Mr. Murphy had lived longer. It is sufficient to take account of what actually happened. I do not agree. A principled approach must yield a coherent solution in all eventualities. The ownership of the policy must be ascertainable at every moment from inception to maturity; it cannot be made to await events. In my view the only way to achieve this is to hold firm to the principle that the manner in which an asset is converted into money does not affect its ownership. The parties' respective rights to the proceeds of the policy depend on their rights to the policy immediately before it was realised on Mr. Murphy's death, and this depends on the shares in which they contributed to the premiums and nothing else. They do not depend on the date at which or the manner in which the chose in action was realised. Of course, Mr. Murphy's early death greatly increased the value of the policy and made the bargain a good one. But the idea that the parties' entitlements to the policy and its proceeds are altered by the death of the life assured is contrary to principle and to the decision of your Lordships' House in *D'Avigdor Goldsmid v. Inland Revenue Commissioners* [1953] A.C. 347. That case establishes that no fresh beneficial interest in a policy of life assurance accrues or arises on the death of the life assured. The sum assured belongs to the person or persons who were beneficial owners of the policy immediately before the death.

In the course of argument it was submitted that if the children, who were innocent of any wrongdoing themselves, had been aware that their father was using stolen funds to pay the premiums, they could have insisted that the premiums should not be paid, and in the events which happened would still have received the same death benefit. But the fact is that Mr. Murphy concealed his wrongdoing from both parties. The proper response is to treat them both alike, that is to say rateably. It is morally offensive as well as contrary to principle to subordinate the claims of the victims of a fraud to those of the objects of the fraudster's bounty on the ground that he concealed his wrongdoing from both of them.

The submission is not (as has been suggested) supported by Professor David Hayton's article "Equity's Identification Rules" in *Professor Peter Birk's Laundering and Tracing* (1995) at pp. 11-12. Professor Hayton is dealing with the very different case of the party who decides to purchase an asset and has the means to pay for it, but who happens to use trust money which he has received innocently, not knowing it to belong to a third party and believing himself to be entitled to it. In such a case his decision to use the trust money rather than his own is independent of the breach of trust; it is a matter of pure chance. This is a problem about tracing, not claiming, and has nothing to do with mixtures, as Professor Hayton's article itself makes clear. It is a difficult problem on the solution to which academic writers are not agreed. But it does not arise in the present case. It was Mr. Murphy's decision to use the plaintiffs' money to pay the later premiums. The children are merely passive recipients of an asset acquired in part by the use of misappropriated trust money. They are innocent of any personal wrongdoing, but they are not contributors. They are volunteers who derive their interest from the wrongdoer otherwise than for value and are in no better position than he would have been if he had retained the policy for the benefit of his estate. It is not, with respect to those who think otherwise, a case where there are competing claimants to a fund who are both innocent victims of a fraud and where the equities are equal. But if it were such a case, the parties would share rateably, which is all that the plaintiffs claim.

I should now deal with the finding of all the members of the Court of Appeal that the plaintiffs were entitled to enforce a lien on the proceeds of the policy to secure repayment of the premiums paid with their money. This is inconsistent with the decision of the majority that the plaintiffs were not entitled to trace the premiums into the policy. An equitable lien is a proprietary interest by way of security. It is enforceable against the trust property and its traceable proceeds. The finding of the majority that the plaintiffs had no proprietary interest in the policy or its proceeds should have been fatal to their claim to a lien.

The Court of Appeal held that the plaintiffs were entitled by way of subrogation to Mr. Murphy's lien to be repaid the premiums. He was, they thought, entitled to the trustee's ordinary lien to indemnify him for expenditure laid out in the preservation of the trust property: see *In re Leslie* (1883) 23 Ch. D. 560. Had Mr. Murphy used his own money, they said, it would have been treated as a gift to his children; but the fact that he used stolen funds rebutted any presumption of advancement.

With all due respect, I do not agree that Mr. Murphy had any lien to which the plaintiffs can be subrogated. He was one of the trustees of his children's settlement, but he did not pay any of the premiums in that capacity. He settled a life policy on his children but without the funds to enable the trustees to pay the premiums. He obviously intended to add further property to the settlement by paying the premiums. When he paid the premiums with his own money he did so as settlor, not as trustee. He must be taken to have paid the later premiums in the same capacity as he paid the earlier ones. I do not for my own part see how his intention to make further advancements into the settlement can be rebutted by showing that he was not using his own money; as between himself and his children the source of the funds is immaterial. He could not demand repayment from the trustees by saying: "I used stolen money; now that I have been found out you must pay me back so that I can repay the money". Moreover, even if the presumption of advancement were rebutted, there would be no resulting trust. Mr. Murphy was either (as I would hold) a father using stolen money to make further gifts to his children or a stranger paying a premium on another's policy without request: see *Falcke v. Scottish Imperial Insurance Co.* (1886) 34 Ch. D. 234.

But perhaps the strongest ground for rejecting the argument is that it makes the plaintiffs' rights depend on the circumstance that Mr. Murphy happened to be one of the trustees of his children's settlement. That is adventitious. If he had not been a trustee then, on the reasoning of the majority of the Court of Appeal, the plaintiffs would have had no proprietary remedy at all, and would be left with a worthless personal claim against Mr. Murphy's estate. The plaintiffs' rights cannot turn on such chances as this.

*The relevant proportions*

Accordingly, I agree with Morritt L.J. in the Court of Appeal that, on well established principles, the parties are entitled to the proceeds of the policy in the proportions in which those proceeds represent their respective contributions. It should not, however, be too readily assumed that this means in the proportions in which the insurance premiums were paid with their money. These represent the *cost* of the contributions, not necessarily their *value*.

A mixed fund, like a physical mixture, is divisible between the parties who contributed to it rateably in proportion to the value of their respective contributions, and this must be ascertained at the time they are added to the mixture. Where the mixed fund consists of sterling or a sterling account or where both parties make their contributions to the mixture at the same time, there is no difference between the cost of the contributions and their sterling value. But where there is a physical mixture or the mixture consists of an account maintained in other units of account and the parties make their contributions at different times, it is essential to value the contributions of *both* parties at the same time. If this is not done, the resulting proportions will not reflect a comparison of like with like. The appropriate time for valuing the parties' respective contributions is when successive contributions are added to the mixture.

This is certainly what happens with physical mixtures. If 20 gallons of A's oil are mixed with 40 gallons of B's oil to produce a uniform mixture of 60 gallons, A and B are entitled to share in the mixture in the proportions of 1 to 2. It makes no difference if A's oil, being purchased later, cost £2 a gallon and B's oil cost only £1 a gallon, so that they each paid out £40. This is because the mixture is divisible between the parties rateably in proportion to the *value* of their respective contributions and not in proportion to their respective *cost*. B's contribution to the mixture was made when A's oil was added to his, and *both* parties' contributions should be valued at that date. Should a further 20 gallons of A's oil be added to the mixture to produce a uniform mixture of 80 gallons at a time when the oil was worth £3 a gallon, the oil would be divisible equally between them. (A's further 20 gallons are worth £3 a gallon--but so are the 60 gallons belonging to both of them to which they have been added). It is not of course necessary to go through the laborious task of valuing every successive contribution separately in sterling. It is simpler to take the account by measuring the contributions in gallons rather than sterling. This is merely a short cut which produces the same result.

In my opinion the same principle operates whenever the mixture consists of fungibles, whether these be physical assets like oil, grain or wine or intangibles like money in an account. Take the case where a trustee misappropriates trust money in a sterling bank account and pays it into his personal dollar account which also contains funds of his own. The dollars are, of course, merely units of account; the account holder has no proprietary interest in them. But no one, I think, would doubt that the beneficiary could claim the dollar value of the contributions made with trust money. Most people would explain this by saying that it is because the account is kept in dollars. But the correct explanation is that it is because the contributions are made in dollars. In order to allocate the fund between the parties rateably in proportion to the value of their respective contributions, it is necessary to identify the point at which the trust money becomes mixed with the trustee's own money. This does not occur when the trustee pays in a sterling cheque drawn on the trust account. At that stage the trust money is still identifiable. It occurs when the bank credits the dollar equivalent of the sterling cheque to the trustee's personal account. Those dollars represent the contribution made by the trust. The sterling value of the trust's contribution must be valued at that time; and it follows that the trustee's contributions, which were also made in dollars, must be valued at the same time. Otherwise one or other party will suffer the injustice of having his contributions undervalued.

*Calculating the plaintiffs' share*

I finally come to the difficult question: how should the parties' contributions, and therefore their respective shares in the proceeds, be calculated in the case of a unit-linked policy of the present kind? This makes it necessary to examine the terms of the policy in some detail.

All the reported cases have been concerned with ordinary policies of life assurance. In all the cases the insurance moneys have been shared between the parties in the proportions in which their money has been used to pay the premiums irrespective of the dates on which the premiums were paid. This favours the party who paid the later premiums at the expense of the party who paid the earlier ones. There is therefore a case for adding interest to the premiums in order to produce a fair result. This cannot be justified by the need to compensate the parties for the loss of the use of their money over different periods. It is not merely that this branch of the law is concerned with vindicating property rights and not with compensation for wrongdoing. It is that ex hypothesi the money has not been lost but used to produce the insurance money. But I think that taking account of interest can be justified nonetheless. The policy and its proceeds are not the product of the uninvested premiums alone. If they were, the sum assured would be very much smaller than it is. They are the product of the premiums invested at compound interest. It does not matter, of course, what the insurance company actually does with the money. What matters is how the

sum assured is calculated, because this shows what it represents. In practice it represents the sum which would be produced by the premiums over the term of the expected life of the assured together with compound interest at the rate available at the inception of the policy on long term government securities. But the question has not been the subject of argument before us, and having regard to the mechanics of the present policy the calculations may not be worth doing. I agree therefore with my noble and learned friend Lord Hoffmann that there is no need to explore this aspect further.

Unit-linked policies, however, are very different. These policies have become popular in recent years, and are commonly employed for personal pension plans taken out by the self-employed. Under such a policy the premiums are applied by the insurance company in the acquisition of accumulation units in a designated fund usually managed by the insurance company. The bid and offer prices of the units are published daily in the financial press. The value of the units can go down as well as up, but since they carry the reinvested income their value can be expected to increase substantially over the medium and long term. The policy is essentially a savings medium, and (subject to tax legislation) can be surrendered at any time. On surrender the policyholder is entitled to the value of the units allocated to the policy. Early policies provided that on death the policyholder was entitled merely to the return of his premiums with interest, but more modern policies provide for payment of the value of the units in this event also.

Where money belonging to different parties is used to pay the premiums under a policy of this kind, it cannot be right to divide the proceeds of the policy crudely according to the number of premiums paid by each of them. The only sensible way of apportioning the proceeds of such a policy is by reference to the number of units allocated to the policy in return for each premium. This is readily ascertainable, since policyholders are normally issued with an annual statement showing the number of units held before receipt of the latest premium, the number allocated in respect of the premium, and the total number currently held. But in any case these numbers can easily be calculated from published material.

This would obviously be the right method to adopt if the policyholder acquired a proprietary interest in the units. These would fall to be dealt with in the same way as grain, oil or wine. There would of course still be a mixed substitution, since after the mixture neither party's contributions can be identified. Neither can recover his own property, but only a proportion of the whole. Unlike Roman law, the common law applied the same principles whenever there is no means of identifying the specific assets owned by either party. In the United States they have been applied to logs, pork, turkeys, sheep and straw hats: see *Dr. Lionel Smith, The Law of Tracing*, at p. 70. In fact unit-linked policies normally provide that the policyholder has no proprietary interest in the units allocated to the policy. They are merely units of account. The absence of a proprietary interest in the units would be highly material in the event of the insolvency of the insurance company. But it should have no effect on the method of calculating the shares in which competing claimants are entitled to the proceeds of the policy. This depends upon the proportions in which they contributed to the acquisition of the policy, and the question is: in what units of account should the parties' respective contributions be measured? Should they be measured in sterling, this being the currency in which the premiums were paid? Or should they be measured by accumulation units, if this was the unit of account into which the premiums were converted before the admixture took place? Principle, and the cases on physical mixtures, indicate that the second is the correct approach. A unit linked policy of the kind I have described is simply a savings account. The account is kept in units. The mixing occurs when the insurance company, having received a premium in sterling, allocates units to the account of the insured where they are at once indistinguishably mixed with the units previously allocated. The contribution made by each of the parties consists of the units, not merely of their sterling equivalent. The proceeds of a unit-linked policy should in my opinion be apportioned rateably between the parties in proportion to the value of their respective contributions measured in units, not in sterling.

The policy in the present case is only a variant of the unit-linked policy of the kind I have described. It is also primarily a savings medium but it offers an additional element of life assurance. This protects the assured against the risk of death before the value of the units allocated to the policy reaches a predetermined amount. On receipt of each premium, the insurance company allocates accumulation units in the designated fund to the policy ("the investment element"), and immediately thereafter cancels sufficient of the units to provide "the insurance element." This is in effect an internal premium retained by the insurance company to provide the life cover. The amount of the internal premium is calculated each year by a complicated formula. The important feature of the formula for present purposes is that the internal premium is not calculated by reference to the sum assured of £1m. but by reference to

the difference between the current value of the units allocated to the policy and the sum assured. As the value of the units increases, therefore, the amount of the internal premium should reduce. When their value is equal to or greater than the sum assured, no further internal premiums are payable. Thenceforth the policy is exactly like the kind of unit-linked policy described above. The policyholder is entitled to the investment element, ie. the value of the accumulated units, on death as well as on surrender.

If the policyholder dies at a time when the investment element is less than the sum assured, then he receives the sum assured. This is paid as a single sum, but it has two components with different sources. One is the investment element, which represents the value of the accumulated units at the date of death. The other is the insurance element, which is merely a balancing sum. It will be very large in the early years of the policy and will eventually reduce to nothing. It is the product of the internal premiums and is derived from the cancelled units. The internal premiums, however, though derived from the cancelled units, were credited to the account in sterling. The proceeds of the internal premiums, therefore, should be apportioned between the parties pro rata in the proportions in which those premiums were provided in sterling.

In my opinion the correct method of apportioning the sum assured between the parties is to deal separately with its two components. The investment element (which amounted to £39,347 at the date of death in the present case) should be divided between the parties by reference to the value at maturity of the units allocated in respect of each premium and not cancelled. The balance of the sum assured should be divided between the parties rateably in the proportions in which they contributed to the internal premiums. This is not to treat the allocated units as a real investment separate from the life cover when it was not. Nor is it to treat the method by which the benefits payable under the policy is calculated as determinative or even relevant. It is to recognise the true nature of the policy, and to give effect to the fact that the sum assured had two components, to one of which the parties made their contributions in units and to the other of which they made their contributions in the sterling proceeds of realised units.

These calculations require the policyholder's account to be redrawn as two accounts, one for each party. The number of units allocated to the policy on the receipt of each premium should be credited to the account of the party whose money was used to pay the premium. The number of units so allocated should be readily ascertainable from the records of the insurance company, but if not it can easily be worked out. The number of units which were cancelled to provide the internal premium should then be ascertained in similar fashion and debited to the appropriate account. In the case of the earlier premiums paid with Mr. Murphy's own money this will be the trustees' account. In the case of the later premiums paid with the plaintiffs' money, the cancelled units should not be debited wholly to the plaintiffs' account, but rateably to the two accounts. The amount of the internal premiums should then be credited to the two accounts in the same proportions as those in which the cancelled units were debited to provide them.

This approach is substantially more favourable to the children than a crude allocation by reference to the premiums. By taking account of the value of the units, it automatically weights the earlier premiums which should have bought more units than the later ones. And it gives effect to the fact that, under the terms of the policy, both parties contributed to the later internal premiums which produced the greater part of the death benefit.

It is, of course, always open to the parties in any case to dispense with complex calculations and agree upon a simpler method of apportionment. But in my opinion the court ought not to do so without the parties' consent. If it does, anomalies and inconsistencies will inevitably follow. Take the present case. The method of apportionment, with greatly differing results, ought not to depend upon whether the value of the units at the date of death is slightly more or slightly less than the sum assured. Yet once their value exceeds the amount of the sum assured, the policy becomes an ordinary unit-linked pension policy without an insurance element. If the sum assured is divided crudely in proportion requires that the same method be adopted for pension policies, which is surely wrong. If it is adopted for pension policies, then it is difficult to see how foreign currency assets can be treated differently, which is certainly wrong. There is an enormous variety of financial instruments. For present purposes they form a seamless web. Cutting corners in the interest of simplicity is tempting, but in my opinion the temptation ought to be resisted.

*Conclusion*

Accordingly I would allow the appeal. In my opinion the insurance money ought to be divided between the parties in the proportions I have indicated. But I am alone in adopting this approach, and as the question was not argued before us I am content that your Lordships should declare that the money should be divided between the parties in proportions in which they contributed to the premiums. For the reasons given by my noble and learned friend Lord Hope of Craighead, with which I agree, I would dismiss the children's cross-appeal.

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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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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
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 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 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 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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*Sprint Canada Inc. v. Bell Canada*, 1997 CarswellOnt 4135, 79 C.P.R. (3d) 31 (Ont. Gen. Div.) — 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, 1975 CarswellSask 56, 1975 CarswellSask 97 (S.C.C.) — considered

*Toronto (City) v. C.U.P.E., Local 79*, 2003 SCC 63, 2003 CarswellOnt 4328, 2003 CarswellOnt 4329, 2003 C.L.L.C. 220-071, 232 D.L.R. (4th) 385, 9 Admin. L.R. (4th) 161, 311 N.R. 201, 120 L.A.C. (4th) 225, 179 O.A.C. 291, [2003] 3 S.C.R. 77, 17 C.R. (6th) 276 (S.C.C.) — referred to

*Transport North American Express Inc. v. New Solutions Financial Corp.*, 2004 SCC 7, 2004 CarswellOnt 512, 2004 CarswellOnt 513, 40 B.L.R. (3d) 18, 316 N.R. 84, 235 D.L.R. (4th) 385, [2004] 1 S.C.R. 249, [2004] S.C.J. No. 9, 70 O.R. (3d) 255 (note), 18 C.R. (6th) 1, 17 R.P.R. (4th) 1, 183 O.A.C. 342 (S.C.C.) — referred to

**Statutes considered:**

*Code civil du Québec*, L.Q. 1991, c. 64

art. 1493 — referred to

art. 1494 — referred to

*Constitution Act, 1867 (U.K.)*, 30 & 31 Vict., c. 3, reprinted R.S.C. 1985, App. II, No. 5

s. 91 ¶ 19 — referred to

s. 91 ¶ 27 — referred to

s. 92 ¶ 13 — referred to

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

Generally — referred to

s. 15 — considered

s. 347 — referred to

s. 347(1) — considered

s. 347(1)(b) — referred to

*Municipal Franchises Act*, R.S.O. 1990, c. M.55

Generally — referred to

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

Generally — referred to

s. 18 — considered

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

s. 25 — considered

**Rules considered:**

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

Generally — referred to

R. 45.02 — considered

  

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 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.

**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 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.

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?

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*

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.

*(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 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.

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.

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 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 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 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 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 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 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.

2006 CarswellOnt 987
Ontario Superior Court of Justice

General Motors Corp. v. Peco Inc.

2006 CarswellOnt 987, [2006] O.J. No. 636, 146 A.C.W.S. (3d) 18, 15 B.L.R. (4th) 282, 19 C.B.R. (5th) 224

# General Motors Corporation (Applicant) and Peco, Inc. (Respondent)

Cumming J.

Heard: February 16, 2006
Judgment: February 17, 2006
Docket: 05-CL-5957

Counsel: Craig Hill for Mantum Corporation
Rachelle Moncur for Respondent, Receiver

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

**Related Abridgment Classifications**

Bankruptcy and insolvency
X Priorities of claims
X.7 Unsecured claims
X.7.a General principles
Bankruptcy and insolvency
X Priorities of claims
X.7 Unsecured claims
X.7.d Workers' Compensation Board
Debtors and creditors
VII Receivers
VII.7 Actions involving receiver
VII.7.b Actions against receiver
VII.7.b.iii Miscellaneous
Equity
IV Relief from unconscionable transactions
IV.1 Unconscionable or improvident transactions
IV.1.f Unjust enrichment
Restitution and unjust enrichment
IV Benefits conferred under ineffective transactions
IV.4 Breach, repudiation or abandonment of contract

**Headnote**

Bankruptcy and insolvency --- Priorities of claims — Unsecured claims — General principles

Pursuant to contract dated March 23, 2000, creditor pursued Workers' Compensation refund because of over-payments on behalf of debtor, for which it was to be paid 35 per cent of sums recovered — Creditor was successful by June 15, 2005 in obtaining refund, and refund was quantified at $234,577.77 on August 22, 2005 — On initiative of secured creditor, receiver was appointed June 24, 2005 with power to carry on debtor's business — Receiver was aware in early July of possibility of refund but did not know of creditor's role until August 11, 2005 — Creditor picked up refund cheque in full amount on September 1, 2005, presented invoice on September 2, and was informed by receiver on September 7 that it was simply unsecured creditor — Creditor moved for order that receiver pay it 35 per cent of refund recovered — Motion granted — While receiver learned of creditor by August 11, 2005, at no time did it dissuade creditor from continuing its efforts by indicating that creditor's continued

 

involvement was no longer wanted and its payment for services was at risk — Receivership order effectuating continuation of services to debtor provided for full payment by receiver for supply of services after date of order — While bulk of creditor's work was done before order, significant work was done in late August, and creditor was entitled only to fee at point of recovery — Receiver adopted contract between creditor and debtor.

Restitution --- Benefits conferred under ineffective transactions — Breach, repudiation or abandonment of contract — Innocent party seeking relief

Unjust enrichment — Pursuant to contract, creditor pursued Workers' Compensation refund because of over-payments on behalf of debtor, for which it was to be paid 35 per cent of sums recovered — Five years later, creditor was successful in securing $234,577.77 refund — After securing refund, but before refund was quantified and paid, receiver was appointed with power to carry on debtor's business — After receiving cheque from creditor, receiver informed creditor that it was simply unsecured creditor — Creditor moved for order that receiver pay it 35 per cent of refund recovered — Motion granted — Creditor was entitled to recovery on basis of unjust enrichment — Receiver was enriched in having in hand 100 per cent of refund rather than 65 per cent to which it was entitled, and there was no juristic reason for receiver to retain 35 per cent of refund — Pursuant to contract, refund was paid in its entirety to debtor, and thereupon creditor was entitled to receive fee of 35 per cent of recovered refund from debtor — Debtor did not have expectation of retaining creditor's 35 per cent interest in refund, and receiver standing in creditor's shoes could have no such expectation — Entire refund was identifiable as discrete fund and never became part of general funds or assets of debtor — Contest for 35 per cent was in reality contest between creditor and secured creditor, which was debtor's single creditor.

Equity --- Relief from unconscionable transactions — Unconscionable or improvident transactions — Unjust enrichment

Unjust enrichment — Pursuant to contract, creditor pursued Workers' Compensation refund because of over-payments on behalf of debtor, for which it was to be paid 35 per cent of sums recovered — Five years later, creditor was successful in securing $234,577.77 refund — After securing refund, but before refund was quantified and paid, receiver was appointed with power to carry on debtor's business — After receiving cheque from creditor, receiver informed creditor that it was simply unsecured creditor — Creditor moved for order that receiver pay it 35 per cent of refund recovered — Motion granted — Creditor was entitled to recovery on basis of unjust enrichment — Receiver was enriched in having in hand 100 per cent of refund rather than 65 per cent to which it was entitled, and there was no juristic reason for receiver to retain 35 per cent of refund — Pursuant to contract, refund was paid in its entirety to debtor, and thereupon creditor was entitled to receive fee of 35 per cent of recovered refund from debtor — Debtor did not have expectation of retaining creditor's 35 per cent interest in refund, and receiver standing in creditor's shoes could have no such expectation — Entire refund was identifiable as discrete fund and never became part of general funds or assets of debtor — Contest for 35 per cent was in reality contest between creditor and secured creditor, which was debtor's single creditor.

**Table of Authorities**

**Cases considered by *Cumming J.*:**

*Canada (Attorney General) v. Confederation Life Insurance Co.* (1995), 8 C.C.P.B. 1, C.E.B. & P.G.R. 8227 (headnote only), 33 C.B.R. (3d) 161, 8 E.T.R. (2d) 72, 31 C.C.L.I. (2d) 77, 24 O.R. (3d) 717, 1995 CarswellOnt 318 (Ont. Gen. Div.) — referred to

**Statutes considered:**

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

s. 101 — referred to

**Words and phrases considered**

**contracts**

Contracts ultimately are bundles of reciprocal reasonable expectations, created by the exchange of promises.

MOTION by creditor for order that receiver pay it 35 per cent of refund recovered from Worker's Safety and Insurance Board.

***Cumming J.*:**

**The Motion**

  

1 The moving party, Mantum Corporation ("Mantum"), seeks an order that Zeifman &Partners Inc., the Receiver and Manager of PECO, Inc. (the "Receiver"), pay to Mantum 35% of a refund of $234,577.77 (the " Refund") recovered from the Worker's Safety and Insurance Board ("WSIB"), held by the Receiver

**The Evidence**

2 There is common ground the Refund resulted solely as the result of the extensive work performed by Mantum over several years. Mantum has a contract with PECO dated March 23, 2000, whereby Mantum would determine whether PECO was entitled to Workers' Compensation refunds due to overpayments. The contract provided:

> ...Mantum will be paid a fee of 35% of amounts recovered and/or savings obtained for all previous years....
>
> Fees become payable at the time refunds/savings are realized by way of cheque, credit or reduction in accrued amounts payable.

3 This work culminated in a successful appeal conducted by Mantum on behalf of PECO before the Workplace Safety and Insurance Appeals Tribunal November 30, 2004 with the 10 page decision dated March 30, 2005 allowing PECO's appeal. There remained the precise quantification of the Refund, to be determined by the WSIB after a typical audit by WSIB conducted after any decision affecting classification.

4 PECO did not have all the requisite historical records. Mantum was successful by June 15, 2005 in convincing WSIB to process PECO's adjustments determining the Refund without requiring the usual source documents. Mantum continued in discussions with the WSIB, eventually resulting in a determination about August 22, 2005 that the Refund was quantified at $234, 577.77, after a re-calculated reduction of some $150,000.00 by the WSIB from the calculation of $404,798.34 the WSIB had initially made July 15, 2005.

5 Of this amount of $234,577.77, Mantum would be entitled to its fee of 35% thereof. Mantum picked up the cheque for $234,577.77 on September 1, 2005 with the authority of PECO.

6 Mantum presented an invoice September 2, 2005 but was told by the Receiver September 7, 2005 that Mantum was simply an unsecured creditor of PECO.

7 There is common ground that any unsecured creditors of PECO would have no recovery in any bankruptcy proceeding, PECO being insolvent albeit not in formal bankruptcy.

8 On the initiative of General Motors Corporation ("GMC") as a secured creditor, the Receiver had been appointed by Court Order June 24, 2005 pursuant to s. 101 of the *Courts of Justice Act*, the Receivership Order having the terms of a standard, normative order.

9 The powers pursuant to the Receivership Order included the power to "manage, operate and carry on the business of the Debtor...."

10 The Receiver reportedly learned of the possibility of a refund in early July, 2005 but did not know of Mantum's role until August 11, 2005.

11 Mr. Terrence J. Ryan, the principal of Mantum, had learned August 4, 2005 from Mr. Glen Retty, the Controller of PECO, that PECO was in receivership but was told that Mantum would be paid in full for his services. Mr. Retty had the authority from the Receiver to make such a commitment to Mantum although the Receiver did not know the commitment was made, nor as stated above, know of Mantum's involvement in the refund process until August 11, 2005.

12 The Receiver, aware in early July that there was the possibility of a refund, had the opportunity from that point onwards to determine the precise status and arrangements in respect of the refund process.

  

**The Law**

***Paragraph 11 of the Receivership Order***

13 In my view, in operating PECO, the Receiver's surrogates, being Mr. Retty and Mr. Glen Rogers, both key employees of PECO, had the authority to and did bind the Receiver, after the creation of the Receivership, to Mantum's continued role in providing services in pursuing a refund.

14 Moreover, the Receiver did not at any point after learning of Mantum August 11, 2005 and within a few days thereafter receiving from Mantum a copy of its contract with PECO, dissuade Mantum from continuing its efforts by indicating that Mantum's continued involvement was no longer wanted and its payment for services was at risk.

15 Paragraph 11 of the Receivership Order, effectuating the continuation of services to PECO, provides for full payment by the Receiver for the supply of services after the date of the Order, June 24, 2005.

16 Although the bulk of Mantum's work was before June 24, 2005, there was significant work done right into late August. Moreover, Mantum's fee accrued only at the point of actual recovery of the Refund, being September 1, 2005. Mantum was entitled to the fee only at the point of recovery and simply for achieving that recovery. It did not matter how much time or effort was expended or for how long. Accordingly, in my view, given the nature of the contract and the evidentiary record, the Receiver adopted the contract between PECO and Mantum by the actions and conduct of its authorized surrogates. I find that paragraph 11 of the Receivership Order applies.

***Unjust Enrichment***

17 In my view, and I so find, Mantum is also entitled to recovery on a basis of unjust enrichment.

18 There is an *enrichment*, in that the Receiver has in hand 100% of the Refund rather than 65%, being all to which PECO was entitled. There is a corresponding *deprivation* inasmuch as Mantum is short the 35% of the Refund to which it is entitled.

19 It is agreed the only possible issue in respect of a sustainable claim for unjust enrichment is whether there is the absence of a *juristic reason* for the enrichment.

20 An obligation which leads to the enrichment — whether the obligation arises from a debtor-creditor relationship or other contractual context, or whether it arises by way of the principles of common law or of equity or by way of statute — may constitute a juristic reason. *Canada (Attorney General) v. Confederation Life Insurance Co.* (1995), 24 O.R. (3d) 717 (Ont. Gen. Div.) at 769.

21 Turning to the situation at hand, given its terms, the contract between Mantum and PECO does read literally as though the obligation of PECO is to pay Mantum upon Mantum providing the service of obtaining the Refund to the credit of PECO. No part, ie. 35%, of the Refund is paid by the WSIB directly to Mantum. By the contractual terms, the Refund in its entirety is paid to or credited to the account of PECO. Thereupon, Mantum is entitled to receive a fee of 35% of the amount of the recovered Refund from PECO.

22 However, the literal contractual arrangements must be considered within the context of the overall circumstances.

23 Mantum and PECO had agreed to a contractual arrangement which in substance was a contingency agreement whereby there was to be a sharing on a fixed formula of whatever quantum resulted from the successful venture.

24 Contracts ultimately are bundles of reciprocal reasonable expectations, created by the exchange of promises. Such reasonable expectations are determined on an objective test. Turning to the instant situation, on an objective test the reasonable expectations of the parties were that if Mantum was successful there would be a sharing of the Refund. The parties had as reasonable expectations that PECO had a 65% interest in the Refund fund and Mantum had a 35% interest in that fund. Indeed,

  

as seen from the evidentiary record, on a subjective test these were the reasonable expectations held by both Mantum and PECO, with each party knowing full well the reasonable expectation of the other.

25 PECO clearly did not have any expectation of retaining the 35% interest of Mantum in the Refund. GMC and the Receiver, standing in PECO's shoes, can have no such expectation.

26 Second, the entire Refund is identifiable as a discrete fund, received from the WSIB via Mantum and held to date by the Receiver. That is, the monies have never become part of the general funds or assets of PECO.

27 Third, in reality, the contest for the 35% is between Mantum and only a single creditor of PECO, being GMC as a secured creditor. This is not a situation seen in an insolvency whereby the monies in dispute would be shared amongst creditors of a bankrupt if the moving party, Mantum, was unsuccessful.

28 If Mantum is not entitled to its claimed 35%, then the secured creditor receives the enrichment of that amount, ie. the secured creditor through the Receiver receives 100% of the Refund. No creditor of PECO, other than GMC, is disadvantaged by Mantum receiving the 35% of the Refund in dispute. To not give Mantum the 35%would result in a windfall to GMC.

29 Fourth, as stated above, the Receiver through its surrogates in operating the business authorized Mantum to continue in its efforts after the creation of the Receivership and assured Mantum it would receive its 35% if it were successful.

30 Considering all of these factors, in my view, and I so find, there is no juristic reason for the Receiver to retain the 35% of the Refund in dispute. Mantum is entitled to its claimed 35% of the Refund plus any interest earned thereon in the interval from its receipt to payment pursuant to the Order implementing this decision. This result is consistent with principles of equity and is the only result possible that is equitable and fair to all parties.

**Disposition**

31 For the reasons given, the motion is allowed. I impose a constructive trust upon the Refund in respect of Mantum's interest therein and entitlement thereto. I order the Receiver to pay Mantum forthwith its entitlement in the Refund that is subject to the constructive trust.

32 I may be spoken to as to costs.

*Motion granted.*

2007 SKCA 72
Saskatchewan Court of Appeal

ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.

2007 CarswellSask 324, 2007 SKCA 72, [2007] 9 W.W.R. 79, [2007] S.J. No. 313, 159 A.C.W.S. (3d) 671, 299 Sask. R. 194, 33 C.B.R. (5th) 50, 408 W.A.C. 194

# ICR Commercial Real Estate (Regina) Ltd. (Appellant) and Bricore Land Group Ltd., Bricore Investment Group Ltd., 624796 Saskatchewan Ltd. 603767 Saskatchewan Ltd.,(Respondents)

Klebuc C.J.S., Jackson, Smith JJ.A.

Heard: June 7, 2007
Judgment: June 13, 2007
Docket: 1443, 1452

Proceedings: affirming *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.* (2007), 2007 SKQB 121, 2007 CarswellSask 157 (Sask. Q.B.); additional reasons at *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.* (2007), 2007 SKQB 144, 2007 CarswellSask 264 (Sask. Q.B.); and reversing *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.* (2007), 2007 SKQB 144, 2007 CarswellSask 264 (Sask. Q.B.)

Counsel: Fred C. Zinkhan for Appellant
Jeffrey M. Lee for Respondents
Kim Anderson for Monitor, Ernst & Young

Subject: Civil Practice and Procedure; Insolvency; Corporate and Commercial
**Related Abridgment Classifications**
Bankruptcy and insolvency
XVII Practice and procedure in courts
XVII.4 Stay of proceedings
Bankruptcy and insolvency
XIX Companies' Creditors Arrangement Act
XIX.2 Initial application
XIX.2.f Lifting of stay
Civil practice and procedure
XXIV Costs
XXIV.7 Particular orders as to costs
XXIV.7.e Costs on solicitor and client basis
XXIV.7.e.ii Grounds for awarding
XXIV.7.e.ii.A Unfounded allegations
Debtors and creditors
VII Receivers
VII.7 Actions involving receiver
VII.7.b Actions against receiver

  

VII.7.b.i Liability
Debtors and creditors
VII Receivers
VII.7 Actions involving receiver
VII.7.e Practice and procedure
VII.7.e.iii Costs

**Headnote**

Bankruptcy and insolvency --- Practice and procedure in courts — Stay of proceedings
Application to lift stay — B Ltd. owned building and other properties — B Ltd. filed under Companies Creditors' Arrangement Act ("CCAA") and stay of proceedings was imposed — Supervising judge appointed exclusive selling officer for B Ltd. properties, and appointed chief restructuring officer ("CRO") to assist with sale — CRO accepted purchaser's offer on B Ltd. properties ("offer") — CRO submitted report to supervising judge recommending sale of building and advising that offer represented greatest value obtainable — CRO signed agreement with realtor ("disputed agreement") — Disputed agreement provided that realtor would be protected as agent of record if B Ltd. properties were sold to other potential buyers, including City of Regina ("city") — B Ltd. properties were ultimately sold pursuant to offer, and purchaser later resold building to city — Realtor took position that it had introduced city to opportunity to purchase building, and was therefore entitled to commission — Realtor's application for leave to commence action against B Ltd. was dismissed — Supervising judge held that realtor failed to establish "prima facie case" — Realtor appealed — Appeal allowed in part — Appeal was allowed with respect to costs only — "Sound reasons" test was better than "prima facie case" test in deciding whether to lift stay under CCAA — Nonetheless, realtor did not reach necessary threshold — Relevant facts included that building was subject to exclusive selling officer agreement; that two days before disputed agreement, supervising judge received CRO report recommending sale of building; that disputed agreement stated that properties were under contract to sell; and that there was no sale from B Ltd. to city — Language in disputed agreement supported CRO's position that purpose of agreement was to provide for eventuality of failed sale — Further, supervising judge issued at least five orders dealing substantively with sale of building to purchaser — B Ltd.'s argument, that it was not subject to stay order, was rejected — Application to lift stay must be made to commence action against debtor subject to CCAA order, regardless of whether claim arises before or after initial order — Section 11.3 of CCAA does not grant post-filing creditor right to sue without obtaining leave.
Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Arrangements — Effect of arrangement — Stay of proceedings
Application to lift stay — B Ltd. owned building and other properties — B Ltd. filed under Companies Creditors' Arrangement Act ("CCAA") and stay of proceedings was imposed — Supervising judge appointed exclusive selling officer for B Ltd. properties, and appointed chief restructuring officer ("CRO") to assist with sale — CRO accepted purchaser's offer on B Ltd. properties ("offer") — CRO submitted report to supervising judge recommending sale of building and advising that offer represented greatest value obtainable — CRO signed agreement with realtor ("disputed agreement") — Disputed agreement provided that realtor would be protected as agent of record if B Ltd. properties were sold to other potential buyers, including City of Regina ("city") — B Ltd. properties were ultimately sold pursuant to offer, and purchaser later resold building to city — Realtor took position that it had introduced city to opportunity to purchase building, and was therefore entitled to commission — Realtor's application for leave to commence action against B Ltd. was dismissed — Supervising judge held that realtor failed to establish "prima facie case" — Realtor appealed — Appeal allowed in part — Appeal was allowed with respect to costs only — "Sound reasons" test was better than "prima facie case" test in deciding whether to lift stay under CCAA — Nonetheless, realtor did not reach necessary threshold — Relevant facts included that building was subject to exclusive selling officer agreement; that two days before disputed agreement, supervising judge received CRO report recommending sale of building; that disputed agreement stated that properties were under contract to sell; and that there was no sale from B Ltd. to city — Language in disputed agreement supported CRO's position that purpose of agreement was to provide for eventuality of failed sale — Further, supervising judge issued at least five orders dealing substantively with sale of building to purchaser — B Ltd.'s argument, that it was not subject to stay order, was rejected — Application to lift stay must be made to commence action against debtor subject to CCAA order, regardless of whether claim arises before or after initial order — Section 11.3 of CCAA does not grant post-filing creditor right to sue without obtaining leave.
Debtors and creditors --- Receivers — Actions by and against receiver — Actions against receiver

  

Against chief restructuring officer — Application to lift stay — B Ltd. owned building and other properties — B Ltd. filed under Companies Creditors' Arrangement Act ("CCAA") — Supervising judge stayed proceedings and appointed chief restructuring officer ("CRO") — Order appointing CRO stated that he could not be sued personally except for acts of fraud, gross negligence or wilful misconduct, but order was ambiguous about acts of bad faith — CRO accepted purchaser's offer on B Ltd. properties ("offer") — CRO submitted report to supervising judge recommending sale of building and advising that offer represented greatest value obtainable — CRO signed agreement with realtor ("disputed agreement") — Disputed agreement provided that realtor would be protected as agent of record if B Ltd. properties were sold to other potential buyers, including City of Regina ("city") — B Ltd. properties were ultimately sold pursuant to offer, and purchaser later resold building to city — Realtor took position that it had introduced city to opportunity to purchase building, and was therefore entitled to commission — Realtor's application for leave to commence action against CRO personally based on bad faith was dismissed — Supervising judge held that realtor was required to allege fraud, gross negligence or wilful misconduct, and failed to do so — Supervising judge accepted CRO's explanation that he was not aware that purchaser was going to resell building — Realtor appealed — Appeal allowed in part — Appeal was allowed with respect to costs only — Supervising judge did not err in refusing to lift stay to permit action against CRO personally — Supervising judge considered status of CRO as officer of court, noted ambiguity in order, and weighed evidence to certain extent.

Debtors and creditors --- Receivers — Actions by and against receiver — Practice and procedure — Costs

On application to lift stay — B Ltd. owned building and other properties — B Ltd. filed under Companies Creditors' Arrangement Act ("CCAA") — Supervising judge stayed proceedings and appointed chief restructuring officer ("CRO") — Order appointing CRO stated that he could not be sued personally except for bad faith or other acts of misconduct — CRO accepted purchaser's offer on B Ltd. properties ("offer") — CRO signed agreement with realtor ("disputed agreement") — Disputed agreement provided that realtor would be protected as agent of record if B Ltd. properties were sold to other potential buyers, including City of Regina ("city") — B Ltd. properties were ultimately sold pursuant to offer, and purchaser later resold building to city — Realtor took position that it had introduced city to opportunity to purchase building, and was therefore entitled to commission — Realtor's application for leave to commence action against B Ltd. and against CRO personally was dismissed — Supervising judge held that realtor did not have tenable cause of action against B Ltd. or CRO — Supervising judge accepted CRO's explanation that he was not aware that purchaser was going to resell building — Supervising judge awarded substantial indemnity costs to B Ltd. and CRO, on ground that realtor had alleged bad faith by CRO — Supervising judge declined to award solicitor-and-client costs on ground that there was no inappropriate conduct giving rise to litigation — Realtor appealed — Appeal allowed in part — Appeal was allowed with respect to costs only — Supervising judge erred in awarding substantial indemnity costs — There was no basis on which to order substantial indemnity costs with respect to stay in relation to B Ltd. — Bad faith was not alleged on part of B Ltd. — With respect to allegation of bad faith against CRO, realtor could not be faulted for making very allegation that it was required to make to bring application — Award of substantial indemnity costs is punitive and must meet same test used for solicitor-and-client costs.

Civil practice and procedure --- Costs — Particular orders as to costs — Costs on solicitor and client basis — Grounds for awarding — Unfounded allegations

Against chief restructuring officer — B Ltd. owned building and other properties — B Ltd. filed under Companies Creditors' Arrangement Act ("CCAA") — Supervising judge stayed proceedings and appointed chief restructuring officer ("CRO") — Order appointing CRO stated that he could not be sued personally except for bad faith or other acts of misconduct — CRO accepted purchaser's offer on B Ltd. properties ("offer") — CRO signed agreement with realtor ("disputed agreement") — Disputed agreement provided that realtor would be protected as agent of record if B Ltd. properties were sold to other potential buyers, including City of Regina ("city") — B Ltd. properties were ultimately sold pursuant to offer, and purchaser later resold building to city — Realtor took position that it had introduced city to opportunity to purchase building, and was therefore entitled to commission — Realtor's application for leave to commence action against B Ltd. and against CRO personally was dismissed — Supervising judge held that realtor did not have tenable cause of action against B Ltd. or CRO — Supervising judge accepted CRO's explanation that he was not aware that purchaser was going to resell building — Supervising judge awarded substantial indemnity costs to B Ltd. and CRO, on ground that realtor had alleged bad faith by CRO — Supervising judge declined to award solicitor-and-client costs on ground that there was no inappropriate conduct giving rise to litigation — Realtor appealed — Appeal allowed in part — Appeal was allowed with respect to costs only — Supervising judge erred in awarding substantial indemnity costs — There was no basis on which to order substantial indemnity costs with respect to stay in relation to B Ltd. —

  

Bad faith was not alleged on part of B Ltd. — With respect to allegation of bad faith against CRO, realtor could not be faulted for making very allegation that it was required to make to bring application — Award of substantial indemnity costs is punitive and must meet same test used for solicitor-and-client costs.

**Table of Authorities**

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*Air Canada, Re* (2004), 47 C.B.R. (4th) 182, 2004 CarswellOnt 643 (Ont. S.C.J. [Commercial List]) — referred to

*Campeau v. Olympia & York Developments Ltd.* (1992), 14 C.B.R. (3d) 303, 14 C.P.C. (3d) 339, 1992 CarswellOnt 185 (Ont. Gen. Div.) — considered

*Canadian Airlines Corp., Re* (2000), 19 C.B.R. (4th) 1, 2000 CarswellAlta 622 (Alta. Q.B.) — considered

*Caterpillar Financial Services Ltd. v. 360networks corp.* (2007), 2007 BCCA 14, 2007 CarswellBC 29, 61 B.C.L.R. (4th) 334, 28 E.T.R. (3d) 186, 27 C.B.R. (5th) 115, 10 P.P.S.A.C. (3d) 311, 235 B.C.A.C. 95, 388 W.A.C. 95 (B.C. C.A.) — referred to

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*Hashemian v. Wilde* (2006), [2007] 2 W.W.R. 52, 40 C.P.C. (6th) 10, 2006 SKCA 126, 2006 CarswellSask 740, 382 W.A.C. 105, 289 Sask. R. 105 (Sask. C.A.) — followed

*Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 51 B.C.L.R. (2d) 84, 1990 CarswellBC 394, 4 C.B.R. (3d) 311, *(*sub nom. *Chef Ready Foods Ltd. v. Hongkong Bank of Canada)* [1991] 2 W.W.R. 136 (B.C. C.A.) — referred to

*Ivaco Inc., Re* (2003), 2003 CarswellOnt 6097, 1 C.B.R. (5th) 204, 6 P.P.S.A.C. (3d) 261 (Ont. S.C.J. [Commercial List]) — considered

*Ivaco Inc., Re* (2006), 2006 CarswellOnt 8025 (Ont. S.C.J.) — considered

*Ma, Re* (2001), 143 O.A.C. 52, 2001 CarswellOnt 1019, 24 C.B.R. (4th) 68 (Ont. C.A.) — followed

*Martin v. Deutch* (1943), [1943] O.R. 683, 1943 CarswellOnt 36, [1943] 4 D.L.R. 600 (Ont. C.A.) — referred to

*Mosaic Group Inc., Re* (2004), 2004 CarswellOnt 2254, 3 C.B.R. (5th) 40 (Ont. S.C.J.) — referred to

*New Skeena Forest Products Inc., Re* (2005), 7 M.P.L.R. (4th) 153, [2005] 8 W.W.R. 224, *(*sub nom. *New Skeena Forest Products Inc. v. Kitwanga Lumber Co.)* 210 B.C.A.C. 247, *(*sub nom. *New Skeena Forest Products Inc. v. Kitwanga Lumber Co.)* 348 W.A.C. 247, 2005 BCCA 192, 2005 CarswellBC 705, 9 C.B.R. (5th) 278, 39 B.C.L.R. (4th) 338 (B.C. C.A.) — considered

*Ptarmigan Airways Ltd. v. Federated Mining Corp.* (1973), 1973 CarswellNWT 10, [1973] 3 W.W.R. 723 (N.W.T. S.C.) — referred to

*Quintette Coal Ltd. v. Nippon Steel Corp.* (1990), 51 B.C.L.R. (2d) 105, 1990 CarswellBC 384, 2 C.B.R. (3d) 303 (B.C. C.A.) — referred to

*Ramsay Plate Glass Co. v. Modern Wood Products Ltd.* (1954), 1954 CarswellQue 24, 34 C.B.R. 82 (C.S. Que.) — considered

*Siemens v. Bawolin* (2002), 2002 SKCA 84, 2002 CarswellSask 448, 46 E.T.R. (2d) 254, [2002] 11 W.W.R. 246, 219 Sask. R. 282, 272 W.A.C. 282 (Sask. C.A.) — followed

*Smart v. South Saskatchewan Hospital Centre* (1989), 75 Sask. R. 34, 60 D.L.R. (4th) 8, [1989] 5 W.W.R. 289, 1989 CarswellSask 266 (Sask. C.A.) — considered

*Smith Brothers Contracting Ltd., Re* (1998), 1998 CarswellBC 678, 53 B.C.L.R. (3d) 264, 13 P.P.S.A.C. (2d) 316 (B.C. S.C.) — considered

*Stelco Inc., Re* (2005), 2005 CarswellOnt 5024, 15 C.B.R. (5th) 283 (Ont. S.C.J. [Commercial List]) — considered

*360networks Inc., Re* (2003), 45 C.B.R. (4th) 151, 2003 BCSC 1030, 2003 CarswellBC 1636 (B.C. S.C.) — considered

**Statutes considered:**

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

Generally — referred to

*Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act and the Income Tax Act, Act to amend the*, S.C. 1997, c. 12

Generally — referred to

*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36

Generally — referred to

  

s. 11 [rep. & sub. 2005, c. 47, s. 128] — referred to

s. 11(3) — considered

s. 11(4) — considered

s. 11(4)(c) — considered

s. 11(6) — considered

s. 11(6) [en. 1997, c. 12, s. 124] — considered

s. 11.1(2) [en. 1997, c. 12, s. 124] — considered

s. 11.11 [en. 2001, c. 9, s. 577] — considered

s. 11.2 [en. 1997, c. 12, s. 124] — considered

s. 11.3 [en. 1997, c. 12, s. 124] — considered

s. 12(1) "claim" — considered

s. 13 — referred to

*Real Estate Act*, S.S. 1995, c. R-1.3

Generally — referred to

**Rules considered:**

*Queen's Bench Rules*, Sask. Q.B. Rules

R. 173 — referred to

**Words and phrases considered:**

**Substantial indemnity costs**

[Jackson J.A. (Klebuc C.J.S. and Smith J.A. concurring):] . . . while [the judge, in awarding substantial indemnity costs,] indicated he was not awarding solicitor-and-client costs, there is not a sufficient distinction between substantial indemnity costs and solicitor-and-client costs. An award approaching solicitor-and-client costs is still a punitive order and, as there is no authority for the awarding of substantial indemnity costs, relies upon the same jurisprudential base as solicitor-and-client costs.

APPEAL by creditor from judgment reported at *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.* (2007), 2007 SKQB 121, 2007 CarswellSask 157, 33 C.B.R. (5th) 39 (Sask. Q.B.) dismissing application to lift stay against debtor under Companies Creditors' Arrangement Act, and from judgment reported at *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.* (2007), 2007 SKQB 144, 2007 CarswellSask 264, 33 C.B.R. (5th) 46 (Sask. Q.B.) ordering costs against creditor.

***Jackson J.A.*:**

**I. Introduction**

1 This appeal concerns a claim arising on a "post-filing" basis after a restructuring order had been made under the *Companies' Creditors Arrangement Act* [1] (the "*CCAA*"). The restructuring failed. The principal assets of the companies have been sold and the net proceeds are being held for distribution. The post-filing claim is asserted against: (i) the companies, which are subject to the *CCAA* order; and (ii) against the companies' Chief Restructuring Officer.

  

2 The post-filing claimant is ICR Commercial Real Estate (Regina) Ltd. ("ICR"). ICR claims a real estate commission with respect to the sale of a building belonging to Bricore Land Group Ltd. Bricore Land and four related companies (collectively "Bricore") are all subject to an initial order ("Initial Order") granted by Koch J. on January 4, 2006 pursuant to s. 11(3) of the *CCAA*. The Chief Restructuring Officer, Maurice Duval (the "CRO"), was appointed by Koch J. on May 23, 2006 (the "CRO Order"). Koch J. has been the supervising *CCAA* judge since the Initial Order.

3 The Initial Order and the CRO Order impose the usual stay of proceedings against Bricore and prohibit the commencement of new actions against Bricore and the CRO, without leave of the Court.

4 ICR applied to Koch J. for directions and, in the alternative, for leave to commence actions against Bricore and the CRO. By fiats dated April 9, 2007 and April 25, 2007, Koch J. held that the Initial Order and the CRO Order prohibiting the commencement of actions apply to ICR and that leave of the Court is required. He refused leave and also awarded substantial indemnity costs against ICR.

5 On May 23, 2007, ICR applied in Court of Appeal chambers for leave to appeal, pursuant to s. 13 of the *CCAA*, and received leave to appeal the same day. The appeal was heard on June 7, 2007 and dismissed in relation to the lifting of the stay application and allowed in relation to the costs order on June 13, 2007, with reasons to follow. These are those reasons.

**II. Issues**

6 The issues are:

> 1. Does the stay of proceedings imposed by the supervising *CCAA* judge J. under the Initial Order apply to an action commenced by ICR, a post-filing claimant, such that leave to commence an action against Bricore is required?
>
> 2. Does s. 11.3 of the *CCAA* mean that a post-filing claimant cannot be subject to the stay of proceedings imposed by the Initial Order?
>
> 3. If leave is required, did the supervising *CCAA* judge commit a reviewable error in refusing ICR leave to commence an action against Bricore?
>
> 4. Did the supervising *CCAA* judge make a reviewable error in refusing leave to commence an action against the CRO?
>
> 5. Did the supervising *CCAA* judge err in awarding costs on a substantial indemnity basis?

**III. Background**

7 ICR's claim to a real estate commission arises as a result of these brief facts. Bricore owned four commercial real estate properties in Saskatoon and three such properties in Regina (the "Bricore Properties"). ICR argued that it had marketed one of the Regina properties, known as the Department of Education Building (the "Building"), to the City of Regina.

8 Bricore sold the Building, at a purchase price of $700,000,[2] to a proposed purchaser, which assigned its interest to 101086849 Saskatchewan Ltd. 101086849 Saskatchewan in its turn sold the Building to the City of Regina for a price of $1,075,000.[3] The certificate of title to the Building issued in early January, 2007 to 101086849 Saskatchewan, and the certificate of title issued to the City of Regina in late January, 2007. The Building came to be sold pursuant to a series of Court Orders made by Koch J., which I will now summarize.

9 As I have indicated, the Initial Order was made on January 4, 2006. On February 13, 2006 Koch J. appointed CMN Calgary Inc. as an Officer of the Court to pursue opportunities and to solicit offers for the sale or refinancing of the Bricore Properties. He also authorized Bricore to enter into an agreement with CMN Calgary dated as of January 30, 2006 entitled "Exclusive Authority To Solicit Offers To Purchase."

  

10 In May 2006, it was determined that Bricore could not be reorganized and, therefore, all the Bricore Properties should be sold. On May 23, 2006, Koch J. appointed Maurice Duval, C.A., of Saskatoon, Saskatchewan as an officer of the Court to act as CRO, and to assist with the sale of the assets.

11 The CRO Order confers these powers on the CRO pertaining to the proposed sale of the Bricore Properties:

> 7 ...
>
> (e) subject to the stay of proceedings in effect in these proceedings, the power to take steps for the preservation and protection of the Bricore Properties, including, without restricting the generality of the foregoing, (i) the right to make payments to persons, if any, having charges or encumbrances on the Bricore Properties or any part or parts thereof on or after the date of this Order, which payments shall include payments in respect of realty taxes owing in respect of any of the Bricore Properties, (ii) the right to make repairs and improvements to the Bricore Properties or any parts thereof and (iii) the right to make payments for ongoing services in respect of the Bricore Properties;
>
> . . . . .
>
> (g) subject to paragraphs 7C, 7D and 7E hereof, **the power to work with, consult with and assist the court-appointed selling officer (CMN Calgary Inc.) to negotiate with parties who make offers to purchase** the Bricore Properties in a manner substantially in accordance with the process and proposed timeline for solicitation of such offers to purchase the Bricore Properties recommended by the Monitor in the Monitor's Third Report. ... [4] [Emphasis added.]

12 On June 19, 2006, Koch J. authorized the CRO to accept an offer to purchase the Bricore Properties, including the Building, made by an undisclosed purchaser (the "Proposed Purchaser"), which offer to purchase was filed with the Court and temporarily sealed. The order directed that any further negotiations between the CRO and the Proposed Purchaser were to be completed by August 1, 2006.

13 Negotiations were protracted resulting in a further series of orders:

> (a) August 1, 2006: Koch J. extended the timeframe for due diligence and further negotiations to be completed by August 15, 2006; [5]
>
> (b) August 18, 2006: Koch J. authorized the CRO to accept an Amended Offer to Purchase made the 15th day of August, 2006. The Amended Offer to Purchase contemplated the sale by Bricore to the Proposed Purchaser of six of the seven Bricore Properties including the Building; [6]
>
> (c) September 25, 2006: The closing date for the proposed sale by Bricore to the Proposed Purchaser of the six properties was extended from October 15, 2006 to November 15, 2006; [7]
>
> (d) October 10, 2006: Koch J. approved the sale of the six properties to their respective purchasers; in the case of the Building, it was sold to 101086849 Saskatchewan Ltd. [8]

Koch J. ultimately approved the sale of the Building to 101086849 Saskatchewan Ltd. as of November 30, 2006.

14 ICR said it had introduced the City of Regina to the opportunity to purchase the Building and it was therefore entitled to a real estate commission based on the sale price to the City of Regina. Once its claim was denied by the Monitor, ICR applied to Koch J. on March 22, 2007 contending that (a) "prior Orders of this Court requiring leave to commence action" against Bricore and the CRO "do not apply in the circumstances"; and (b) in the alternative, "it is entitled to an order granting leave to commence the proposed proceedings." In support of its notice of motion, ICR filed a draft statement of claim and a supporting affidavit with exhibits.

  

15 This is the substance of ICR's draft statement of claim against Bricore and the CRO:

> 4. At all material times Duval's actions in relation to the matters in issue in the within proceedings were carried out in his capacity as chief restructuring officer for the Bricore Group.
>
> . . . . .
>
> 7. Duval, pursuant to Order of the Court under the *Companies' Creditors Arrangement Act*, was authorized in accordance in such order to market various assets of the Bricore Group, including the [Building]. [sic]
>
> 8. In the course of his efforts to market the [Building], Duval enlisted the aid of the plaintiff and its commercial realtors, licensed as brokers under *The Real Estate Act*.
>
> 9. The plaintiff, in its efforts to market the properties of the Bricore Group under the direction of Duval, including the [Building], introduced a prospective purchaser to Duval, namely the City of Regina.
>
> 10. By agreement dated September 27, 2006 made between the Plaintiff, the Bricore Group and Duval, it was agreed that the Plaintiff would be protected as the agent of record to a commission for the sale of any of the Bricore Group Properties for which the Plaintiff had located a purchaser.
>
> 11. The Plaintiff says that at the time of execution of the said Agreement by Duval on September 28, 2006, the City of Regina was in the process of doing its "due diligence" on the [Building] and it was expected that a sale of the [Building] to the City of Regina would be completed in the near future.
>
> 12. The Plaintiff says that, contrary to the Agreement entered into between the Plaintiff and the Defendants, Duval, **without the Plaintiff's knowledge and in bad faith**, proceeded to arrange to sell the [Building] to a third party, namely 101086849 Saskatchewan ltd., which became the owner of the [Building] on or about January 3, 2007. [9] [Emphasis added.]

16 While the words "bad faith" are not repeated in the affidavit evidence, Paul Mehlsen, the principal of ICR, swore an affidavit in support of the application for leave, stating that he had examined the statement of claim and that to the best of his knowledge the allegations contained therein are true. His affidavit also states:

> 13. Insofar as the attached letter states that "ICR is protected as agent of record", this is commonly understood in the industry as meaning that in the event a sale of the property took place in the protected period to a purchaser introduced by the agent of record, then they would receive the usual commission for such sale, which in this case would be 5%.
>
> 14. It would appear from the attached exhibit "A" that Larry Ruf arranged to have the Respondent, Maurice Duval, agree to the arrangement, as well as adding that the protection would extend to the closing of any sale or December 31, 2006, whichever was the earlier.
>
> 15. Attached hereto and marked as exhibit "B" to this my Affidavit is a true copy of an email dated October 31, 2006 from Larry Ruf to Evan Hubick, Jim Kambeitz and Jim Thompson of the proposed plaintiff, ICR. Such email states in part:
>
> > I can confirm, on behalf of the CRO, that protection for the potential deals referenced in your letter of September 27, 2006 will be honoured to November 30, 2006. [10]

17 Exhibit "A" is a letter dated September 27, 2006 from Mr. Jim Thompson of ICR to Mr. Larry Ruf of Horizon West Management Inc. It reads, in material part, as follows:

> Please be advised that we have had ongoing discussions with potential buyers and tenants as follows:
>
> > 1. 1500 — 4th Avenue [Department of Education Building] — we have been in regular contact with the City of Regina Real Estate Department for over a year regarding the possibility of this site being acquired by the City. In July a large contingent of City employees including a number from the Works and Engineering Department toured the building

  

> over several hours. We have had continuous follow up with a Real Estate Department official who confirmed recently that there still is an interest in the property and officials are in the due diligence stage. In addition, we have exposed the property to Alfords Furniture and Flooring who have an ongoing interest.
>
> . . . . .
>
> The purpose of this memo is to reinforce our ongoing efforts to market and represent the Bricore assets in Regina. We are aware that the properties are under contract to sell and request that ICR be protected in the specific situations as outlined.
>
> In the event we are not able to carry on in a formal fashion we would ask that you sign where indicated to acknowledge that ICR is protected as the agent of record for the Tenants/Buyers noted herein for a period to extend to December 31, 2006. [11]

The words "December 31, 2006" are struck out and these words are added: "Date of closing of a sale or December 31, 2006 whichever is earlier." Mr. Ruf's name is crossed out and the signature of Maurice Duval, Chief Restructuring Officer is added in its place.

18 Mr. Ruf, on behalf of Bricore, refuted ICR's claim in a sworn affidavit stating:

> 3. At no time did I approach ICR Regina in 2006 to initiate discussions regarding the sale or lease of the Department of Education Building.
>
> 4. I received two or three unsolicited telephone calls regarding the Department of Education Building in September of 2006 from representatives of ICR Regina (including Paul Mehlsen, Jim Kambeitz and Evan Hubick). During those calls, representatives of ICR Regina informed me that they knew of certain parties who would be interested in purchasing the Department of Education Building. In response to each of these inquiries, I informed representatives of ICR:
>
> > (a) that I had no authority to participate in communications regarding a sale of the Department of Education Building, and that all such inquiries should be directed to Maurice Duval, the court-appointed Chief Restructuring Officer of Bricore Group; and
> >
> > (b) that further information on the status of the restructuring of Bricore Group could be obtained on the website of MLT. [12]

19 The CRO filed a report in response to ICR:

> 6. At the time of my review of the September 27, 2006 letter from ICR Regina, I was working very hard to attempt to negotiate and conclude the final closing of the sale of the Bricore Properties to the purchasers identified in the Accepted Offer to Purchase. I fully expected that sale to close (as it ultimately did effective November 30, 2006). However, I determined that, in the event that such sale failed to close, Bricore Group would need to identify other potential purchasers of the Bricore Properties very quickly. I therefore decided that it would be appropriate for Bricore Group, by the CRO, to agree to protect ICR Regina for a commission in the unlikely event that the sale contemplated by the Accepted Offer to Purchase did not close, and it subsequently became necessary for Bricore Group instead to conclude a sale of the Bricore Properties to one or more of the prospective purchasers of the three Bricore Properties located in Regina (as specifically identified in Mr. Thompson's September 27, 2006 letter). For that reason, and that reason only, I agreed to sign the September 27, 2006 letter.
>
> 7. In signing the September 27, 2006 letter, my intention, as court-appointed CRO of Bricore Group, was to strike an agreement that, in the unlikely event that:
>
> > (a) the sale of the Bricore Properties identified in the Accepted Offer to Purchase fell apart; and
> >
> > (b) it subsequently became necessary for Bricore Group to sell the Bricore Properties to one or more of the prospective purchasers identified in the September 27, 2006 letter;

  

then Bricore Group would agree to pay a commission to ICR Regina. In regard to the Department of Education Building located at 1500 — 4th Avenue in Regina (the "Department of Education Building"), the two prospective purchasers in respect of which ICR Regina was protected for a commission were the City of Regina and Alford's Furniture and Flooring. The reference to closing date was to the closing of the Avenue Sale, which occurred effective November 30, 2006.

8. In January of 2007, after much effort and expenditure of resources, the sale of the Bricore Properties contemplated in the Accepted Offer to Purchase was unconditionally closed (effective November 30, 2006). The entity named as purchaser of the Department of Education Building in the final closing documents was a numbered Saskatchewan company controlled by Avenue Commercial Group of Calgary. Such entity was a nominee corporation operating entirely at arm's length from the City of Regina and Bricore Group. At all times after June 2006, the CRO had no authority to sell the property, as it was already sold.

9. It was subsequently brought to my attention that the numbered company which purchased the Department of Education Building had promptly "flipped" such property to the City of Regina. I knew nothing of such a proposed flip prior to learning of it from ICR Regina. [13]

20 To rebut this, Mr. Mehlsen of ICR swore a further affidavit deposing:

3. As indicated in my Affidavit sworn March 22, 2007, ICR had an ongoing relationship with the Bricore Companies prior to 2006. This relationship continued after the Initial Order in January 2006 in that ICR continued to show Bricore Properties for lease or sale, including the [Building].

4. Attached hereto and marked as Exhibit E to this my Affidavit is a true copy of an e-mail from my contact at the City of Regina ... dated April 13, 2006 advising that the City was interested in purchasing the [Building].

5. I immediately passed this information along to Larry Ruf, as evidenced in the e-mail dated April 13, 2006 attached hereto and marked as Exhibit "F" to this my affidavit.

6. In reply to paras. 2 and 12 of Mr. Duval's Report, it was not known to ICR that all of the Bricore Properties were sold as claimed; rather, it was known that some of the Bricore Properties had been sold, but not the subject property, [the Building], as it was the "ugly duckling" of the Bricore Properties and therefore had been excluded from the reported sale. ICR's efforts were directed at the sale of [the Building] and leasing the other two Regina properties.

7. In response to para. 13 of Mr. Duval's Report, it is true that there were no direct communications between ICR and Mr. Duval as all communications were with Larry Ruf, who indicated that he acted under the authority and with the knowledge of Mr. Duval.

8. As a result of contact in early summer with Mr. Ruf, ICR actively marketed the [Building] by placing signage on the property, developing an "information" or "fact" sheet detailing aspects of the building, and showed the property to the City of Regina and other prospective purchasers.

. . . . .

11. Because of delays on the part of the City of Regina in its due diligence and the fact that ICR has been working without any formal agreement, I caused the letter of September 27, 2006 (exhibit "A" to my Affidavit sworn March 22, 2007) to be sent.

12. At no time did either Mr. Ruf or Mr. Duval advise that the [Building] was sold and that ICR's role was merely that of a "backup offer". The signed letter of September 27, 2006 and Mr. Ruf 's e-mail of October 31, 2006 make no mention of these events and this was never disclosed to myself or ICR.

. . . . .

14. In hindsight, it would appear that the confidential information concerning the intention of the City of Regina to purchase the [Building] that was provided by myself and representatives of ICR to Mr. Ruf and Mr. Duval was communicated to

  

the [Proposed Purchaser], who then incorporated 101086849 Saskatchewan Ltd. to take advantage of this opportunity. Attached hereto and marked as exhibit "I" to this my Affidavit is a true copy of a Profile Report from the Corporate Registry indicating that 101086849 Saskatchewan Ltd. was incorporated by solicitors as a "shelf company" on May 31, 2006, with new Directors in the form of Garry Bobke and Steven Butt taking office on August 17, 2006.

15. My understanding is that the [Proposed Purchaser] initially excluded the [Building] from their offer to purchase the Bricore Group properties and made a separate offer through 101086849 Saskatchewan Ltd. when they were made aware of the confidential information about the City of Regina's plans to purchase the property. [14]

21 In refusing ICR leave to commence action, Koch J. wrote:

[1] On January 4, 2006, I granted an initial order pursuant to the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, (the "*CCAA*") protecting the respondent corporations Bricore Land Group Ltd. et al. (collectively "Bricore"), from claims of their respective creditors. The order (paragraph 5) explicitly provides in accordance with the authority conferred upon the Court pursuant to s. 11(3) of the *CCAA* that "no Person shall commence or continue any Enforcement or Proceeding of any kind against or in respect of Bricore Group or the Property". The initial period of 30 days has been extended many times. The stay of proceedings continues in effect. Ernst & Young Inc. was appointed monitor. That appointment continues.

. . . . .

[16] Although the interpretation of s. 11.3 of the *CCAA* is not necessarily well settled in all aspects, it appears that the import of s. 11.3, which was introduced as an amendment to the Act in 1997, is this:

> (a) An application to lift a stay of proceedings must be addressed in the context of the broad objectives of the *CCAA* which is to promote re-organization and restructuring of companies. If s. 11.3 is interpreted too literally, it can render the stay provisions ineffective, leaving the collective good of the restructuring process subservient to the self-interest of a single creditor. Clearly, s. 11.3 must be construed so as not to defeat the overall objectives of the Act. See *Smith Brothers Contracting Ltd. (Re)* (1998), 53 B.C.L.R. (3d) 264 (B.C.S.C.).
>
> (b) The standard for determining whether to lift the stay of proceedings is not, as ICR contends, whether the action is frivolous, analogous to the standard which a defendant applicant under Rule 173 of *The Queen's Bench Rules* must meet to set aside a statement of claim. Rather, to obtain an order lifting the stay ad hoc to permit the suit to proceed, the proposed plaintiff must establish that the cause of action is tenable. I interpret that to mean that the proposed plaintiff has a *prima facie* case. See *Ivaco Inc. (Re)*, [2006] O.J. No. 5029 (Ont. S.C.J.).
>
> (c) In determining whether to lift a stay, the Court must take into consideration the relative prejudice to the parties. See *Ivaco, Inc. (Re)*, *supra*, para. 20; and Richard H. McLaren & Sabrina Gherbaz, *Canadian Commercial Reorganization: Preventing Bankruptcy* (Toronto: Canada Law Book, 1995) at 3-18.1. Counsel have cited the case of *GMAC Commercial Credit Corporation — Canada v. T.C.T. Logistics Inc*., [2006] 2 S.C.R. 123, 2006 SCC 35. The circumstances in that case are somewhat analogous but it is of limited assistance because the *CCAA* does not contain a provision equivalent to s. 215 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, which expressly provides that no action lies against the superintendent, an official receiver, an interim receiver or a trustee in certain circumstances without leave of the Court.

[17] For reasons outlined *supra*, I do not find the cause of action ICR asserts against Bricore to be tenable, not even as against Bricore Land Group Ltd. Therefore, the application to lift the stay of proceedings to permit the proposed action against Bricore is dismissed.

[18] Neither is there any basis upon which to lift the stay with respect to the proposed action against Maurice Duval, the Chief Restructuring Officer. Considerations applicable to Bricore under s. 11.3 do not apply to a court-appointed restructuring officer. Maurice Duval, as an officer of the Court, has explained his position in a cogent way. I accept his explanation. He did not sell the Department of Education Building to the City of Regina. He was not aware at the relevant

  

time that the purchaser was going to resell. Indeed, his efforts were directed toward closing a single transaction involving all six Bricore properties. Although the proposed pleading accuses Mr. Duval of acting in "bad faith", it is not suggested on behalf of ICR that Mr. Duval has been guilty of fraud, gross negligence or wilful misconduct; that is, any of the limitations or exceptions expressly listed in paragraph 20(c) of the order of May 23, 2006.

[19] As stated previously, the overriding purpose of the *CCAA* must also be considered. That applies in the Duval situation too. The statute is intended to facilitate restructuring to serve the public interest. In many cases such as the present it is necessary for the Court to appoint officers whose expertise is required to fulfill its mandate. It is clearly in the public interest that capable people be willing to accept such assignments. It is to be expected that such acceptance be contingent on protective provisions such as are included in the order of May 23, 2006, appointing Mr. Duval. It is important that the Court exercise caution in removing such restrictions; otherwise, the ability of the Court to obtain the assistance of needed experts will necessarily be impaired. Qualified professionals will be less willing to accept assignments absent the protection provisions in the appointing order. [15]

**IV. Issue #1: Does the Stay of Proceedings Imposed by the Supervising CCAA Judge under the Initial Order Apply to an Action Commenced by ICR, a Post-Filing Claimant, Such That Leave to Commence an Action Against Bricore Is Required?**

22 ICR argues that, as a post-filing creditor, the Initial Order does not apply to it, either as a matter of law or on the basis of a proper interpretation of the Initial Order.

23 The authority to make an order staying and prohibiting proceedings against a debtor company is contained in s. 11(3) of the *CCAA*:

11. (3) A court may, on an initial application in respect of a company, make an order on such terms as it may impose, effective for such period as the court deems necessary not exceeding thirty days,

(a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

24 Pursuant to s. 11(3) of the *CCAA*, Koch J. granted the Initial Order providing for a stay and prohibition of new proceedings in these terms:

5. During the 30-day period from and after the date of filing of this application on January 4, 2006 or during the period of any extension of such 30-day period granted by further order of the Court (the "Stay Period"), no Person shall commence or continue any Enforcement or Proceeding of any kind against or in respect of Bricore Group or the Property. Any and all Enforcement or Proceedings already commenced (as at the date of this Order) against or in respect of Bricore Group or the Property are hereby stayed and suspended.

6. During the Stay Period, no person shall assert, invoke, rely upon, exercise or attempt to assert, invoke, rely upon or exercise any rights:

a) against Bricore Group or the Property;

b) as a result of any default or non-performance by Bricore Group, the making or filing of this proceeding or any admission or evidence in this proceeding, or

  

> c) in respect of any action taken by Bricore Group or in respect of any of the Property under, pursuant to or in furtherance of this Order.
>
> . . . . .
>
> 11. Notwithstanding any of the provisions of this Order:
>
> a) no creditor of Bricore Group shall be under any obligation, by reason only of the issuance of this Order, to advance or re-advance any monies or otherwise extend any credit to Bricore Group, except as such creditor may agree; and
>
> b) Bricore Group may, by written consent of its counsel of record, agree to waive any of the protections that this Order provides to them, whether such waiver is given in respect of a single creditor or class of creditors or is given in respect of all creditors generally.
>
> . . . . .
>
> 13. Any act or action taken or notice given by creditors or other Persons or their agents, from and after 12:01 a.m. (local Saskatoon time) on the date of the filing of the application for this Order to the time of the granting of this Order, to commence or continue Enforcement or to take any Proceeding (including, without limitation, the application of funds in reduction of any debt, set-off or the consolidation of accounts) is, unless the Court orders otherwise, deemed not to have been taken or given.

"Proceeding" is defined in para. 22 of Schedule "A" to the Initial Order as "a lawsuit, legal action, court application, arbitration, hearing, mediation process, enforcement process, grievance, extrajudicial proceeding of any kind or other proceeding of any kind."

25 The authority to extend an initial order is contained in s. 11(4) of the *CCAA:*

> 11(4) A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose,
>
> (a) staying, until otherwise ordered by the court, for such period as the court deems necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);
>
> (b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
>
> (c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

Koch J., pursuant to this subsection, extended the stay many times and the stay continues in force.

26 As authority for the proposition that the Initial Order does not stay proceedings with respect to claims that arise after the Initial Order, ICR's counsel cites Professor Honsberger's *Debt Restructuring Principles & Practice*:

> The scope of an order staying proceedings extends only to claims that arose prior to the order. A proceeding based on a claim that arose after an order was made staying proceedings is not affected by the stay. [16] [Footnote omitted.]

The only case footnoted is *Ramsay Plate Glass Co. v. Modern Wood Products Ltd.* [17] In my respectful view, the facts in *Ramsay Plate Glass* narrow its application.

27 In *Ramsay Plate Glass Co.*, the initial *CCAA* order, dated April 12, 1951, suspended all proceedings against Modern Wood Products Ltd. Modern Wood Products made an offer of compromise that was accepted by its existing creditors and approved by the Court on May 21, 1951. Ramsay Glass sought to enforce a claim against Modern Wood Products that arose in 1953. Modern Wood Products sought to strike Ramsay Glass's claim on the basis that its proceedings were stayed by the April 1951 order.

  

28 In dismissing the application to strike, Prevost J. wrote:

> CONSIDERING that said claim is not provable in bankruptcy and that under *The Bankruptcy Act* an order staying proceedings would not apply to such a claim: *Richardson & Co. v. Storey*, 23 C.B.R. 145, [1942] 1 D.L.R. 182, Abr. Con. 301; *In re Bolf*, 26 C.B.R. 149, [1945] Que. S.C. 173, Abr. Con. 303;
>
> CONSIDERING that s. 10 of *The Companies' Creditors Arrangement Act* and the judgments rendered under its authority should receive the same interpretation in this respect as s. 40 of *The Bankruptcy Act*;
>
> CONSIDERING that the present claim is in no way affected by the judgment rendered on April 12, 1951 by Boyer J. under *The Companies' Creditors Arrangement Act*, ordering suspension of all proceedings against defendant company the present claim being posterior to said date and having not been made the subject of any compromise or arrangement homologated by this Court;
>
> CONSIDERING that the present claim arose in 1953, two years after the judgment of Boyer J. homologating the compromise following the non-payment by defendant company of merchandise purchased by it from plaintiff company during said year; [18]

I do not interpret *Ramsay Plate Glass* as permitting a post-filing claimant to commence an action against a debtor company without obtaining leave while the *CCAA* stay is in effect. In my opinion, *Ramsay Plate Glass* can be read as authority for the proposition that a post-filing creditor need not apply for leave after the stay has been lifted. In that respect, it parallels *360networks Inc., Re*; [19] *Stelco Inc., Re*; [20] and *Campeau v. Olympia & York Developments Ltd.* [21]

29 In *360networks*, a creditor (Caterpillar Financial Services Limited) had both pre-filing and post-filing claims. Caterpillar applied, *inter alia*, for an order lifting the stay of proceedings. Tysoe J. wrote:

> 8 On the hearing of the applications, Caterpillar continued to take the position that all of its claims could properly be determined within the *CCAA* proceedings on the first of its two applications. I agree that the Deficiency Claim and the Secured Creditor Claim are properly determinable within the *CCAA* proceedings, but it is my view that it would not be appropriate to make determinations in respect of the Trust Claim or the Post-Filing Claim in the *CCAA* proceedings. The only remaining thing to be done in the *CCAA* proceedings is the determination of the validity of claims for the purposes of the Restructuring Plan (with Caterpillar's claims being the only unresolved ones). **Neither the Trust Claim nor the Post-Filing Claim falls into this category of claim because each of these types of claim is not affected by the Restructuring Plan.** Indeed, the Post-Filing Claim was not asserted in Caterpillar's proof of claim and surely cannot be adjudicated upon within Caterpillar's appeal of the disallowance of its proof of claim. The B.C. Court of Appeal has recently affirmed, in *United Properties Ltd. v. 642433 B.C. Ltd.*, 2003 BCCA 203 (B.C.C.A.), that it is appropriate for the court to decline jurisdiction to resolve a dispute in *CCAA* proceedings which, although it may relate to them, is not part and parcel of the proceedings. [Emphasis added.]
>
> . . . . .
>
> 11 Counsel for Caterpillar relies for the first ground on the fact that s. 12 of the *CCAA* authorizes the court to deal with secured and unsecured claims. However, s. 12 deals with the determination of claims for the purposes of the CCAA and does not authorize the court to determine claims which fall outside of *CCAA* proceedings, such as the Trust Claim and the Post-Filing Claim. [22]

In the result, Tysoe J. lifted the stay so as to permit an action to be commenced to resolve all of Caterpillar's claims. The significance of the decision for our purposes is that the Court in *360networks* considered the stay as applying to claims that arose after the initial order.

30 In *Stelco*, Farley J., relying on *360networks*, also held that the post-filing creditor's claim in that case "continues to be stayed and is to be dealt with in the ordinary course of litigation after Stelco's *CCAA* protection is terminated." [23]

  

31 *Campeau* does not deal with a post-filing creditor, but it does address the situation where a creditor, whose claim is not accepted as part of the plan of arrangement, wants to commence action. Blair J. (as he then was) refused an application brought by Robert Campeau and the Campeau Corporations to lift the stay of proceeding imposed by the initial order. In doing so, he wrote:

> 24. In making these orders, I see no prejudice to the Campeau plaintiffs. The processing of their action is not being precluded, but merely postponed. Their claims may, indeed, be addressed more expeditiously than might have otherwise been the case, as they may be dealt with — at least for the purposes of that proceeding — in the C.C.A.A. proceeding itself. On the other hand, there might be great prejudice to Olympia & York if its attention is diverted from the corporate restructuring process and it is required to expend time and energy in defending an action of the complexity and dimension of this one. While there may not be a great deal of prejudice to National Bank in allowing the action to proceed against it, I am satisfied that there is little likelihood of the action proceeding very far or very effectively unless and until Olympia & York — whose alleged misdeeds are the real focal point of the attack on both sets of defendants — is able to participate.
>
> 25 In addition to the foregoing, I have considered the following factors in the exercise of my discretion:
>
> > 1. Counsel for the plaintiffs argued that the Campeau claim must be dealt with, either in the action or in the C.C.A.A. proceedings and that it cannot simply be ignored. I agree. However, in my view, it is more appropriate, and in fact is essential, that the claim be addressed within the parameters of the C.C.A.A. proceedings rather than outside, in order to maintain the integrity of those proceedings. Were it otherwise, the numerous creditors in that mammoth proceeding would have no effective way of assessing the weight to be given to the Campeau claim in determining their approach to the acceptance or rejection of the Olympia & York Plan filed under the Act.
> >
> > 2. In this sense, the Campeau claim — like other secured, undersecured, unsecured, and contingent claims — must be dealt with as part of a "controlled stream" of claims that are being negotiated with a view to facilitating a compromise and arrangement between Olympia & York and its creditors. In weighing "the good management" of the two sets of proceedings — i.e. the action and the CCAA proceeding — the scales tip in favour of dealing with the Campeau claim in the context of the latter: see *Attorney General v. Arthur Andersen & Co.* (United Kingdom) (1988), [1989] E.C.C. 224 (C.A.), cited in *Arab Monetary Fund v. Hashim, supra.*
>
> **I am aware, when saying this, that in the initial plan of compromise and arrangement filed by the applicants with the court on August 21, 1992, the applicants have chosen to include the Campeau plaintiffs amongst those described as "Persons not Affected by the Plan".** This treatment does not change the issues, in my view, as it is up to the applicants to decide how they wish to deal with that group of "creditors" in presenting their plan, and up to the other creditors to decide whether they will accept such treatment. In either case, the matter is being dealt with, as it should be, within the context of the C.C.A.A. proceedings. [24] [Emphasis added.]

*Campeau* is further authority for the proposition that a supervising *CCAA* judge can refuse a prospective creditor, who is not part of the plan of arrangement, leave to commence proceedings and that the creditor may commence action after the stay is lifted.

32 Each of *360networks* [25], *Stelco* [26] and *Campeau* [27] supports the proposition that while a stay of proceedings is extant, an application to lift the stay must be made to permit an action to be commenced against a debtor that is subject to a *CCAA* order, regardless of whether the claim arises before or after the initial order, or whether the prospective creditor is able to take part in the plan of arrangement.

33 Prevost J. in *Ramsay Plate Glass* points out that under the *Bankruptcy and Insolvency Act* [28] (*the* "*BIA*") the stay of proceedings does not extend to a claim not provable in bankruptcy. This is so, however, because of the definition of "claim provable in bankruptcy" and ss. 69.3(1) and s. 121. (See Houlden & Morawetz, *The 2007 Annotated Bankruptcy and Insolvency Act.* [29]) While s. 12 of the *CCAA* defines "claim" by reference to "claim provable in bankruptcy," it has not been interpreted as limiting the extent of the stay.

  

34 On the face of ss. 11(3) and (4) of the *CCAA*, the authority to safeguard the company is not limited to staying existing actions, but extends to "prohibiting, until otherwise ordered by the court, the commencement of ... any other action, suit or proceeding against the company." Unlike the *BIA* there are no words limiting this phrase to debts or claims in existence at the time of the initial order.

35 With respect to the wording of the Initial Order, there can be no question that it applies to post-filing creditors. The broad wording of paras. 5 and 6 of the Initial Order and the definition of "proceeding" confirm this. No distinction is made between creditors in existence at the time of the Initial Order and those who become creditors after. Paragraph 11(b) also establishes a mechanism for post-filing creditors to seek relief by obtaining an exemption from the protection afforded Bricore, which would include the prohibition of proceedings. The obvious implication is that the prohibition of proceedings applies to post-filing creditors, subject, of course, to obtaining leave of the Court to commence action.

**V. Issue #2. Does s. 11.3 of the CCAA Mean That a Post-Filing Claimant Cannot Be Subject to the Stay of Proceedings Imposed by the Initial Order?**

36 ICR argued that by the addition of s. 11.3 in 1997 [30] to the *CCAA*, Parliament intended to grant a post-filing creditor the right to sue without obtaining leave.

37 In my respectful view, s. 11.3 cannot be interpreted in the way in which ICR contends. Indeed, a more logical and internally consistent reading of s. 11.3 and the other sections of the *CCAA* is to permit the supervising judge to determine, as a matter of discretion, whether an action commenced by a post-filing creditor should be permitted to proceed.

38 Section 11.3 forms part of a comprehensive series of sections addressing the question of stays added in 1997 and 2001: [31]

> **No stay, etc., in certain cases**
>
> 11.1 (2) No order may be made under this Act **staying or restraining** the exercise of any right to terminate, amend or claim any accelerated payment under an eligible financial contract or preventing a member of the Canadian Payments Association established by the *Canadian Payments Act* from ceasing to act as a clearing agent or group clearer for a company in accordance with that Act and the by-laws and rules of that Association. (Added by S.C.1997, c. 12, s. 124)
>
> **No stay, etc., in certain cases**
>
> 11.11 No order may be made under this Act **staying or restraining**
>
> > (a) the exercise by the Minister of Finance or the Superintendent of Financial Institutions of any power, duty or function assigned to them by the *Bank Act*, the *Cooperative Credit Associations Act*, the *Insurance Companies Act* or the *Trust and Loan Companies Act*;
> >
> > (b) the exercise by the Governor in Council, the Minister of Finance or the Canada Deposit Insurance Corporation of any power, duty or function assigned to them by the *Canada Deposit Insurance Corporation Act*; or
> >
> > (c) the exercise by the Attorney General of Canada of any power, assigned to him or her by the *Winding-up and Restructuring Act*. (Added by S.C. 2001, c. 9, s. 577.)
>
> **No stay, etc. in certain cases**
>
> 11.2 No order may be made under section 11 **staying or restraining any action, suit or proceeding** against a person, other than a debtor company in respect of which an application has been made under this Act, who is obligated under a letter of credit or guarantee in relation to the company. (Added by S.C.1997, c. 12, s. 124)
>
> 11.3 No order made under section 11 shall have the effect of

  

> (a) prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration provided after the order is made; or
>
> (b) requiring the further advance of money or credit. (Added by S.C.1997, c. 12, s. 124)

[Emphasis added.]

39 In ss. 11.1(2), 11.11 and 11.2, Parliament uses the words "staying or restraining" to describe those circumstances limiting the scope of the stay power, but these words are not repeated in s. 11.3. This application of the *expressio unius* principle supports the obvious implication that s. 11.3 does not limit the authority of the court to stay all proceedings.

40 While the debates of the House of Commons in Hansard do not comment on s. 11.3, several text book authors assist with the task of interpretation. Professor Honsberger states:

> A distinction is made between the compulsory supply of goods and services and the extension of credit by suppliers to a debtor company in CCAA proceedings.
>
> Suppliers may be enjoined from cutting off services or discontinuing the supply of goods by reason of there being arrears of payment provided the debtor commences regular payments for current deliveries.
>
> However, no order made under s. 11 of the Act has the effect of prohibiting a person from requiring immediate payment for goods, services, use of leased or licensed property or other valuable consideration after the order is made.
>
> . . . . .
>
> ... A court could make a similar order after the 1997 amendments provided it stipulated that the debtor company made immediate payment for goods, services, use of leased or licensed property or other valuable consideration after the order is made. [32]
>
> [Footnotes omitted.]

41 Professor McLaren similarly comments in his text "Canadian Commercial Reorganization": [33]

> 3.800 ... Section 11.3 acts as an exemption to the stay provisions of s. 11 of the CCAA. It appears the section is meant to balance the rights of creditors with debtors. The section addresses the concern that judges had too much discretion in issuing stays. Under s. 11.3(a), if a person supplies goods or services or if the debtor continues to occupy or use leased or licensed property, the court will not issue a stay order with respect to the payment for such goods or services or leased or licensed property. In essence, s. 11.3(a) will not permit the court to prohibit these individuals from demanding payment from the debtor for goods, services or use of leased property, after a court order is made.

42 Finally, Professor Sarra in *Rescue! The Companies' Creditors Arrangement Act* [34] provides this insight:

> While the court cannot compel a supplier to continue to extend credit to the debtor during a *CCAA* proceeding, the court can protect trade suppliers that choose to supply goods or credit during the stay period by granting them a charge on the assets of the debtor that will rank ahead of other claims. While section 11.3 of the *CCAA* states that no stay of proceedings can have the effect of prohibiting a person from requiring immediate payment for goods, services or the use of leased or licensed property, or requiring the further advance of money or credit, trade suppliers were often continuing credit only to find that they had lost further assets during the workout period because of their priority in the hierarchy of claims. Hence the practice of post-petition trade credit priority charges developed, first recognized in Alberta. [35] [Footnotes omitted.]

43 *Smith Brothers Contracting Ltd., Re* [36] also supports a narrow reading of s. 11.3. After citing *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* [37] and *Quintette Coal Ltd. v. Nippon Steel Corp.* [38] with respect to the intention of Parliament and the object and scheme of the *CCAA*, Bauman J. in *Smith Brothers* wrote:

  

45 It is interesting that Gibbs J.A. suggested that it would be unlikely that a court would exercise its s. 11 jurisdiction:

> ... where the result would be to enforce the continued supply of goods and services to the debtor company without payment for current deliveries ...

46 Parliament has now precluded that by adding s. 11.3(a) to the CCAA. It is instructive to note, however, that the subsection has been added against the backdrop of jurisprudence which has underlined the very broad scope of the court's jurisdiction to stay proceedings under s. 11.

47 To repeat the relevant portion of the section:

> 11.3 No order made under s. 11 shall have the effect of
>
> > (a) prohibiting a person from requiring immediate payment for ... use of leased or licenced property ... provided after the order is made;

It is noted that the remedy which is preserved for creditors is a relatively narrow one; it is the right to require immediate payment for the use of the leased property. [39]

Thus, Bauman J. interpreted s. 11.3 in accordance with Parliament's intention and the object and scheme of the C*CAA* as creating a narrow right — the right to withhold services without immediate payment.

44 I agree with Bricore's counsel. When a supplier is requested to provide goods or services on a post-filing basis to a company operating under a stay of proceedings imposed by the *CCAA*, s. 11.3 allows the supplier the right:

> (a) to refuse to supply any such goods or services at all;
>
> (b) to supply such goods or services on a "cash on demand" basis only;
>
> (c) to negotiate with the insolvent corporation for the amendment of the *CCAA* Order to create a post-filing supplier's charge on the assets of the insolvent corporation to secure the payment by the insolvent corporation of amounts owing by it to such post-filing suppliers; or
>
> (d) to take the risk of supplying goods or services on credit.

Where the Initial Order imposes a stay of proceedings and prohibits further proceedings, s. 11.3 does not permit the supplier of goods or services to sue without obtaining leave of the court to do so.

**VI. Issue #3: If Leave Is Required, Did the Supervising CCAA Judge Commit a Reviewable Error in Refusing ICR Leave to Commence an Action Against Bricore?**

45 Having determined that the stay and prohibition of proceedings applies to ICR, notwithstanding its status as a post-filing creditor, the next issue is whether Koch J. erred in refusing to lift the stay on the basis that the claim was not tenable.

46 The claim against Bricore is presumably against Bricore both in its own right and pursuant to its indemnification agreement with the CRO. Paragraph 18 of the CRO Order requires Bricore to indemnify the CRO:

> 18. Bricore Group shall indemnify and hold harmless the CRO from and against all costs (including, without limitation, defence costs), claims, charges, expenses, liabilities and obligations of any nature whatsoever incurred by the CRO that may arise as a result of any matter directly or indirectly relating to or pertaining to any one or more of:
>
> > (a) the CRO's position or involvement with Bricore Group;

  

(b) the CRO's administration of the management, operations and business and financial affairs of Bricore Group;

(c) any sale of all or part of the Property pursuant to these proceedings;

(d) any plan or plans of compromise or arrangement under the CCAA between Bricore Group and one or more classes of its creditors; and/or

(e) any action or proceeding to which the CRO may be made a party by reason of having taken over the management of the business of Bricore Group. [40]

47 The authority to lift the stay imposed by the Initial Order against Bricore is contained in s. 11(4) of the *CCAA*:

11(4) A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose,

. . . . .

(c) prohibiting, **until otherwise ordered by the court**, the commencement of or proceeding with any other action, suit or proceeding against the company. [Emphasis added.]

48 This is a discretionary power, which invokes the standard of appellate review stated as follows:

[22] ... [T]he function of an appellate court is not to exercise an independent discretion of its own. It must defer to the judge's exercise of his discretion and must not interfere with it merely on the ground that members of the appellate court would have exercised the discretion differently. The function of the appellate court is one of review only. It may set aside the judge's exercise of his discretion on the ground that it was based on a misunderstanding of the law or of the evidence before him or on an inference that particular facts existed or did not exist, which, although it was one that might legitimately have been drawn on the evidence that was before the judge, can be demonstrated to be wrong by further evidence that has become available by the time of the appeal, or on the ground that there has been a change of circumstances after the judge made his order. [41]

It is often expressed as permitting intervention where the judge acts arbitrarily, on a wrong principle, or on an erroneous view of the facts, or when the appeal court is satisfied that there is likely to be a failure of justice as a result of the refusal. See: *Martin v. Deutch* [42]

49 With respect to discretionary decisions made under the *CCAA*, there is a particular reluctance to intervene. The reluctance is justified on the basis of the specialization of the judges who have carriage of complex proceedings that are often replete with compromised solutions. [43] This does not mean that the Court of Appeal can turn a blind eye or permit an injustice, but it does provide the backdrop against which *CCAA* discretionary decisions are reviewed.

50 Unlike the *BIA*, [44] the *CCAA* contains no specific statutory test to provide guidance on the circumstances in which a *CCAA* stay of proceedings is to be lifted. Some guidance, nonetheless, can be found in the statute and in the jurisprudence.

51 Subsection 11(6) of the *CCAA* states:

11 (6) The court shall not make an order under subsection (3) or (4) unless

(a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and

(b) in the case of an order under subsection (4), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

  

While the reference to "order" in the opening clause "[t]he court shall not make an order under s. (3) or (4)" may very well be to the Initial Order and not to the order lifting the stay, s. 11(6) and, in particular, its legislative history, are also relevant to an application to lift the stay.

52 Subsection 11(6) was brought into effect in 1997 by Bill C-5, which enacted "An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act and the Income Tax Act." When Bill C-5 received third reading on October 23, 1996, s. 11(6) took this form:

> 11 (6) The court shall not make an order under subsection (3) or (4) unless
>
> (a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and
>
> (b) in the case of an order under subsection (4), the applicant also satisfies the court that:
>
> (i) the applicant has acted, and is acting, in good faith and with due diligence,
>
> (ii) a viable compromise or arrangement could likely be made in respect of the company, if the order being applied for were made, and
>
> (iii) no creditor would be materially prejudiced if the order being applied for were made.

After Bill C-5 received third reading, it was referred to the Standing Senate Committee on Banking, Trade and Commerce. [45] The Committee reported:

> A number of insolvency experts were of the opinion that the proposed amendment would make it virtually impossible to obtain extensions of the initial 30-day stay under the CCAA and force companies to file plans of arrangement within 30 days after the making of the initial stay order.
>
> Others suggested that some CCAA reorganizations would have turned out differently if the amendment had been in place.
>
> . . . . .
>
> Of the submissions received about proposed subsection 11(6), all but one condemned the provision. ...
>
> The CLHIA [Canadian Life and Health Insurance Association] argued that the amendment to the bill would be a significant improvement to the CCAA for four reasons:
>
> (a) it would give direction to the courts as to the tests that must be met before the extension order was granted;
>
> (b) it would more closely align the CCAA with the BIA;
>
> (c) the tests are well-established under the BIA and have received extensive scrutiny and study; and
>
> (d) the tests would direct the courts to consider how the stay would affect creditors. [Footnote omitted.]
>
> . . . . .
>
> The Committee shares the concerns expressed about the potential impact of proposed subsection 11(6) of the CCAA, particularly the concern that the CCAA may no longer be a sufficiently flexible vehicle for large, complex corporate reorganizations.
>
> While the Committee fully supports initiatives to align the provisions of the CCAA more closely with those of the BIA, these initiatives must be the subject of thorough discussion and analysis before [making] their way into legislation. Unfortunately, such discussion did not take place prior [to] the introduction of proposed subsection 11(6). [46]

Notwithstanding the submissions of the Canadian Life and Health Insurance Association, the Standing Committee recommended that Bill C-5 be amended by striking subparagraphs 11(6)(b)(ii) and (iii).

  

53 The House of Commons concurred in the Amendments recommended by the Senate on April 15, 1997. [47] Bill C-5, as thus amended, received Royal Assent on April 25, 1997 and was proclaimed in its present skeletal form on September 30, 1997. [48] Neither the amending legislation [49] nor the proposed Bill presently before the Senate [50] make any change to s. 11 in this regard.

54 The Senate's and Parliament's specific rejection of a limitation on the court's discretion is a strong indication of Parliamentary intention. The fact that Parliament did not see fit to limit the discretion in any significant manner, despite having been given the opportunity to do so, confirms the broad discretion given in ss. 11(3) and (4) to the supervising *CCAA* judge. Discretion is never completely unfettered, but an appellate court should be reluctant to impose rigid tests, standards or criteria where Parliament has declined to do so. Some guidance can be taken from the jurisprudence.

55 In *Canadian Airlines Corp., Re* [51] Paperny J. (as she then was) indicated that the obligation of the supervising *CCAA* judge is to "always have regard to the particular facts" and "to balance" the interests. As Farley J. said in *Ivaco Inc., Re*, [52] the supervising *CCAA* judge must also be concerned not to permit one creditor to mount "an indirect but devastating attack on the CCAA stay" so as to give one creditor an inappropriate advantage over other unsecured creditors as well as over secured creditors with priority.

56 In *Ivaco Inc., Re* [53] Ground J. stated this to be the criteria to determine whether a stay should be lifted:

> 20 It appears to me that the criteria which the court must consider in determining whether to lift a stay, being whether the proposed cause of action is tenable, the balancing of interests as between the parties, the relative prejudice to the parties, and whether the proposed action would be oppressive or vexatious or an abuse of the court process, would all be met with respect to a trial of issues to resolve interpretation of the APAs with respect to the calculation of the working capital adjustments.

Ground J. went on to confirm that finding a tenable or reasonable cause of action is not the only factor to be considered:

> 30 Even if the Statement of Claim did disclose a tenable or reasonable cause of action, there are a number of other factors which this court must consider which militate against the lifting of the stay in the circumstances of this case. The institution of the Proposed Action, even if a tight timetable is imposed, would inevitably result in considerable delay and complication with respect to the full distribution of the estate to the detriment of many small trade creditors and individual creditors as well as to pension claimants. In addition, it would appear from the evidence before this court that Heico has been aware of most of the matters alleged in the Statement of Claim for approximately 2 years and there does not appear to be any valid reason given for the delay in commencing the application to lift the stay.

57 Turning back to the case before us, Koch J.'s reasons for refusing to lift the stay were:

> [16] . . .
>
> > (a) An application to lift a stay of proceedings must be addressed in the context of the broad objectives of the *CCAA* which is to promote re-organization and restructuring of companies. ....
> >
> > (b) The standard for determining whether to lift the stay of proceedings is not, as ICR contends, whether the action is frivolous, analogous to the standard which a defendant applicant under Rule 173 of *The Queen's Bench Rules* must meet to set aside a statement of claim. Rather, to obtain an order lifting the stay ad hoc to permit the suit to proceed, the proposed plaintiff must establish that the cause of action is tenable. I interpret that to mean that the proposed plaintiff has a *prima facie* case. See *Ivaco Inc. (Re)*, [2006] O.J. No. 5029 (Ont. S.C.J.).
> >
> > (c) In determining whether to lift a stay, the Court must take into consideration the relative prejudice to the parties. See *Ivaco, Inc. (Re)*, *supra*, para. 20; and Richard H. McLaren & Sabrina Gherbaz, *Canadian Commercial Reorganization: Preventing Bankruptcy* (Toronto: Canada Law Book, 1995) at 3-18.1. ... [54]

  

He went on to find that the proposed action against Bricore was not "tenable."

58 On an application made by a post-filing creditor, a supervising *CCAA* judge can refuse to lift the stay on the basis that the creditor's claim is outside the *CCAA* process and the action can be commenced after the *CCAA* order is lifted. (See *360networks* [55] and *Stelco* [56]). Koch J. did not exercise this option. He was no doubt motivated in part by the fact that by the time ICR's claim could be tried, after the stay is no longer in effect, there may be no funds for it to claim as Bricore has now liquidated all of its assets and there remains, for all intents and purposes, a pool of funds only. The funds are subject to a plan of distribution, approved by the creditors, and will be distributed over this year.

59 Instead of simply rejecting the claim, Koch J. appears to have weighed the evidence to a certain extent as a means of deciding the next step. He concluded that the claim was not frivolous within the meaning of a Queen's Bench Rule 173 striking motion, but it was nonetheless an untenable claim. The question becomes whether a supervising *CCAA* judge can weigh a post-filing claim in this manner.

60 Professor Sarra comments on the anomalous position of liquidating *CCAA* proceedings:

> One policy issue that has not to date been fully explored is whether the *CCAA* should be used to effect an organized liquidation that should properly occur under the *BIA* or receivership proceedings. Increasingly, there are liquidating *CCAA* proceedings, whereby the debtor corporation is for all intents and purposes liquidated, but not under the supervision of a trustee in bankruptcy or in compliance with all of the requirements of the *BIA*. While creditors still must vote in support of such plans in the requisite amounts, there may be some public policy concerns regarding the use of a restructuring statute, under the broad scope of judicial discretion, to effect liquidation. ... [57]

The issue of whether the *CCAA* should be used for a liquidating, as opposed to a restructuring purpose, is not before us. In the case at bar, when the Initial Order was granted, it was thought possible that Bricore could be restructured. It was only some months after the Initial Order that it became clear that all of the assets would have to be sold. Our task at this point is to address the position of an undetermined claim arising post-filing in such a context.

61 If a claim had some reasonable prospect of success and were otherwise meritorious in the *CCAA* context, it seems inappropriate to refuse simply to lift the stay on the basis that the claim is outside the *CCAA* process knowing that, by the time the matter is heard in the ordinary course, there will be no assets remaining. On the other hand, it also seems inappropriate to delay distribution of the assets under a plan of arrangement, or make some other accommodation, for an action that is likely to fail. I should make it clear that I am not addressing the issue of whether a meritorious claimant can share in a proposed plan of distribution as a result of the liquidation of the assets. The issue before this Court is whether a post-filing creditor should be permitted to commence action, in the context of what is now a liquidating *CCAA*, and avail itself of whatever pre-judgment remedies might be available to it as a result of its claim.

62 In the face of a liquidating plan of arrangement, given the broad jurisdiction conferred by the *CCAA* on the Court, it seems appropriate that the supervising judge establish some mechanism to weigh the post-filing claim to determine the next step. The next step might entail permitting the claimant to commence action and attempt to convince a chambers judge to grant it a pre-judgment remedy in relation to the funds. It is also possible that the supervising judge may delay distribution of the funds, or some portion thereof, with or without full security for costs, or on such other terms as seems fit. Mechanisms to test the claim could include referral to a special claims officer, examination of the pertinent principal parties, or a settlement conference, or, as in this case, a preliminary examination by the supervising *CCAA* judge in chambers based on affidavit evidence.

63 In the case at bar, having determined that it was appropriate to assess ICR's claim in some way, did Koch J. err either in his statement of the appropriate test or in its application?

64 Koch J. used *prima facie* case, which he equated with tenable cause of action. "Tenable cause of action" is taken from Ground J.'s decision in *Ivaco Inc., Re*, [58] but Ground J. used "reasonable cause of action" or "tenable case," as comparable

  

terms and as only one of four criteria to be considered. The use of "*prima facie* case" defined as "tenable cause of action" is not particularly helpful as the words have been used in different contexts with different purposes in mind. Even in the context of bankruptcy where specific guidelines are given, and the courts have had long experience with the application of the tests, the debate continues as to what is meant by *prima facie* case and whether it is too high of a standard to apply in determining whether an action may be commenced. [59]

65 Koch J. was clearly correct to hold that the threshold established by s. 173 of *The Queen's Bench Rules* is too low. On the other hand, it is also important not to decide the case. The purpose for passing on the claim is not to determine whether it will or will not succeed, but to determine whether the plan of arrangement should be delayed or further compromised to accommodate a future claim, or some other step need be taken to maintain the integrity of the *CCAA* proceeding.

66 Given the broad discretion granted to a supervisory judge under the *CCAA*, as well as the knowledge and experience he or she gains from the ongoing dealings with the parties under the proceedings, it would be contrary to the purpose of the *CCAA* for the law under it to develop in a restrictive way. Having regard for this, there ought not to be rigid requirements imposed on how a supervising *CCAA* judge must exercise his or her discretion with respect to lifting the stay.

67 Nonetheless, a broad test articulated along the lines of that in *Ma, Re* [60] may be of assistance. The test from *Ma, Re* is:

> 3 ... As stated in *Re Francisco*, the role of the court is to ensure that there are "sound reasons, consistent with the scheme of the *Bankruptcy and Insolvency Act*" to relieve against the automatic stay. While the test is not whether there is a *prima facie* case, that does not, in our view, preclude any consideration of the merits of the proposed action where relevant to the issue of whether there are "sound reasons" for lifting the stay. For example, if it were apparent that the proposed action had little prospect of success, it would be difficult to find that there were sound reasons for lifting the stay.

While the *Ma, Re* test was developed for use under the *BIA*, a test based on sound reasons, consistent with the scheme of the *CCAA*, to relieve against the stay imposed by ss. 11(3) and (4) of the *CCAA*, may be a better way to express the task of the chambers judge faced with a liquidating *CCAA* than a test based simply on *prima facie* case. It must be kept firmly in mind that the Court is dealing with a claimant that did not avail itself of the remedy of withholding services under s. 11.3. It is also useful to remind oneself that, in a case such as this, the *CCAA* proceeding began as a restructuring exercise with the attendant possibility of creating s. 11.3 claimants. The threshold must be a significant one, but not insurmountable.

68 In determining what constitutes "sound reasons," much is left to the discretion of the judge. However, previous decisions on this point provide some guidance as to factors that may be considered:

> (a) the balance of convenience;
>
> (b) the relative prejudice to the parties;
>
> (c) the merits of the proposed action, where they are relevant to the issue of whether there are "sound reasons" for lifting the stay (i.e., as was said in *Ma, Re*, if the action has little chance of success, it may be harder to establish "sound reasons" for allowing it to proceed).

The supervising *CCAA* judge should also consider the good faith and due diligence of the debtor company as referenced in s. 11(6). Ultimately, it is in the discretion of the supervising *CCAA* judge as to whether the proposed action ought to be allowed to proceed in the face of the stay.

69 While Koch J. did not state the test as broadly as I have, I agree that ICR does not reach the necessary threshold. ICR did not structure its affairs or establish a claim with the specificity that justifies the development of a remedy to allow it to participate in the liquidation of the Bricore assets. There is also no aspect of the liquidation that requires the Court in this case to be concerned. In particular, the stay need not be lifted, and no other step need be taken in the context of the *CCAA* proceedings in light of these facts:

  

1. as of January 30, 2006, the Building was subject to an exclusive Selling Officer Agreement that provided CMN Calgary with the exclusive right to sell the property and to earn a commission of 1.25% of the purchase price, [61] which is significantly less than that being claimed by ICR at a 5% commission;

2. the sale to the Proposed Purchaser was a sale of six of the seven Bricore properties;

3. the trial judge received a report dated September 25, 2006 from the CRO recommending approval of the sale, which is two days before the alleged contract with ICR was proposed; [62]

4. in the September 25 report, the CRO advised the Court that "the total aggregate purchase price for the Bricore Properties obtained by Bricore in the Accepted Offer to Purchase represented the greatest value which it would be possible to obtain for all of the Bricore Properties;" [63]

5. the September 27, 2006 letter from ICR to Bricore, states "we are aware that the properties are under contract to sell ..."; and,

6. there was no sale from Bricore to the City of Regina.

70 While ICR denies knowledge of the sale, it is important to come back to the September 27th letter from ICR to Mr. Ruf. It states:

> **We are aware that the properties are under contract to sell** and request that ICR be protected in the specific situations as outlined. [64] [Emphasis added]

The addition by the CRO of these words, "Date of closing of *a sale* or December 31, 2006 whichever is earlier," to that letter adds further support to the veracity of the CRO's report to the effect that the CRO entered into discussions with ICR to provide for the eventuality of a failed sale to the purchaser with whom Bricore already had a contractual relationship.

71 Finally, in assessing Koch J.'s decision, and in determining the deference that is owed to it, I am not unmindful that he issued some 20 orders in 2006, pertaining to the Bricore restructuring, at least five of which dealt substantively with the Building and its prospective sale to the Proposed Purchaser.

72 Thus, applying the standard of review previously articulated, I cannot say that Koch J. acted arbitrarily, on a wrong principle, or on an erroneous view of the facts, or that a failure of justice is likely to result from the exercise of his discretion in the manner he did.

**VII. Issue #4. Did the Supervising CCAA Judge Make a Reviewable Error in Refusing Leave to Commence an Action Against the CRO?**

73 In addition to the indemnification provided by para. 18 of the CRO Order quoted above, the Order goes on to indicate the only circumstances in which the CRO can be sued personally:

> 20. For greater clarity, the CRO [*sic*]:
>
> . . . . .
>
> (c) the CRO shall incur no liability or obligation as a result of his appointment or as a result of the fulfillment of his powers and duties as CRO, except as a result of instances of fraud, gross negligence or wilful misconduct on his part; and
>
> (d) no Proceeding shall be commenced against the CRO as a result of or relating in any way to his appointment or to the fulfillment of his powers and duties as CRO, without prior leave of the Court on at least seven days' notice to Bricore Group, the CRO and legal counsel to Bricore Group.

  

> 21. Subject to paragraph 20 hereof, nothing in this Order shall restrict an action against the CRO for acts of gross negligence, bad faith or wilful misconduct committed by him.

Setting aside the obvious ambiguity in this Order, it can be taken that to assert a claim against the CRO personally, ICR had to claim "fraud, gross negligence, wilful misconduct or bad faith." ICR claimed "bad faith."

74 Based on para. 20(d) of the Initial Order, there is no question that ICR was required to obtain prior leave of the court. The issue thus becomes whether the supervising *CCAA* judge erred in exercising his discretion in refusing to lift the stay.

75 Koch J.'s reasons for refusing to lift the stay are these:

> [18] Neither is there any basis upon which to lift the stay with respect to the proposed action against Maurice Duval, the Chief Restructuring Officer. Considerations applicable to Bricore under s. 11.3 do not apply to a court-appointed restructuring officer. Maurice Duval, as an officer of the Court, has explained his position in a cogent way. I accept his explanation. He did not sell the Department of Education Building to the City of Regina. He was not aware at the relevant time that the purchaser was going to resell. Indeed, his efforts were directed toward closing a single transaction involving all six Bricore properties. Although the proposed pleading accuses Mr. Duval of acting in "bad faith", it is not suggested on behalf of ICR that Mr. Duval has been guilty of fraud, gross negligence or wilful misconduct; that is, any of the limitations or exceptions expressly listed in paragraph 20(c) of the order of May 23, 2006.
>
> [19] As stated previously, the overriding purpose of the *CCAA* must also be considered. That applies in the Duval situation too. The statute is intended to facilitate restructuring to serve the public interest. In many cases such as the present it is necessary for the Court to appoint officers whose expertise is required to fulfill its mandate. It is clearly in the public interest that capable people be willing to accept such assignments. It is to be expected that such acceptance be contingent on protective provisions such as are included in the order of May 23, 2006, appointing Mr. Duval. It is important that the Court exercise caution in removing such restrictions; otherwise, the ability of the Court to obtain the assistance of needed experts will necessarily be impaired. Qualified professionals will be less willing to accept assignments absent the protection provisions in the appointing order. [65]

76 Again, Koch J. employed the same mechanism that he used to assess the claim against Bricore. He considered the status of the CRO as an officer of the court, noted the ambiguity in the Order and weighed the evidence to a certain extent. The question he was answering was the sufficiency of the claim to permit an action to be commenced against the Court's officer.

77 Again, applying the standard of review with respect to discretionary orders, there is no basis upon which the Court can intervene with Koch J.'s refusal to lift the stay so as to permit an action against the CRO in his personal capacity.

**VIII. Issue #5. Did the Supervising CCAA Judge Err in Awarding Costs on a Substantial Indemnity Basis?**

78 Koch J. awarded substantial indemnity costs for this reason:

> [6] In my view, allegations of misconduct against a court officer are rare and exceptional. Therefore costs on this motion should be imposed on a substantial indemnity scale, although not on the full solicitor and client basis sought. Bricore is entitled to costs on the motion of $2,000.00, and Maurice Duval is entitled to costs of $1,000.00, payable in each instance by the applicant, ICR Commercial Real Estate (Regina) Ltd. [66]

79 I note that Newbury J.A. in *New Skeena Forest Products Inc., Re* [67] dismissed a challenge to a costs award, holding that "these are the kinds of considerations which the [*CCAA*] Chambers judge ... was especially qualified to make." And, of course, all costs orders are discretionary orders.

80 Nonetheless in this case, it would appear that the supervising *CCAA* judge erred. There is no basis upon which to order substantial indemnity costs with respect to the application to lift the stay in relation to Bricore. Bad faith was not alleged on its

  

part. With respect to the CRO, the only basis upon which the stay could be lifted was to make an allegation of "bad faith." In the absence of some other factor, ICR cannot be faulted for making the very allegation that it was required to make in order to bring its application within the ambit of the stay of proceedings that had been granted.

81 In addition, while Koch J. indicated he was not awarding solicitor-and-client costs, there is not a sufficient distinction between substantial indemnity costs and solicitor-and-client costs. An award approaching solicitor-and-client costs is still a punitive order and, as there is no authority for the awarding of substantial indemnity costs, relies upon the same jurisprudential base as solicitor-and-client costs. As such, the award does not seem to meet the test established in *Siemens v. Bawolin* [68] and *Hashemian v. Wilde* [69] wherein it is stated that solicitor-and-client costs are generally awarded where there has been reprehensible, scandalous or egregious conduct on the part of one of the parties in the context of the litigation.

82 If the parties are unable to agree with respect to costs in the Court of Queen's Bench and in this Court, they may speak to the Registrar to fix a time for a conference call hearing regarding costs.

*Appeal allowed in part.*

Footnotes

1 R.S.C. 1985, c. C-36.

2 Appeal Book, pp. 17a and 22a [Affidavit of Paul Mehlsen].

3 *Ibid*. at pp. 27a and 32a.

4 Order (Appointment of Chief Restructuring Officer, Extension of Stay of Proceedings; Additional DIP Financing) made May 23, 2006.

5 Order (Extension of Stay of Proceedings) made August 1, 2006.

6 Order (Extension of Stay of Proceedings) made August 18, 2006.

7 Order (Extension of Stay of Proceedings, Extension of Appointment of CRO and Increase in Maximum CRO Remuneration; Increase to Administrative Charge) made September 25, 2006.

8 Order (Approving Sale; Extending Stay of Proceedings; Extending Appointment of CRO) made October 10, 2006.

9 Appeal Book, p. 7a-8a.

10 *Ibid*. at p. 12a.

11 *Ibid.* at pp. 14a-15a.

12 *Ibid*. at p. 46a.

13 *Ibid*. at pp. 38a-39a.

14 *Ibid*. at p. 51a-52a.

15 *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*, 2007 SKQB 121 (Sask. Q.B.).

16 John D. Honsberger, *Debt Restructuring: Principles and Practice*, looseleaf (Aurora, Ont.: Canada Law Book, 2007) at p. 9.61.

17 (1954), 34 C.B.R. 82 (C.S. Que.). There are no cases referring to *Ramsay Plate Glass* on the point that Prof. Honsberger raises in his text. (*Ptarmigan Airways Ltd. v. Federated Mining Corp.*, [1973] 3 W.W.R. 723 (N.W.T. S.C.) mentions *Ramsay Plate Glass* but not in reference to the point made here.)

  

18 *Ibid*. at p. 83.

19 (2003), 45 C.B.R. (4th) 151 (B.C. S.C.), appeal dismissed [*Caterpillar Financial Services Ltd. v. 360networks corp.*] (2007), 27 C.B.R. (5th) 115 (B.C. C.A.).

20 (2005), 15 C.B.R. (5th) 283 (Ont. S.C.J. [Commercial List]).

21 (1992), 14 C.B.R. (3d) 303 (Ont. Gen. Div.).

22 *360networks*, *supra* note 19.

23 *Stelco*, *supra* note 20 at para. 11.

24 *Campeau*, *supra* note 21.

25 *360networks*, *supra* note 19.

26 *Stelco*, *supra* note 20.

27 *Campeau*, *supra* note 21.

28 R.S.C. 1985, c. B-3.

29 Lloyd W. Houlden & Geoffrey B. Morawetz, *The 2007 Annotated Bankruptcy and Insolvency Act* (Toronto: Thomson Carswell, 2006) at pp. 562 and 789.

30 *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act and the Income Tax Act*, S.C. 1997, c. 12, s. 124.

31 *Financial Consumer Agency of Canada Act*, S.C. 2001, c. 9, s. 577.

32 *Debt Restructuring Principles and Practice*, *supra* note 16 at p. 9-88.1.

33 Richard H. McLaren, *Canadian Commercial Reorganization: Preventing Bankruptcy*, looseleaf (Aurora, Ont.: Canada Law Book, 2007) at p. 3-17.

34 Janis Sarra, *Rescue! The Companies' Creditors Arrangement Act* (Toronto: Thomson Carswell, 2007).

35 *Ibid.* at pp. 110-11.

36 (1998), 53 B.C.L.R. (3d) 264 (B.C. S.C.). See also *Air Canada, Re* (2004), 47 C.B.R. (4th) 182 (Ont. S.C.J. [Commercial List]), and *Mosaic Group Inc., Re* (2004), 3 C.B.R. (5th) 40 (Ont. S.C.J.).

37 (1990), [1991] 2 W.W.R. 136 (B.C. C.A.).

38 (1990), 51 B.C.L.R. (2d) 105 (B.C. C.A.).

39 *Smith Brothers Contracting Ltd.*, *supra* note 36.

40 Order (Appointment of Chief Restructuring Officer; Extension of Stay of Proceedings; Additional DIP Financing) made May 23, 2006.

41 Bayda C.J.S., for the majority, in *Smart v. South Saskatchewan Hospital Centre* (1989), 75 Sask. R. 34 (Sask. C.A.), paraphrasing Lord Diplock in *Hadmor Productions Ltd. v. Hamilton*, [1982] 1 All E.R. 1042 (U.K. H.L.) at 1046.

42 [1943] O.R. 683 (Ont. C.A.) at 698.

  

43 *Rescue! The Companies' Creditors Arrangement Act*, *supra* note 34 at pp. 88-92.

44 *Supra* note 28.

45 Twelfth Report of the Standing Senate Committee on Banking, Trade and Commerce, February 1997, unnumbered p. 3 of the Chairman's Report, and p. 18.

46 *Ibid*. at pp. 17-18.

47 Canada Legislative Index, 2nd Session, 35th Parliament, Bill C-5, S.C. 1997, c. 12, pp. 1 & 2.

48 *Ibid.*

49 *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47, s. 128.

50 Bill C-62, *An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada*, 2005, 1st Sess., 39th Parl., 2006-2007.

51 (2000), 19 C.B.R. (4th) 1 (Alta. Q.B.) at para 15.

52 (2003), 1 C.B.R. (5th) 204 (Ont. S.C.J. [Commercial List]) at para 3.

53 [2006] O.J. No. 5029 (Ont. S.C.J.).

54 *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*, *supra* note 15.

55 *360networks*, *supra* note 19.

56 *Stelco*, *supra* note 20.

57 *Rescue! The Companies' Creditors Arrangements Act*, *supra* note 34 at p. 82.

58 *Ivaco Inc., Re*, *supra* note 53.

59 *Ma, Re* (2001), 24 C.B.R. (4th) 68 (Ont. C.A.). See Houlden & Morawetz, *The 2007 Annotated Bankruptcy and Insolvency Act*, supra note 29 at p. 403.

60 *Ibid.*

61 Order (Extension of Stay, DIP Financing, Sale Process & Shareholder Proceedings) of Koch J. in Chambers dated February 13, 2006.

62 Order made September 25, 2006, *supra* note 7.

63 Appeal Book, p. 37a, para. 3.

64 *Supra* note 11.

65 *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*, *supra* note 15.

66 *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*, 2007 SKQB 144 (Sask. Q.B.).

67 [2005] 8 W.W.R. 224 (B.C. C.A.) at para. 23.

68 2002 SKCA 84, [2002] 11 W.W.R. 246 (Sask. C.A.).

  

69 2006 SKCA 126, [2007] 2 W.W.R. 52 (Sask. C.A.).

**Most Negative Treatment:** Not followed
**Most Recent Not followed:** I.U.O.E., Local 894 v. Smurfit-Stone Container (Canada) Inc. | 2004 NBBR 70, 2004 NBQB 70, 2004 CarswellNB 67, 2004 CarswellNB 778, 129 A.C.W.S. (3d) 107, 45 C.C.P.B. 259, 712 A.P.R. 340, 271 N.B.R. (2d) 340, [2004] N.B.J. No. 57 | (N.B. Q.B., Feb 12, 2004)

1993 CarswellBC 44
Supreme Court of Canada

Peter v. Beblow

1993 CarswellBC 1258, 1993 CarswellBC 44, [1993] 1 S.C.R. 980, [1993] 3 W.W.R. 337, [1993] R.D.F. 369, [1993] B.C.W.L.D. 1264, [1993] W.D.F.L. 721, [1993] S.C.J. No. 36, 101 D.L.R. (4th) 621, 150 N.R. 1, 23 B.C.A.C. 81, 39 W.A.C. 81, 39 A.C.W.S. (3d) 646, 44 R.F.L. (3d) 329, 48 E.T.R. 1, 77 B.C.L.R. (2d) 1, J.E. 93-660, EYB 1993-67100

# CATHERINE PETER v. WILLIAM BEBLOW

La Forest, L'Heureux-Dubé, Sopinka, Gonthier, Cory, McLachlin and Iacobucci JJ.

Heard: November 12, 1992
Judgment: March 25, 1993
Docket: Doc. 22258

Proceedings: reversed *Peter v. Beblow* ((1990)), 1990 CarswellBC 237, 50 B.C.L.R. (2d) 266, 29 R.F.L. (3d) 268, 39 E.T.R. 113, [1991] 1 W.W.R. 419 ((B.C. C.A.))

Counsel: *G. William Wagner* and *R.C. Bernhardt*, for appellant.
*Nuala J. Hillis* and *Jessie MacNeil*, for respondent.

Subject: Family; Insolvency; Estates and Trusts; Property
**Related Abridgment Classifications**
Family law
VII Division of property
VII.2 Determination of ownership of property
VII.2.a Application of trust principles
VII.2.a.i Resulting and constructive trusts
VII.2.a.i.B Constructive trusts generally
**Headnote**
Family Law --- Family property on marriage breakdown — Determination of ownership of property — Application of trust principles — Resulting and constructive trusts — Constructive trusts generally
Family law — Unmarried couples — Property — Constructive and resulting trusts — Woman in long-term common law relationship maintaining and improving property and helping raise family without compensation — Court considering requirements for unjust enrichment — Court considering nexus between contribution and property necessary for constructive trust — Court awarding property to woman under constructive trust.
Trusts — Constructive trusts — Woman in long-term common law relationship maintaining and improving property and helping raise family without compensation — Court considering requirements for unjust enrichment — Court considering nexus between contribution and property necessary for constructive trust — Court awarding property to woman under constructive trust.
Restitution — Unjust enrichment — Woman in long-term common law relationship maintaining and improving property and helping raise family without compensation — Court considering requirements for unjust enrichment — Court considering nexus

 

between contribution and property necessary for constructive trust — Court awarding property to woman under constructive trust.

The man and woman lived together in a common law relationship in the man's house for over 12 years. The woman cared for both sets of children while they remained at home. She cooked, cleaned, washed clothes, looked after the garden and worked on the property. The man did not pay the woman for her work. Both contributed to the purchase of groceries and supplies, the man contributing a greater share. The woman worked outside the home part-time during the summers, and purchased a property elsewhere. The man paid off his mortgage on the house and bought a houseboat and a van. After the parties separated, the house remained vacant. The woman brought an action claiming that the man had been unjustly enriched by her work. She sought to have a constructive trust imposed respecting the house or, alternatively, damages. The trial judge found that the man had been unjustly enriched since he had obtained the woman's services without compensation. He also found that the woman was under no obligation to perform the work without reasonable expectation of compensation, and that the man ought to have known that. He concluded that she had conferred a proprietary benefit upon the house in an amount just over its assessed value. As the man was living elsewhere and a monetary judgment would be impracticable since he was living on his pension, the fairest apportionment would be to transfer the house to the woman. The British Columbia Court of Appeal allowed the man's appeal on the grounds that the woman was not deprived, that she had no reasonable expectation of compensation, and that there was insufficient nexus between her contribution and the property. The woman appealed.

**Held:**

Appeal allowed.

Per MCLACHLIN J. (LA FOREST, SOPINKA and IACOBUCCI JJ. concurring): Unjust enrichment has three elements: 1) an enrichment; 2) a corresponding deprivation; and 3) the absence of a juristic reason for the enrichment. One remedy for unjust enrichment is a monetary award. The remedy of constructive trust arises where monetary damages are inadequate and where there is a link between the contribution that founds the action and the property in which the constructive trust is claimed. Here the three elements necessary to establish a claim for unjust enrichment were established. The woman's housekeeping and child-care services constituted a benefit to the man. Those services constituted a corresponding detriment to the woman. Finally, since there was no obligation existing between the parties which would justify the unjust enrichment, there was no juristic reason for the enrichment.

In determining whether there is an absence of juristic reason for the enrichment, the test is flexible. The fundamental concern is the legitimate expectation of the parties. In family cases, this concern may raise certain subsidiary matters: whether the plaintiff conferred the benefit as a valid gift, or obligation owed the defendant; whether the plaintiff submitted to, or compromised, the defendant's honest claim; whether public policy supports the enrichment. Here the first and third factors could be argued. The law presumes no duty on a common law spouse to perform work and services for her partner. As the trial judge found on the facts that the woman was under no obligation to perform the work without reasonable expectation of compensation, the woman's services were neither performed pursuant to obligation nor were they a gift. Concerning public policy, there is no logical reason to distinguish domestic services from other contributions. Refusing to put a price on these services systematically devalues women's contributions to the family economy and contributes to the feminization of poverty. Today courts regularly recognize the value of domestic services. Although the legislature has excluded unmarried couples from matrimonial property legislation, it is precisely where an injustice arises without a legal remedy that equity finds a role. Accordingly, there were no juristic arguments that would justify the unjust enrichment.

In determining the proper remedy for unjust enrichment the same general principles apply in both commercial and in family cases. The first step is to determine whether a monetary award is insufficient and whether sufficient nexus between the contribution and the property has been made out. In considering whether a monetary award is insufficient the court may consider the probability of the award being paid as well as the special interest in the property acquired by the contributions. The extent of the interest is to be determined on the basis of the actual value of the matrimonial property — the "value-survived" approach. The "value-received" approach applies only to a monetary award. Where the claim is for an interest in the property one must necessarily determine what portion of the property's value is attributable to the plaintiff's services. A "value-received" approach to property would present practical problems with calculation. Moreover, a "value-survived" approach would accord best with the expectations of most parties, who expect to share in the wealth generated by their partnership. The trial judge's approach accorded with these principles. He assessed the value received by the woman, held that a monetary judgment would be inadequate, and concluded that there was a sufficiently direct connection between the services rendered and the property

  

to support a constructive trust. Considering the woman's proper share of all the family assets, the evidence supported the trial judge's conclusion that the woman had established a constructive trust entitling her to title to the family home. Her services helped preserve the property and saved the man large sums of money which he used to pay off his mortgage and to purchase a houseboat and a van.

Per CORY J. (concurring) (L'HEUREUX-DUBÉ and GONTHIER JJ. concurring):

A constructive trust arises where a person who holds title to property is subject to an equitable duty to convey it to another on the ground that he or she would be unjustly enriched if he or she were permitted to retain it. The constructive trust may be applied where the spouse has contributed either to the acquisition of property or to its preservation, maintenance or improvement. This remedy may be applied to common law relationships. Here the trial judge specifically found that the woman's services had enriched the man.

Particularly in a matrimonial or long-term common law relationship it should, in the absence of cogent evidence to the contrary, be taken that the enrichment of one party will result in a deprivation of the other. The constructive trust is used to redress gains made through a breach of trust in a commercial or business relationship. Parties involved in long-term common law relationships will also base their actions on mutual trust. They too are entitled, in appropriate circumstances, to the remedy of constructive trust. In today's society it is unreasonable to assume that the presence of love automatically implies the gift of one party's services to another. Nor is it unreasonable for the party providing the domestic labour to share in the parties' property when the relationship is ended. The balancing of benefits in a matrimonial or common law relationship cannot be accomplished with the precision possible in a commercial relationship. The trial judge must consider the nature of the relationship, its duration and the contributions of the parties. Here there was ample evidence to justify the trial judge's finding that the woman had suffered deprivation. As a result of the relationship, including the efforts of the woman, the house was looked after and maintained. A 12-year relationship was long enough to provide a strong presumption that the services provided by the woman would not be used solely to enrich the man. The woman worked to create a home for the man, which involved many hours of work per week. The test regarding juristic reasons for the enrichment is an objective one. In a common law relationship, it is not necessary that there be evidence of promises to marry or to compensate the claimant for the services provided. Rather, where a person provides "spousal services" to another, those services should be taken as having been given with the expectation of compensation unless there is evidence to the contrary. Here the trial judge appropriately drew the inference that the woman would reasonably have had an expectation of sharing the wealth she helped to create. All the conditions for unjust enrichment were made out.

While there is a need to limit the use of the constructive trust remedy in a commercial context, the same proposition should not be rigorously applied in a family relationship. Unlike a commercial relationship, in a family relationship the work, services and contributions provided by one of the parties need not be directly linked to a specific property. As long as there was no compensation provided for one party's services then it can be inferred that the provision of those services permitted the other party to acquire lands or to improve them. It follows that in a quasi-marital relationship where third party rights are not involved, the choice between a monetary award and a constructive trust will be discretionary and should be exercised flexibly. The decision as to which property, if there is more than one, should be made the subject of a constructive trust is also a discretionary one. Where the relationship is short or there are no assets surviving its dissolution, a monetary award should be made. A monetary payment might also be more appropriate than a constructive trust if the plaintiff's entitlement is small or could be satisfied apart from the property, if the defendant has any special attachment to the property, or if an award to the plaintiff of an interest in the property might cause hardship to the defendant. Here the woman contributed to the maintenance and preservation of the house. The trial judge was correct in finding that a monetary award would be impracticable. The property was vacant and the woman might have formed an emotional attachment to it. It was both reasonable and appropriate to choose the house for a constructive trust.

The two methods of evaluating the contribution of a party in a matrimonial relationship are the "value received" approach and the "value surviving" approach. While the former has traditionally been used in constructive trust cases, there is no reason why the latter approach could not be used. The remedy should be flexible. Nevertheless, the value surviving approach will often be preferable. This method will usually be more equitable and will more closely accord with the parties' expectations. Further, this method will avoid the difficult task of putting a dollar value on domestic services. Here the trial judge used a value received approach. Awarding the house to the woman reflected a fair assessment of her contribution to the relationship.

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**Words and phrases considered:**

**CONSTRUCTIVE TRUST**

In Austin Wakeman Scott and William Franklin Fratcher, *The Law of Trusts*, vol. 5, 4th ed. (Boston: Little, Brown, 1989) at p. 304, the following definition appears:

A constructive trust arises where a person who holds title to property is subject to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to retain it.

The constructive trust, based on analogy to the formal trust of traditional equity, is a proprietary concept . . . for a constructive trust to arise, the plaintiff must establish a direct link to the property which is the subject of the trust by reason of the plaintiff's contribution.

. . . . .

. . . monetary compensation must be inadequate and there must be a link between the services rendered and the property in which the trust is claimed.

  

Appeal from judgment of British Columbia Court of Appeal, [1991] 1 W.W.R. 419, 50 B.C.L.R. (2d) 266, 39 E.T.R. 113, 29 R.F.L. (3d) 268, reversing judgment of Arkell L.J.S.C. awarding common law wife matrimonial home under constructive trust.

***McLachlin J. (La Forest, Sopinka and Iacobucci JJ.* concurring):**

1 I have had the advantage of reading the reasons of Justice Cory. While I agree with his conclusion and with much of his analysis, my reasons differ in some respects on two matters critical to this appeal: the issues raised by the requirement of the absence of juristic reason for an enrichment and the nature and application of the remedy of constructive trust.

2 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 La Forest J.A. (as he then was) in *White v. Central Trust Co.* (1984), 7 D.L.R. (4th) 236, at p. 246, "... the well recognized categories of unjust enrichment must be regarded as clear examples of the more general principle that transcends them."

3 The basic notions are simple enough. An action for unjust enrichment arises when three elements are satisfied: (1) an enrichment; (2) a corresponding deprivation; and (3) the absence of a juristic reason for the enrichment. These proven, the action is established and the right to claim relief made out. At this point, a second doctrinal concern arises: the nature of the remedy. "Unjust enrichment" in equity permitted a number of remedies, depending on the circumstances. One was a payment for services rendered on the basis of quantum meruit or quantum valebat. Another equitable remedy, available traditionally where one person was possessed of legal title to property in which another had an interest, was the constructive trust. While the first remedy to be considered was a monetary award, the Canadian jurisprudence recognized that in some cases it might be insufficient. This may occur, to quote Justice La Forest in *Lac Minerals Ltd. v. International Corona Resources Ltd.*, [1989] 2 S.C.R. 574, at p. 678, "if there is reason to grant to the plaintiff the additional rights that flow from recognition of a right of property." Or to quote Dickson J., as he then was, in *Pettkus v. Becker*, [1980] 2 S.C.R. 834, at p. 852, where there is a "contribution [to the property] sufficiently substantial and direct as to entitle [the plaintiff] to a portion of the profits realized upon sale of [the property]." In other words, the remedy of constructive trust arises, where monetary damages are inadequate and where there is a link between the contribution that founds the action and the property in which the constructive trust is claimed.

4 Notwithstanding these rather straightforward doctrinal underpinnings, their application has sometimes given rise to difficulty. There is a tendency on the part of some to view the action for unjust enrichment as a device for doing whatever may seem fair between the parties. In the rush to substantive justice, the principles are sometimes forgotten. Policy issues often assume a large role, infusing such straightforward discussions as whether there was a "benefit" to the defendant or a "detriment" to the plaintiff. On the remedies side, the requirements of the special proprietary remedy of constructive trust are sometimes minimized. As Professor Palmer has said: "The constructive trust idea stirs the judicial imagination in ways that assumpsit, quantum meruit and other terms as sociated with quasi-contract have never quite succeeded in duplicating" (G.E. Palmer, *The Law of Restitution*, vol. 1, at p. 16). Occasionally the remedial notion of constructive trust is even conflated with unjust enrichment itself, as though where one is found the other must follow.

5 Such difficulties have to some degree complicated the case at bar. At the doctrinal level, the simple question of "benefit" and "detriment" became infused with moral and policy questions of when the provision of domestic services in a quasi-matrimonial situation can give rise to a legal obligation. At the stage of remedy, the trial judge proceeded as if he were making a monetary award, and then, without fully explaining how, awarded the appellant the entire interest in the matrimonial home on the basis of a constructive trust. It is only by a return to the fundamental principles laid out in cases like *Pettkus v. Becker* and *Lac Minerals*, that one can cut through the conflicting findings and submissions on these issues and evaluate whether in fact the appellant has made out a claim for unjust enrichment, and if so what her remedy should be.

  

**1. Is the Appellant's Claim for Unjust Enrichment Made Out?**

6 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.

7 The main arguments on this appeal centred on whether the law should recognize the services which the appellant provided as being capable of founding an action for unjust enrichment. It was argued, for example, that the services cannot give rise to a remedy based on unjust enrichment because the appellant had voluntarily assumed the role of wife and stepmother. It was also said that the law of unjust enrichment should not recognize such services because they arise from natural love and affection. These arguments raise moral and policy questions and require the Court to make value judgments.

8 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 [[1986] 5 W.W.R. 289]; *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".

9 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.

10 In every case, the fundamental concern is the legitimate expectation of the parties: *Pettkus v. Becker*, supra. In family cases, this concern may raise the following subsidiary questions:

11 (i) Did the plaintiff confer the benefit as a valid gift or in pursuance of a valid common law, equitable or statutory obligation which he or she owed to the defendant?

12 (ii) Did the plaintiff submit to, or compromise, the defendant's honest claim?

13 (iii) Does public policy support the enrichment?

14 In the case at bar, the first and third of these factors were argued. It was argued first that the appellant's services were rendered pursuant to a common law or equitable obligation which she had assumed. Her services were part of the bargain she made when she came to live with the respondent, it was said. He would give her and her children a home and other husbandly services, and in turn she would look after the home and family.

15 This Court has held that a common law spouse generally owes no duty at common law, in equity or by statute to perform work or services for her partner. As Dickson C.J., speaking for the Court put it in *Sorochan v. Sorochan*, supra, at p. 46, the common law wife "was under no obligation, contractual or otherwise, to perform the work and services in the home or on the land." So there is no general duty presumed by the law on a common law spouse to perform work and services for her partner.

  

16 Nor, in the case at bar was there any obligation arising from the circumstances of the parties. The trial judge held that the appellant was "under no obligation to perform the work and assist in the home without some reasonable expectation of receiving something in return other than the drunken physical abuse which she received at the hands of the respondent." This puts an end to the argument that the services in question were performed pursuant to obligation. It also puts an end to the argument that the appellant's services to her partner were a "gift" from her to him. The central element of a gift at law — intentional giving to another without expectation of remuneration — is simply not present.

17 The third factor mentioned above raises directly the issue of public policy. While it may be stated in different ways, the argument at base is simply that some types of services in some types of relationships should not be recognized as supporting legal claims for policy reasons. More particularly, homemaking and childcare services should not, in a marital or quasi-marital relationship, be viewed as giving rise to equitable claims against the other spouse.

18 I concede at the outset that there is some judicial precedent for this argument. Professor Marcia Neave has observed generally that "analysis of the principles applied in English, Australian and Canadian courts sometimes fails to confront this question directly ... Courts which deny or grant remedies usually conceal their value judgments within statements relating to doctrinal requirements." (Marcia Neave, "Three Approaches to Family Property Disputes — Intention/Belief, Unjust Enrichment and Unconscionability," in T.G. Youdan, ed., *Equity, Fiduciaries and Trusts*, at p. 251). More pointedly, Professor Farquhar has observed that many courts have strayed from the framework of *Sorochan* for public policy reasons: "the courts ... have, after *Sorochan*, put up warning signs that there are aspects of relationships that are not to be analyzed in the light of unjust enrichment and constructive trust." (Keith B. Farquhar, "Causal Connection in Constructive Trust After *Sorochan v. Sorochan*" (1989), 7 Can. J. of Family Law 337, at p. 343). The public policy issue has been summed up as follows by Professor Neave at p. 251: "whether a remedy, either personal or proprietary, should be provided to a person who has made contributions to family resources." On the judicial side, the view of the respondent is pointedly stated in *Grant v. Edwards*, [1986] 2 All E.R. 426, at p. 439, per Browne-Wilkinson V.C.:

> Setting up house together, having a baby and making payments to general housekeeping expenses ... may all be referable to the mutual love and affection of the parties and not specifically referable to the claimant's belief that she has an interest in the house.

Proponents of this view, Professor Neave, at p. 253 argues, "regard it as distasteful to put a price upon services provided out of a sense of love and commitment to the relationship. They suggest it is unfair for a recipient of indirect or non-financial contributions to be forced to provide recompense for those contributions." To support this position, the respondent cites several cases. *Kshywieski v. Kunka Estate* (1986), 50 R.F.L. (2d) 421 [[1986] 3 W.W.R. 472] (Man. C.A.); *Houghen v. Monnington* (1991), 37 R.F.L. (3d) 279 (B.C.C.A.); *Prentice v. Lang* (1987), 10 R.F.L. (3d) 364 (B.C.S.C.); *Hyette v. Pfenniger*, B.C.S.C., Dec. 19, 1991 [now reported (1991), 39 R.F.L. (3d) 30, additional reasons at 39 R.F.L. (3d) at 44].

19 It is my view that this argument is no longer tenable in Canada, either from the point of view of logic or authority. From the point of view of logic, I share the view of Professors Hovius and Youdan [*The Law of Family Property*] that "there is no logical reason to distinguish domestic services from other contributions" (at p. 146). The notion that household and childcare services are not worthy of recognition by the court fails to recognize the fact that these services are of great value, not only to the family, but to the other spouse. As Lord Simon observed nearly thirty years ago: "The cock-bird can feather his nest precisely because he is not required to spend most of his time sitting on it" ("With All My Worldly Goods," *Holdsworth Lecture* (University of Birmingham, 20th March 1964), at p. 32). The notion, moreover, is a pernicious one that systematically devalues the contributions which women tend to make to the family economy. It has contributed to the phenomenon of the feminization of poverty which this Court identified in *Moge v. Moge*, [1992] 3 S.C.R. 813 [[1993] 1 W.W.R. 481], per L'Heureux-Dubé J., at pp. 853-54.

20 Moreover, the argument cannot stand with the jurisprudence which this and other courts have laid down. Today courts regularly recognize the value of domestic services. This became clear with the Court's hold ing in *Sorochan*, leading one author to comment that "the Canadian Supreme court has finally recognized that domestic contribution is of equal value as financial

  

contribution in trusts of property in the familial context" (Mary Welstead, "Domestic Contribution and Constructive Trusts: The Canadian Perspective," [1987] Denning L.J. 151, at p. 161). If there could be any doubt about the need for the law to honestly recognize the value of domestic services, it must be considered to have been banished by *Moge v. Moge*, supra. While that case arose under the *Divorce Act*, R.S.C. 1985 c. 3 (2nd Supp.), the value of the services does not change with the legal remedy invoked.

21 I cannot give credence to the argument that legal recognition of the value of domestic services will do violence to the law and the social structure of our society. It has been recognized for some time that such services are entitled to recognition and compensation under the *Divorce Act* and the provincial Acts governing the distribution of matrimonial property. Yet society has not been visibly harmed. I do not think that similar recognition in the equitable doctrine of unjust enrichment will have any different effect.

22 Finally, I come to the argument that, because the legislature has chosen to exclude unmarried couples from the right to claim an interest in the matrimonial assets on the basis of contribution to the relationship, the court should not use the equitable doctrine of unjust enrichment to remedy the situation. Again, the argument seems flawed. It is precisely where an injustice arises without a legal remedy that equity finds a role. This case is much stronger than *Rawluk v. Rawluk*, [1990] 1 S.C.R. 70, where I dissented on the ground that the statute expressly pronounced on the very matter with respect to which equity was invoked.

23 Accordingly, I would agree with Cory J. that there are no juristic arguments which would justify the unjust enrichment, and the third element is made out. Like him, I conclude that the plaintiff was enriched, to the benefit of the defendant, and that no justification existed to vitiate the unjust enrichment claim. The claim for unjust enrichment is accordingly made out and it remains only to determine the appropriate remedy.

**2. Remedy — Monetary Judgment or Constructive Trust?**

24 The other difficult aspect of this case is the question of whether the remedy which the trial judge awarded — title to the matrimonial home — is justified on the principles governing the action for unjust enrichment. Two remedies are possible: an award of money on the basis of the value of the services rendered, i.e., quantum meruit; and the one the trial judge awarded, title to the house based on a constructive trust.

25 In Canada the concept of the constructive trust has been used as a vehicle for compensating for unjust enrichment in appropriate cases. The constructive trust, based on analogy to the formal trust of traditional equity, is a proprietary concept. The plaintiff is found to have an interest in the property. A finding that a plaintiff is entitled to a remedy for unjust enrichment does not imply that there is a constructive trust. As I wrote in *Rawluk*, supra, for a constructive trust to arise, the plaintiff must establish a direct link to the property which is the subject of the trust by reason of the plaintiff's contribution. This is the notion underlying the constructive trust in *Pettkus v. Becker*, supra, and *Sorochan v. Sorochan*, supra, as I understand those cases. It was also affirmed by La Forest J. in *Lac Minerals*, supra.

26 My colleague Cory J. suggests that, while a link between the contribution and the property is essential in commercial cases for a constructive trust to arise, it may not be required in family cases. He writes [pp. 31-32]:

> ... La Forest J. concluded [in *Lac Minerals*, supra] that the constructive trust should only be awarded when the personal monetary award is insufficient; that is, when there is reason to grant to the plaintiff the additional rights that flow from recognition of a right to property.
>
> I agree with my colleague that there is a need to limit the use of the constructive trust remedy in a commercial context. Yet I do not think the same proposition should be rigorously applied in a family relationship.

27 I doubt the wisdom of dividing unjust enrichment cases into two categories — commercial and family — for the purpose of determining whether a constructive trust lies. A special rule for family cases finds no support in the jurisprudence. Neither *Pettkus*, nor *Rathwell* [*Rathwell v. Rathwell*, [1978] 2 W.W.R. 101], nor *Sorochan* suggest such a departure. Moreover, the notion that one can dispense with a link between the services rendered and the property which is claimed to be subject to the

  

trust is inconsistent with the proprietary nature of the notion of constructive trust. Finally, the creation of special rules for special situations might have an adverse effect on the development of this emerging area of equity. The same general principles should apply for all contexts, subject only the demonstrated need for alteration. Wilson J. in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426 [35 B.C.L.R. (2d) 145, [1989] 3 W.W.R. 385], at p. 519 (adopted by La Forest J. in *Lac Minerals*, supra, at p. 675), warns against confining constructive trust remedies to family law cases stating that: "to do so would be to impede the growth and impair the flexibility crucial to the development of equitable principles." The same result, I fear, may flow from developing special rules for finding constructive trusts in family cases. In short, the concern for clarity and doctrinal integrity with which this Court has long been preoccupied in this area mandates that the basic principles governing the rights and remedies for unjust enrichment remain the same for all cases.

28 Nor does the distinction between commercial cases and family cases on the remedy of constructive trust appear to be necessary. Where a monetary award is sufficient, there is no need for a constructive trust. Where a monetary award is insufficient in a family situation, this is usually related to the fact the claimant's efforts have given her a special link to the property, in which case a constructive trust arises.

29 For these reasons, I hold the view that in order for a constructive trust to be found, in a family case as in other cases, monetary compensation must be inadequate and there must be a link between the services rendered and the property in which the trust is claimed. Having said this, I echo the comments of Cory J. at p. 28 [p. 32] that the courts should exercise flexibility and common sense when applying equitable principles to family law issues with due sensitivity to the special circumstances that can arise in such cases.

30 The next question is the extent of the contribution required to give rise to a constructive trust. A minor or indirect contribution is insufficient. The question, to quote Dickson C.J. in *Pettkus v. Becker*, supra, at p. 852, is whether "[the plaintiff's] contribution [was] sufficiently substantial and direct as to entitle her to a portion of the profits realized upon sale of the ... property." Once this threshold is met, the amount of the contribution governs the extent of the constructive trust. As Dickson C.J. wrote in *Pettkus v. Becker*, supra, at pp. 852-53:

> Although equity is said to favour equality, as stated in *Rathwell*, it is not every contribution which will entitle a spouse to a one-half interest in the property. *The extent of the interest must be proportionate to the contribution, direct or indirect, of the claimant. Where the contributions are unequal, the shares will be unequal*. [Emphasis added.]

Cory J. advocates a flexible approach to determining whether a constructive trust is appropriate; an approach "based on common sense and a desire to achieve a fair result for both parties" (at p. 28 [p. 32]). While agreeing that courts should avoid becoming overly technical on matters which may not be susceptible of precise monetary valuation, the principle remains that the extent of the trust must reflect the extent of the contribution.

31 Before leaving the principles governing the remedy of constructive trust, I turn to the manner in which the extent of the trust is determined. The debate centres on whether it is sufficient to look at the value of the services which the claimant has rendered (the "value received" approach), or whether regard should be had to the amount by which the property has been improved (the "value survived" approach). Cory J. expresses a preference for a "value survived" approach. However, he also suggests, at p. 31 [pp. 33-34], that "there is no reason why quantum meruit or the value received approach could not be utilized to quantify the value of the constructive trust." With respect, I cannot agree. It seems to me that there are very good reasons, both doctrinal and practical, for referring to the "value survived" when assessing the value of a constructive trust.

32 From the point of view of doctrine, "the extent of the interest must be proportionate to the contribution" to the property: *Pettkus v. Becker*, supra, at p. 852. How is the contribution to the property to be determined? One starts, of necessity, by defining the property. One goes on to determine what portion of that property is attributable to the claimant's efforts. This is the "value survived" approach. For a monetary award, the "value received" approach is appropriate; the value conferred on the property is irrelevant. But where the claim is for an interest in the property one must of necessity, it seems to me, determine what portion of the value of the property claimed is attributable to the claimant's services.

  

33 I note, as does my colleague, that there may also be practical reasons for favouring a "value survived" approach. Cory J., alludes to the practical problems with balancing benefits and detriments as required by the "value received" approach, leading some to question whether it is the least attractive approach in most family property cases (see *Davidson v. Worthing* (1986), 6 R.F.L. (3d) 113 [9 B.C.L.R. (2d) 202] (S.C.), McEachern C.J.S.C.; Hovius and Youdan at pp. 136ff). Moreover, a "value survived" approach arguably accords best with the expectations of most parties; it is more likely that a couple expects to share in the wealth generated from their partnership, rather than to receive compensation for the services performed during the relationship.

34 To summarize, it seems to me that the first step in determining the proper remedy for unjust enrichment is to determine whether a monetary award is insufficient and whether the nexus between the contribution and the property described in *Pettkus v. Becker* has been made out. If these questions are answered in the affirmative the plaintiff is entitled to the proprietary remedy of constructive trust. In looking at whether a monetary award is insufficient the court may take into account the probability of the award's being paid as well as the special interest in the property acquired by the contributions: per La Forest J. in *Lac Minerals*. The value of that trust is to be determined on the basis of the actual value of the matrimonial property — the "value survived" approach. It reflects the court's best estimate of what is fair having regard to the contribution which the claimant's services have made to the value surviving, bearing in mind the practical difficulty of calculating with mathematical precision the value of particular contributions to the family property.

35 I turn now to the application of these principles to the case at bar. The trial judge began by assessing the value received by the respondent (the quantum meruit). He went on to conclude that a monetary judgment would be inadequate. The respondent had few assets other than his houseboat and van, and no income save for a War Veteran's Allowance. The judge concluded, as I understand his reasons, that there was a sufficiently direct connection between the services rendered and the property to support a constructive trust, stating that "[the appellant] has shown that there was a positive proprietary benefit conferred by her upon the Sicamous property." Accordingly, he held that the remedy of constructive trust was made out. This approach accords with principles discussed above. In effect, the trial judge found the monetary award to be inadequate on the grounds that it would not be paid and on the ground of a special contribution to the property. These findings support the remedy of constructive trust in the property.

36 The remaining question is the quantification of the trust. The trial judge calculated the quantum meruit for her housekeeping for 12 years at $350 per month and reduced that figure by 50% "for the benefits she received." The final amount was $25,200. He then reasoned that, since the services rendered amounted to $25,200 after appropriate deductions, it follows that the appellant should receive title to the respondent's property, valued at $23,200. The missing step in this analysis is the failure to link the value received with the value surviving. As discussed above, a constructive trust cannot be quantified by simply adding up the services rendered; the court must determine the extent of the contribution which the services have made to the parties' property.

37 Notwithstanding the trial judge's failure to make this link, his conclusion that the appellant had established a constructive trust entitling her to title to the family home can be maintained if a trust of this magnitude is supported on the evidence. This brings me to a departure from the methods used below. The parties and the Court of Appeal appear to have treated the house as a single asset rather than as part of a family enterprise. This led to the argument that the appellant could not be entitled to full ownership in the house because the respondent had contributed to its value as well. The approach I would take — and the approach I believe the trial judge implicitly to have taken — is to consider the appellant's proper share of all the family assets. This joint family venture, in effect, was no different from the farm which was the subject of the trust in *Pettkus v. Becker*.

38 With this in mind, I turn to the evidence on the extent of the contribution. The appellant provided extensive household services, over a period of 12 years, including care for the children while they were living at the house and maintenance of the property. The testimony of the plaintiff's son provides a general idea of her contribution to the family enterprise:

Q. What sort of things did she do?

A. She did all the motherly duties for all of us ...

  

> A. When [the defendant's] two sons and my brother and I were there still, even when my sisters were there, that was quite a long time ago, I was quite young, so there was nothing really bad then, but after the sisters left, she took care of all the duties, cooking and stuff like that, cleaning, laundry. She had her ringer washer, she would do the laundry, she'd worked in the garden, things like that. She took care of all things around the house, when he was gone especially ...
>
> Q. Do you remember what work your mother did in the yard outside?
>
> A. M'hm, they both got together doing the garden, he would do the roto-tilling, they would both take care of the planting and stuff; when he was gone, she would do all the weeding and keeping up. They would share the watering of the garden. She put together three or four flower gardens all herself, except for the hard heavy work, like lifting rocks, when she first started, that was shared by all of us, including the kids.

Of all the chores performed around the property, the son states that the various siblings had minor chores, such as chopping wood and making beds. "Everything else, the major stuff, she would take care of." Other evidence, including testimony from Catherine Peter and William Beblow, supports this picture of the appellant's contribution. The trial judge held that while the respondent worked in the construction business:

> ... he would be away from home during the week and would return on the weekend whenever possible. While he was absent, the plaintiff would care for the property in the home and care for the children while he was away ...
>
> In effect, the plaintiff by moving into the respondent's home became his housekeeper on a full-time basis without remuneration except for the food and shelter that she and the children received until the children left home.

39 The respondent also contributed to the value of the family enterprise surviving at the time of breakup; he generated most of the family income and helped with the maintenance of the property.

40 Clearly, the appellant's contribution — the "value received" by the respondent — was considerable. But what then of the "value surviving"? It seems clear that the maintenance of the family enterprise through work in cooking, cleaning, and landscaping helped preserve the property and saved the respondent large sums of money which he was able to use to pay off his mortgage and to purchase a houseboat and a van. The appellant, for her part, had purchased a lot with her outside earnings. All these assets may be viewed as assets of the family enterprise to which the appellant contributed substantially.

41 The question is whether, taking the parties' respective contributions to the family assets and the value of the assets into account, the trial judge erred in awarding the appellant a full interest in the house. In my view, the evidence is capable of supporting the conclusion that the house reflects a fair approximation of the value of the appellant's efforts as reflected in the family assets. Accordingly, I would not disturb the award.

42 I would allow the appeal with costs.

***Cory J.*** **(concurring) (*L'Heureux-Dubé* and *Gonthier JJ.* concurring):**

43 The issue in this appeal is whether the provision of domestic services during 12 years of cohabitation in a common law relationship is sufficient to establish the proprietary link which is required before the remedy of constructive trust can be applied to redress the unjust enrichment of one of the partners in the relationship. Further, consideration must be given to the extent to which the remedy of constructive trust should be applied in terms of amount or proportion.

**Factual Background**

44 In April 1973, the respondent asked the appellant to come and live with him. That same month, the appellant together with her 4 children moved into the respondent's home in Sicamous, B.C. At the time, 2 children of the respondent were living in the home. The parties continued to live together in a common law relationship for over 12 years, separating in June 1985.

  

During this entire time the appellant acted as the wife of the respondent. She was a stepmother to his children until 1977 while they remained in the home. As well, she cared for her own children, the last one leaving in 1980.

45 During the 12 years, the appellant cooked, cleaned, washed clothes and looked after the garden. As well, she worked on the Sicamous property, undertaking such projects as painting the fence, planting a cedar hedge, buying flowers and shrubs for the property and building a rock garden. She built a pig pen. She kept chickens for a few years, butchering and cooking them for the family. During the winters, the appellant shovelled snow, chopped wood and made kindling. The respondent did not pay the appellant for any of her work. Both the appellant and the respondent contributed to the purchase of groceries and household supplies, although the respondent contributed a greater share.

46 In the first year of the relationship the appellant did not undertake outside work and spent 8 hours a day doing housework and work on the Sicamous property. In subsequent years, she took part-time work as a cook from June to October. During these months she worked some six hours a day at a rate of $4.50 per hour. Except for one winter when she worked at a bakery, the appellant received unemployment insurance benefits in the winter months.

47 Throughout the relationship, the respondent worked on a more or less full-time basis as a grader operator. His work frequently took him out of town to various locations in British Columbia.

48 Before he met the appellant, the respondent had lived in a common law relationship with another woman for 5 years. When she left his home he hired housekeepers. The last housekeeper he had before the appellant came to his home was paid at a rate of $350 per month.

49 The trial judge accepted the appellant's testimony that the respondent had asked her to live with him because he needed someone to care for his 2 children. This need arose when the welfare authorities expressed some concern that the respondent left the children alone when he was working away from home.

50 When the parties met, the appellant had savings of $100. In 1976, she purchased a property in Saskatchewan for $2,500. She sold this property in 1980 for $8,000 and purchased a property at 100 Mile House for $6,500. She used the remainder of the sale proceeds for a trip to Reno. At the time of trial, the appellant still owned the 100 Mile House property.

51 The respondent had purchased the Sicamous property in 1971 for $8,500. Some $900 was paid in cash and the balance of $7,600 was secured by a mortgage. The respondent was able to pay off the mortgage in 1975. The estimated market value of the Sicamous property as of 1987 was $17,800. The property's assessed value in that year was $23,200. In that same year, the respondent rented the property. The tenants were given an option to purchase it for $28,000. The option was not exercised.

52 With the passage of time, the respondent began to drink heavily and became verbally and physically abusive to the appellant. As a result, the appellant moved out of the Sicamous home on June 7, 1985. At the time of the trial, she was on welfare and lived in a trailer court in Sicamous. The respondent by that time had retired and was living on a houseboat in Enderby, B.C. The Sicamous house and property were vacant.

53 The appellant brought an action claiming that the respondent had been unjustly enriched over the years of the relationship as a result of the work which she performed in his home without payment of any kind. She sought to have a constructive trust imposed on her behalf in respect of the Sicamous property or in the alternative, monetary damages as compensation for the labour and services she provided to the respondent.

**Courts Below**

***Trial Judgment***

54 On the basis of *Sorochan v. Sorochan*, [1986] 2 S.C.R. 38 [[1986] 5 W.W.R. 289], the trial judge determined that in order to establish an unjust enrichment, the plaintiff must prove:

(1) enrichment;

  

(2) a corresponding deprivation; and

(3) the absence of any juristic reason for the enrichment.

55 He decided there must also be a clear causal connection between the spousal contribution founding the unjust enrichment and the property which is alleged to be the subject of the constructive trust.

56 The trial judge found that there had been an enrichment since the respondent had obtained the services of a housekeeper, homemaker and stepmother to his children without compensation. He further found that the plaintiff was deprived of any compensation from her labour since she devoted the majority of her time and energy and some of the monies which she earned for the benefit of the respondent, his children and his Sicamous property. Lastly, he found that there was no juristic reason for the enrichment, that is to say the appellant was under no obligation to perform the work and assist in the home without some reasonable expectation of compensation. He found that she was entitled to receive something other than the drunken physical abuse to which she had been subjected by the respondent. He concluded that the respondent ought to have known that the appellant would have a reasonable expectation that she would be compensated. He also concluded that she had shown that there was a proprietary benefit conferred by her upon the Sicamous property.

57 The trial judge then considered what would be a fair and equitable compensation. He took into account the realities of the relationship and the assets and income of the parties in order to fashion the appropriate relief. He observed that if the appellant had been employed as a housekeeper for 12 years at $350 per month, the amount the respondent had paid his last housekeeper before the appellant moved in, she would have earned $50,400. He allowed a 50 percent reduction for the benefits the appellant had received in the relationship and settled on the amount which should be paid to her as $25,200.

58 He then concluded that the fairest disposition of the case would be to award the Sicamous property to the appellant. He noted that the respondent was living in Enderby, on a houseboat. He noted that the respondent also had a van. The respondent was living on a War Veteran's Allowance and was retired. It was obvious to the trial judge that a monetary judgment would be impracticable, probably unrealistic and would not be reasonable under the circumstances. He therefore concluded that the fairest apportionment would be to have the house and land in Sicamous transferred to the appellant free and clear of encumbrances.

***Court of Appeal***

59 The respondent on the appeal [(1990), 50 B.C.L.R. (2d) 266, [1991] 1 W.W.R. 419] contended that, the trial judge had erred first in finding that there had been an unjust enrichment of the respondent, and secondly, that even if there had been an unjust enrichment, that he had erred in ordering the transfer of the Sicamous property to the appellant.

60 Macdonald J.A., writing on behalf of the court, observed that it had been conceded that the respondent had indeed been enriched by receiving the benefit of the appellant's labour and services. Thus, the first condition of *Sorochan* had been met. However, he found that the remaining conditions had not been fulfilled. The Court of Appeal disagreed with the trial judge's finding that there had been any deprivation suffered by the appellant. It found that the appellant had not been deprived as she and her children had lived in the respondent's home rent-free with the respondent's contributing more for the family's groceries than she had. He noted that the appellant had been able to acquire property and he took this as evidence that the appellant had not suffered any deprivation.

61 Macdonald J.A. further concluded that even if there was an imbalance sufficient to support a finding of deprivation, the unjust enrichment claim did not meet the third condition, namely the absence of any juristic reason for the enrichment. In his view, the appellant had failed to establish, as required by *Sorochan*, that she had prejudiced herself on the reasonable expectation of receiving something in return for her work and services. He stressed that there was not, as in other cases, the holding out of a promise to marry. Even though the respondent would, when he was drinking, ask the appellant to marry him, she never took those requests seriously.

 

62 Finally, even if all the conditions of unjust enrichment had been met, Macdonald J.A. disagreed with the trial judge's disposition. In his view, there was not a sufficient nexus between the appellant's contribution and the Sicamous property to entitle the appellant to receive, by way of relief, the property itself rather than a monetary judgment. He decided at p. 272 that the "relatively minor gardening activities and household tasks and expenditures over the 12 years of cohabitation" fell short of establishing a positive contribution to the acquisition, preservation, maintenance or improvement of the property. As a result, it was held that there was no legal ground upon which an order could be made transferring the property to the appellant. The appeal was allowed and the appellant's action was dismissed.

**Position of the Respondent**

63 The respondent conceded that there was an unjust enrichment but contended that there was no corresponding deprivation suffered by the appellant. It was said that she was adequately compensated for her services by the respondent's provision of free shelter and a large portion of the groceries.

64 Second, it was argued that the domestic services provided by the appellant did not establish any causal link to or proprietary interest in the Sicamous property.

65 The Court of Appeal clearly agreed with the respondent on these issues. With respect, I believe they erred in reaching these conclusions.

**Should the Doctrines of Unjust Enrichment and Constructive Trust be Applied to "Common Law" Relationships?**

66 It may be helpful to review once again the application and extension of the doctrine of constructive trust. In Scott, *The Law of Trusts*, vol. 5 (4th ed. 1989) at p. 304 the following definition appears:

> A constructive trust arises where a person who holds title to property is subject to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to retain it. [Footnote omitted.]

67 This definition, which appeared in the same form in earlier editions, was cited with approval in the dissenting reasons of Laskin J. (as he then was) in *Murdoch v. Murdoch*, [1975] 1 S.C.R. 423 [[1974] 1 W.W.R. 361]. In later decisions of this Court the definition has provided a basis for the application of the constructive trust remedy in matrimonial situations.

68 In *Pettkus v. Becker*, [1980] 2 S.C.R. 834, Dickson J. (as he then was) writing for the majority, applied the doctrine of constructive trust to a common law relationship. He noted that a court must first determine whether a claim for unjust enrichment has been established. If it has, then a court must determine whether, in the circumstances presented, a constructive trust is the appropriate remedy to apply to redress the unjust enrichment. In order to determine that there has been an unjust enrichment, the following three conditions must be fulfilled:

69 (1) there has been an enrichment;

70 (2) a corresponding deprivation has been suffered by the person who supplied the enrichment; and

71 (3) there is an absence of any juristic reason for the enrichment itself.

72 The importance of *Pettkus v. Becker*, was emphasized in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426 [35 B.C.L.R. (2d) 145, [1989] 3 W.W.R. 385]. There at p. 471 Dickson C.J. wrote:

> The constructive trust has existed for over two hundred years as an equitable remedy for certain forms of unjust enrichment ... Until the decision of this Court in *Pettkus v. Becker*, the constructive trust was viewed largely in terms of the law of trusts, hence the need for the existence of a fiduciary relationship. In *Pettkus v. Becker*, the Court moved to an approach more in line with restitutionary principles by explicitly recognizing constructive trust as one of the remedies for unjust enrichment.

  

73 Subsequently, this Court made it clear that the constructive trust remedy may also be applied in circumstances where the spouse has contributed not to the acquisition of property but rather to its preservation, maintenance or improvement. In *Sorochan v. Sorochan*, supra, Dickson C.J. gave the reasons for a unanimous Court. There the parties had never married but had cohabited on a farm in Alberta from 1940 to 1982. It is significant that before the parties began living together the defendant was, together with his brother, the owner of the farmland. Thus the lands were not acquired during the period of cohabitation. During the time they lived together the parties had 6 children. The plaintiff did all the domestic work associated with running the household and caring for the children. Both parties worked on the farm. It was conceded that the plaintiff did substantial and arduous work. For many years the defendant worked as a travelling sales representative and during those periods the plaintiff frequently assumed sole responsibility for the work on the farm.

74 It was held that the defendant had been unjustly enriched. That enrichment resulted from his receiving the benefit of the plaintiff's years of labour in the home and on the farm. This obviously resulted in valuable savings. It was pointed out that through the plaintiff's years of labour, the farm was maintained and preserved and did not deteriorate through neglect or disuse. It was found that the plaintiff's maintenance and preservation of the land coffered a significant benefit to the defendant.

75 Thus, it can be seen that the remedy provided by the constructive trust may, in appropriate cases, be applied to common law relationships where the plaintiff's contribution to the land was directed only to its maintenance and preservation. Those contributions which have been considered sufficient to justify the application of a constructive trust have been indirect financial contributions as in *Pettkus v. Becker*, supra, and work on the property which contributed to its maintenance as in *Sorochan*.

**Should the Remedy of Constructive Trust be Applied to the Case at Bar?**

***1. Enrichment***

76 It should not be forgotten that the trial judge specifically found that there had been an enrichment to the respondent "since he obtained the services of the plaintiff as a housekeeper, homemaker and in fact stepmother without compensation." Indeed, it was conceded before us that the respondent was enriched by the work and contributions of the appellant.

***2. A Corresponding Deprivation***

77 It is again important to first consider the finding of the trial judge on this issue. He stated:

> ... the plaintiff was deprived of any compensation for her labour since she devoted the majority of her time and energy and some of the monies she earned towards the benefit of the respondent, his children and his property.

78 That finding would seem sufficient in itself to warrant the conclusion that the appellant suffered a deprivation which corresponds to the enrichment of the respondent.

79 Indeed, I would have thought that if there is enrichment, that it would almost invariably follow that there is a corresponding deprivation suffered by the person who provided the enrichment. There is ample support for the proposition that once enrichment has been found, the conclusion that the plaintiff has suffered a corresponding deprivation is virtually automatic. In *Sorochan*, supra, Dickson C.J. suggested that benefit and deprivation are essentially two sides of the same coin. He wrote at pp. 45-46:

> Moreover, the case law indicates that the full-time devotion of one's labour and earnings without compensation can readily be viewed as a deprivation. In *Murray v. Roty* (1983), 41 O.R. (2d) 705 (Ont. C.A.), for example, a case involving a joint business and farm operation, Cory J.A., commented (at p. 710): "For eight years of her life she devoted all of her time and energy and almost all of her wages for the benefit of Roty. The deprivation is obvious".

In *Everson v. Rich* (1988), 16 R.F.L. (3d) 337, the Saskatchewan Court of Appeal, applying *Sorochan*, stated at p. 342:

> The spousal services provided by the appellant were valuable services and did constitute a benefit conferred upon the respondent. The provision of those services was a detriment to the claimant by virtue of the use of her time and energy.

  

80 I agree with his reasoning. As a general rule, if it is found that the defendant has been enriched by the efforts of the plaintiff there will, almost as a matter of course, be deprivation suffered by the plaintiff. As Professor James McLeod pointed out ((1988), 16 R.F.L. (3d) 338) in his annotation of *Everson v. Rich*, supra, "the deprivation requirement is satisfied by showing the plaintiff expended effort or does not have what he/she had or might have had." Particularly in a matrimonial or long term common law relationship it should, in the absence of cogent evidence to the contrary, be taken that the enrichment of one party will result in a deprivation of the other.

81 Business relationships concerned with commercial affairs may, as a result of the conduct of one of the corporations involved, result in a court's granting a constructive trust remedy. The constructive trust has been appropriately used to redress a gain made through a breach of trust in a commercial or business relationship (See for example: *Canadian Aero Service Ltd. v. O'Malley*, [1974] S.C.R. 592). Yet how much closer and trusting must be a long term common law relationship. In marriages or marriage-like relationships commercial matters and a great deal more will be involved. Clearly, parties to a family relationship will, in a commercial sense, share funds and financial goals. More importantly, couples such as the parties to this case will strive to make a home. By that I mean a place that provides safety, security and love and which is as well frequently the place where children may be cared for and nurtured. In a relationship that involves living and sleeping together, couples will share their worst fears and frustrations and their fondest dreams and aspirations. They will plan and work together to achieve their goals. Just as much as parties to a formal marriage, the partners in a long term common law relationship will base their actions on mutual love and trust. They too are entitled, in appropriate circumstances, to the relief provided by the remedy of constructive trust.

82 This remedy should be granted despite the fact that family will seldom keep the same careful financial records as business associates. Nonetheless, fairness requires that the constructive trust remedy be available to them and applied on an equitable basis without a minute scrutiny of their respective financial contributions. Indeed, in a situation such as the one presented in this case, it may be very difficult to assess the value of making a house a home and of sharing the struggle to raise children to become responsible adults.

83 In the present case, although there was no formal marriage, the couple lived and worked together in the most intimate of relationships. They shared work and the monies which they earned. The amount of the contributions may have been varied and unequal. Yet the very fact that in addition to her household work the appellant contributed something of the income from her outside employment indicates that there was a real sharing of income. As a result of the relationship, the Sicamous property was looked after and maintained. None of this could have been achieved without the efforts of the appellant.

84 Certainly, it cannot be said that the relationship was so short-lived that it should not give rise to mutual rights and obligations. Twelve years is not an insignificant period of time to live in a relationship based on mutual trust and confidence. In those circumstances, there is a strong presumption that the services provided by one party will not be used solely to enrich the other. Both the reasonable expectations of the parties and equity will require that upon the termination of the relationship, the parties will receive an appropriate compensation based on the contribution each has made to the relationship.

85 The respondent asserts that because the appellant loved him she could not have expected to receive compensation or an interest in the property in return for the contributions she made to the home and family. However, in today's society it is unreasonable to assume that the presence of love automatically implies a gift of one party's services to another. Nor is it unreasonable for the party providing the domestic labour required to create a home to expect to share in the property of the parties when the relationship is terminated. Women no longer are expected to work exclusively in the home. It must be recognized that when they do so, women forgo outside employment to provide domestic services and child care. The granting of relief in the form of a personal judgment or property interest to the provider of domestic services should adequately reflect the fact that the income earning capacity and the ability to acquire assets by one party has been enhanced by the unpaid domestic services of the other. Marcia Neave in "Three Approaches to Family Property Disputes — Intention/Belief, Unjust Enrichment and Unconscionability", in T.G. Youdan, ed., *Equity, Fiduciaries and Trusts* (1989), lucidly sets out the position in this way at p. 254:

> The characterization of domestic services as gifts reflects a view of family relationships which is now out-dated and has a differential impact on women, since they are the main providers of such services. Women no longer work exclusively in

  

> the home. Those who do so sacrifice income that could otherwise be earned in paid work. Couples who decide that one partner, usually the woman, will forgo paid employment to provide domestic services and provide child care, presumably believe that this arrangement will maximize their economic resources. Grant of relief, whether personal or proprietary, to the provider of domestic services would recognize that the income-earning capacity of one partner and his ability to acquire assets have been enhanced by the unpaid services of the other and that those services were only provided free because it was believed that the relationship would continue.

86 This same reasoning has been recently applied in the context of divorce in *Moge v. Moge*, [1992] 3 S.C.R. 813 [[1993] 1 W.W.R. 481]. It is appropriate to recognize that the same principle should be applied to long term common law relationships.

87 In the present case it cannot be said, as the respondent suggests, that the contributions of the appellant were minor or that they were compensated by the provision of free accommodation. It is true that the appellant did not devote all of her energy to the home or family business as did Mary Sorochan or Charlotte Murray. However, the mere fact that the appellant was able to engage in part-time employment does not detract from the fact that she provided extensive and valuable services to the respondent for which she was not compensated.

88 It cannot be forgotten that the trial judge recognized that the appellant worked to create a "home" for the respondent. The nature and extent of her efforts were clear from the evidence, but one rather touching indication of her dedication is that she helped the children to make Christmas gifts. The value of the commitment of a homemaker such as the appellant should not be underestimated. The partner who provides domestic services often works far in excess of 40 hours per week in order to provide a "home". Women who work in the home may have given up a career or a type of work which would enable them to improve their earning capacity. These are matters which should be taken into account when considering both the benefits conferred and the deprivation suffered by a claimant who has been a partner in a long term common law relationship.

89 The balancing of benefits conferred and received in a matrimonial or common law relationship cannot be accomplished with precision. Although it may well be essential in a commercial relationship to closely scrutinize the contributions made by each of the business partners to the acquisition of property, such an approach would be unrealistic and unfair in the context of a family relationship. Ordinarily, the trial judge will be in the best position to assess all the evidence presented and to estimate the contribution made by each of the parties. The nature of the relationship, its duration and the contributions of the parties must be considered. Equity and fairness should form the basis for the assessment. There was ample evidence presented in this case to justify the finding of the trial judge that there had been a deprivation suffered by the appellant.

**Absence of Juristic Reason for the Enrichment**

90 In *Pettkus v. Becker*, supra, Dickson J. had this to say at p. 849 with regard to juristic reasons for the enrichment:

> ... I hold that where one person in a relationship tantamount to spousal prejudices herself in the reasonable expectation of receiving an interest in property and the other person in the relationship freely accepts benefits conferred by the first person in circumstances where he knows or ought to have known of that reasonable expectation, it would be unjust to allow the recipient of the benefit to retain it.

91 The test put forward is an objective one. The parties entering a marriage or a common law relationship will rarely have considered the question of compensation for benefits. If asked, they might say that because they loved their partner, each worked to achieve the common goal of creating a home and establishing a good life for themselves. It is just and reasonable that the situation be viewed objectively and that an inference be made that, in the absence of evidence establishing a contrary intention, the parties expected to share in the assets created in a matrimonial or quasi-matrimonial relationship, should it end.

92 *Kshywieski v. Kunka Estate* (1986), 50 R.F.L. (2d) 421, [[1986] 3 W.W.R. 472], is a decision of the Manitoba Court of Appeal. It determined that, in the absence of evidence of a promise of marriage, a promise of compensation or an expectation on the part of the plaintiff that she would be remunerated for her services, it was not unjust for the defendant or his estate to retain the benefit of the spousal service conferred upon him by the plaintiff. Professor McLeod in his annotation ((1986), 50 R.F.L. (2d) 421) summarized the conclusion in this case in these words at p. 422:

  

> Without some prejudicial conduct such as request, inducement, acquiescence or the holding out of future benefit, no restitutionary relief could be awarded.

93 In the case at bar the British Columbia Court of Appeal relied on the *Kshywieski* decision. It concluded that because the respondent's promises to marry the appellant were made when he was drunk, she could not have taken them seriously. As a result, it was found that there was no prejudice occasioned by the appellant. In my view, the Court of Appeal was in error in this conclusion.

94 It is not necessary that there be evidence of promises to marry or to compensate the claimant for the services provided. Rather, where a person provides "spousal services" to another, those services should be taken as having been given with the expectation of compensation unless there is evidence to the contrary. This was the approach properly taken by the Saskatchewan Court of Appeal in *Everson v. Rich*, supra.

95 In the case at bar, the trial judge appropriately drew the inference that, in light of the duration of the relationship and the appellant's contribution to the home and property, she would reasonably have had an expectation of sharing the wealth she helped to create. He concluded that:

> ... there is no juristic reason for the enrichment. She was under no obligation to perform the work and assist in the home without some reasonable expectation of receiving something in return other than the drunken physical abuse which she received at the hands of the respondent.

96 When a claimant is under no obligation contractual, statutory or otherwise to provide the work and services to the recipient, there will be an absence of juristic reasons for the enrichment. See *Murray v. Roty* (1983), 41 O.R. (2d) 705; *Pettkus v. Becker*, supra; *Sorochan v. Sorochan*, supra.

97 In summary then, there was unjust enrichment of the respondent by the work of the appellant. The appellant suffered a corresponding deprivation. There was no juristic reason for the enrichment, that is to say there was no obligation of any kind upon the appellant to provide the services to the respondent. It follows that the trial judge was correct in his finding that there had been an unjust enrichment, a corresponding deprivation and no juristic reason for providing the enriching services. It remains to be considered what remedy should have been provided in the circumstances. Would a monetary judgment have been appropriate or should the remedy of constructive trust have been granted?

**The Appropriate Remedy**

98 In *Sorochan v. Sorochan*, it was noted that although the constructive trust provides an important judicial means of remedying unjust enrichment, there are other remedies available, such as monetary damages. The first question to be resolved is which remedy is appropriate in the circumstances of this case? In *Sorochan* it was said that: the court must consider whether there is a causal connection between the deprivation suffered by the plaintiff and the property in question, because in order to justify the imposition of a constructive trust a court must be satisfied that there is a "clear proprietary relationship" between the services rendered and the disputed assets. The same case confirmed that a flexible approach should be taken in applying the constructive trust remedy and specifically approved of the position adopted by other courts in *Murray v. Roty*, supra; *Hussey v. Palmer*, [1972] 1 W.L.R. 1286; *Lawrence v. Lindsey* (1982), 28 R.F.L. (2d) 356 (Alta. Q.B.). At p. 50, Dickson C.J. wrote:

> In my view, the constructive trust remedy should not be confined to cases involving property acquisition. While it is important to require that some nexus exist between the claimant's deprivation and the property in question, the link need not always take the form of a contribution to the actual acquisition of the property. A contribution relating to the preservation, maintenance or improvement of property may also suffice.

99 In addition to the causal connection requirement Dickson C.J. stated that the claimant must have reasonably expected to receive an interest in the property and that the respondent ought to have been aware of that expectation. He also observed that in considering whether a constructive trust is the appropriate remedy the duration of the relationship should be taken into account.

 

100 The difficulty of establishing a causal connection between unjust enrichment arising from the provision of domestic services and the property has been the subject of scholarly debate (See for example: Ralph E. Scane "Relationships 'Tantamount to Spousal', Unjust Enrichment, and Constructive Trusts" (1991), 70 Can. Bar Rev. 260; Keith B. Farquhar, "Causal Connection in Constructive Trusts" (1986-88), 8 Est. & Tr. Q. 161; Berend Hovius and Timothy G. Youdan, *The Law of Family Property* (1991); Ian Narev, "Unjust Enrichment and De Facto Relationships" (1991), 6 Auckland U.L. Rev. 504). As Professor Ralph Scane (at p. 289) put it, the difficulty with looking for a causal connection in such cases is "that the unjust enrichment created by receipt the benefit of [domestic] services ... seeps throughout all of the assets of the defendant". Thus, the contributions which indirectly created accumulated family wealth for the parties cannot be traced to any one property. However, I do not think that the required link between the deprivation suffered and the property in question is as difficult to establish as it may seem.

101 This Court has specifically recognized that indirect financial contributions to the maintenance of property will be sufficient to establish the requisite property connection for the imposition of a constructive trust. In *Pettkus v. Becker*, supra, the fact that Ms. Becker paid the rent, purchased the food and clothing and looked after other living expenses, enabled Mr. Pettkus to save his entire income, a goodly amount of money which he later used to purchase property. Even though Ms. Becker's financial contributions did not directly finance the purchase of the property, it was held that her indirect financial contribution was sufficient to entitle her to a proprietary interest in the property purchased by Mr. Pettkus upon the dissolution of the relationship.

102 It seems to me that in a family relationship the work, services and contributions provided by one of the parties need not be clearly and directly linked to a specific property. As long as there was no compensation paid for the work and services provided by one party to the family relationship then it can be inferred that their provision permitted the other party to acquire lands or to improve them. In this case the work of the appellant permitted the respondent to pay off the mortgage and, as well, to purchase a houseboat and a cabin cruiser. In the circumstances, the trial judge was justified in applying the constructive trust to the property which he felt would best redress the unjust enrichment and would treat both parties in a just and equitable manner.

103 Goff and Jones support the imposition of a constructive trust in family situations where the plaintiff's contributions cannot be traced to a particular property (*The Law of Restitution* (3rd ed., 1984)). They rely on the case of *Chase Manhattan Bank N.A. v. Israel-British Bank (London) Ltd.*, [1981] Ch. 105, where the plaintiff paid under a mistake of fact over $2 million to the defendants, who discovered the mistake within two days, did nothing to correct it and went into liquidation some four weeks later. Goulding J. held that the defendant was a constructive trustee of the money paid under mistake. But he left open the question whether equity's traditional tracing rules should be applied in order to identify the plaintiff's payment. Goff and Jones maintain that if the tracing rules were applied then it is extremely unlikely that the plaintiff's claim would succeed. Yet, as they point out, it would seem unjust to allow the defendant's general creditors to benefit from the mistaken payment when the defendant knew of the mistake and did nothing to correct it. Therefore, the authors argue on p. 80 of their book that:

> To protect a plaintiff the court will have to impose a trust on, or a lien over, the defendant's unencumbered assets for the plaintiff's benefit even if those assets cannot be "identified" through the application of traditional equitable tracing rules. If a court reaches this conclusion it will do so because it recognises that a trust or lien should be imposed simply because the defendant's assets were swollen by the mistaken payment.

104 In *Lac Minerals Ltd. v. International Corona Resources Ltd.*, [1989] 2 S.C.R. 574, it was determined that the constructive trust is not reserved to situations where a right of property is recognized. As a remedy, the constructive trust may be used to *create* a right of property and this obviates the need to find a pre-existing property right by means of equitable tracing rules. However, La Forest J. indicated that a restitutionary proprietary remedy should not automatically be granted. He found that, since proprietary rights give the plaintiff priority over the legitimate claims of third party creditors, further guidance was needed for determining those situations in which it would be appropriate to award a proprietary remedy. Thus, La Forest J. concluded that the constructive trust should only be awarded when the personal monetary award is insufficient; that is, when there is reason to grant to the plaintiff the additional rights that flow from recognition of a right of property.

105 I agree with my colleague that there is a need to limit the use of the constructive trust remedy in a commercial context. Yet I do not think the same proposition should be rigorously applied in a family relationship. In a marital or quasi-marital relationship,

  

the expectations the parties will have regarding their contributions and interest in the assets acquired are, I expect, very different from the expectation of the parties engaged in a commercial transaction. As I have said, it is unlikely that couples will ever turn their minds to the issue of their expectations about their legal entitlements at the outset of their marriage or common law relationship. If they were specifically asked about their expectations, I would think that most couples would probably state that they did not expect to be compensated for their contribution. Rather, they would say, if the relationship were ever to be dissolved, then they would expect that both parties would share in the assets or wealth that they had helped to create. Thus, rather than expecting to receive a fee for their services based on their market value, they would expect to receive, on a dissolution of their relationship, a fair share of the property or wealth which their contributions had helped the parties to acquire, improve, or to maintain. The remedy provided by the constructive trust seems to best accord with the reasonable expectations of the parties in a marriage or quasi-marital relationship. Nevertheless, in situations where the rights of bona fide third parties would be affected as a result of granting the constructive trust remedy it may well be inappropriate to do so. (See: Berend Hovius and Timothy G. Youdan, *The Law of Family Property*, at p. 146.)

106 It follows that in a quasi-marital relationship in those situations where the rights of third parties are not involved, the choice between a monetary award and a constructive trust will be discretionary and should be exercised flexibly. Ordinarily both partners will have an interest in the property acquired, improved or maintained during the course of the relationship. The decision as to which property, if there is more than one, should be made the subject of a constructive trust is also a discretionary one. It too should be based on common sense and a desire to achieve a fair result for both parties.

107 There will of course be situations where an award for a monetary sum may be the most appropriate remedy. For example where the relationship is of short duration or where there are no assets surviving its dissolution, a monetary award should be made. Professors Berend Hovius and Timothy G. Youdan (*Law of Family Property*, at p. 147) provide the following list of factors which I think are helpful in determining that a monetary distribution may be more appropriate than a constructive trust:

108 (a) is the "plaintiff's entitlement ... relatively small compared to the value of the whole property in question";

109 (b) is the "defendant ... able to satisfy the plaintiff's claim without a sale of the property" in question;

110 (c) does "the plaintiff [have any] special attachment to the property in question";

111 (d) what "hardship might be caused to the defendant if the plaintiff obtained the rights flowing from [the award] of an interest in the property."

112 In this case the appellant contributed to the maintenance and the preservation of the home. She painted the fence, planted the cedar hedge, installed the rock garden and built the chicken coop. Nevertheless, her principal contribution was made through the provision of domestic services. Her work around the house and in caring for the children saved the respondent the expense of hiring a housekeeper and someone to care for the children. As a result he was able to use the money which he had saved to purchase other property and to pay off the mortgage on the Sicamous property.

113 The trial judge found, that since the respondent was now retired and living on a War Veteran's Allowance, a monetary award would be "impracticable, probably unrealistic and would not be reasonable under the circumstances" and imposed a constructive trust upon the Sicamous property. I think he was correct in doing so. It could reasonably be inferred that given the work she had done, the appellant would expect to receive a share in the Sicamous property when the relationship ended. Further, although there was no specific evidence that the appellant had formed an emotional attachment to the property, it would not have been unreasonable for the trial judge to have inferred this in light of the work which she had done on the property. In addition, the property was vacant at the time of the trial and the respondent was retired and living on his veteran's pension in another community. Clearly, he has no particular attachment to the property. A monetary award would be meaningless. Therefore, it was both reasonable and appropriate to choose the Sicamous property as the object of the constructive trust. In the circumstances of this case, the application of the constructive trust remedy was eminently suitable.

**Was the Amount of the Appellant's Interest Reasonably Determined?**

  

114 There are, generally speaking, two methods of evaluating the contribution of a party in a matrimonial relationship. The first method is based upon the value received. This can be thought of as quantum meruit, that is the amount the defendant would have had to pay for the services on a purely business basis to any other person doing the work that was provided by the claimant. Alternatively, it can be based upon what is termed "value surviving" which apportions the assets accumulated by the couple on the basis of the contributions made by each. Value surviving is the approach that has been traditionally employed in cases of constructive trust. However, there is no reason why quantum meruit or the value received approach could not be utilized to quantify the value of the constructive trust. The remedy should be flexible so that it can be readily adapted to the situation presented in any given case. In many cases the cost of retaining and presenting expert evidence as to the value of the property may be beyond the reach of the parties and at times clearly impractical. This in itself indicates the need for maintaining flexibility in the remedy.

115 Here, the trial judge undertook the same type of quantum meruit analysis employed in *Herman v. Smith* (1984), 42 R.F.L. (2d) 152 (Alta. Q.B.). That is, he calculated the appellant's contributions on the basis of what the respondent would have been required to pay a housekeeper. It has to be noted that his calculations were favourable to the respondent in that he used the amount paid prior to the commencement of the common law relationship as a basis for the calculation and then reduced it by 50 percent to allow for the value of the accommodation that the appellant received from the respondent. This was a fair means of calculating the amount due to the appellant.

116 Nonetheless, I would observe that the value surviving approach will often be the preferable method of determining the quantum of a claimant's share. This method will usually be more equitable and will more closely accord with the expectation of the parties as to how the assets which they have accumulated should be divided upon termination of the relationship. Further, the utilization of the value surviving method will avoid the difficult task of assigning a precise dollar value to the services provided by someone who has dedicated him- or herself to raising children and caring for a home. Instead, the contributions of the parties can more accurately be expressed as a percentage of the accumulated wealth existing at the termination of the relationship. Thus, for pragmatic reasons, the value surviving method may be the preferable one in many cases. No matter which method is used, equity and fairness should guide the court in determining the value and contributions made by the parties. In this case awarding the Sicamous property to the appellant reflected a fair assessment of her contribution to the relationship.

**Disposition**

117 In the result, I would allow the appeal, set aside the order of the Court of Appeal and restore the judgment of the trial judge. The appellant should have her costs throughout these proceedings.

*Appeal allowed.*

**Most Negative Treatment:** Distinguished
**Most Recent Distinguished:** Bison Properties Ltd., Re | 2016 BCSC 793, 2016 CarswellBC 1199, [2016] B.C.W.L.D. 3744, [2016] B.C.W.L.D. 3745, [2016] B.C.W.L.D. 3746, 266 A.C.W.S. (3d) 549, 36 C.B.R. (6th) 66 | (B.C. S.C., May 3, 2016)

2013 MBQB 171
Manitoba Court of Queen's Bench

Puratone Corp., Re

2013 CarswellMan 360, 2013 MBQB 171, [2013] M.J. No. 247, 229 A.C.W.S. (3d) 632, 295 Man. R. (2d) 55

# In the Matter of: The Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

In the Matter of: A Plan of Compromise or Arrangement of The Puratone Corporation, Pembina Valley Pigs Ltd. and Niverville Swine Breeders Ltd. (the "Applicants")

Dewar J.

Judgment: July 8, 2013
Docket: Winnipeg Centre CI 12-01-79231

Counsel: David Jackson, for Puratone Corporation
J.J. Burnell, for Bank of Montreal
Jeffrey Lee, Sandra Zinchuk, for Farm Credit Canada
Richard Schwartz, Jason Harvey, for ITB Claimants
Ross McFadyen, for Deloitte Touche Inc.
David Kroft, Aaron Challis, for Directors and Officers

Subject: Insolvency; Civil Practice and Procedure; Contracts; Corporate and Commercial; Estates and Trusts; Restitution; Torts
**Related Abridgment Classifications**
Bankruptcy and insolvency
XIX Companies' Creditors Arrangement Act
XIX.2 Initial application
XIX.2.f Lifting of stay
**Headnote**
Bankruptcy and insolvency --- Companies' Creditors Arrangement Act — Initial application — Lifting of stay
In September 2012, group of three companies involved in commercial hog production filed application and granted initial order under Companies' Creditors Arrangement Act (CCAA) — Order included usual provision staying commencement or continuation of any proceeding against companies, officers and directors — In November 2012, court approved sale of virtually all of companies' assets to third party — In March 2013, court authorized distribution of majority of proceeds of sale to major secured creditors, each of whom sustained significant shortfall — Monitor retained $6.75 million, including $5 million as general holdback, pending completion of CCAA proceeding — Claimants, group of farmers who had supplied grain to companies in two weeks prior to CCAA filing, and who remained unpaid, requested holdback of $903,250 and sought leave to commence action against companies as well as officers and directors for, among other things, damages for fraudulent misrepresentation and declaration of constructive trust on basis of unjust enrichment — Claimants alleged companies, officers and directors must have known that CCAA application, made for purpose of liquidation rather than true restructuring, intended at time grain supplied — Major secured creditors objected on basis proposed action had insufficient merit to justify delay in distribution of holdback moneys — Claimants brought motion for order authorizing commencement of action — Motion granted — Section 11.02(3) of CCAA authorized court to lift stay of proceedings where appropriate and applicant acting in good faith and with due

  

diligence — Judicial authority required "sound reasons", considering balance of convenience, prejudice and merits of proposed action — Scrutiny of proposed action and circumstances suggested dismissal of action not foregone conclusion — Proposed action essentially priority dispute between creditors — Since CCAA proceeding almost over, lifting stay would not put any restructuring plan at risk — Balance of convenience favoured claimants — Holdback of $903,250 would not prejudice secured creditors to significant degree if claimants filed undertaking as to damages.

**Table of Authorities**

**Cases considered by *Dewar J.*:**

*ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.* (2007), 2007 SKCA 72, 2007 CarswellSask 324, [2007] 9 W.W.R. 79, *(*sub nom. *Bricore Land Group Ltd., Re)* 299 Sask. R. 194, *(*sub nom. *Bricore Land Group Ltd., Re)* 408 W.A.C. 194, 33 C.B.R. (5th) 50 (Sask. C.A.) — followed

*International Corona Resources Ltd. v. LAC Minerals Ltd.* (1989), 44 B.L.R. 1, 35 E.T.R. 1, *(*sub nom. *LAC Minerals Ltd. v. International Corona Resources Ltd.)* 69 O.R. (2d) 287, *(*sub nom. *LAC Minerals Ltd. v. International Corona Resources Ltd.)* 61 D.L.R. (4th) 14, 101 N.R. 239, 36 O.A.C. 57, *(*sub nom. *LAC Minerals Ltd. v. International Corona Resources Ltd.)* [1989] 2 S.C.R. 574, 6 R.P.R. (2d) 1, *(*sub nom. *LAC Minerals Ltd. v. International Corona Resources Ltd.)* 26 C.P.R. (3d) 97, 1989 CarswellOnt 126, 1989 CarswellOnt 965 (S.C.C.) — considered

*People's Department Stores Ltd. (1992) Inc., Re* (2004), *(*sub nom. *Peoples Department Stores Inc. (Bankrupt) v. Wise)* 326 N.R. 267 (Eng.), *(*sub nom. *Peoples Department Stores Inc. (Bankrupt) v. Wise)* 326 N.R. 267 (Fr.), 4 C.B.R. (5th) 215, [2004] 3 S.C.R. 461, 2004 SCC 68, 2004 CarswellQue 2862, 2004 CarswellQue 2863, *(*sub nom. *Peoples Department Stores Inc. (Trustee of) v. Wise)* 244 D.L.R. (4th) 564, 49 B.L.R. (3d) 165 (S.C.C.) — considered

**Statutes considered:**

*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36

Generally — referred to

s. 11(6) — considered

s. 11.02(3) [en. 2005, c. 47, s. 128] — considered

*Corporations Act*, R.S.M. 1987, c. C225

s. 234 — referred to

**Rules considered:**

*Queen's Bench Rules*, Man. Reg. 553/88

Generally — referred to

R. 46.14(1) — considered

R. 46.14(3) — considered

MOTION by claimants to authorize commencement of action.

***Dewar J.*:**

1 On September 12, 2012, an Initial Order was pronounced by me in a proceeding under the *Companies' Creditors Arrangement Act*, R.S.C., 1985, c. C-36 (the "CCAA") filed on that date by three of the companies within the Puratone umbrella, namely The Puratone Corporation, Pembina Valley Pigs Ltd., and Niverville Swine Breeders Ltd. (hereinafter "Puratone").

2 The Puratone Group of companies ran a commercial hog production business. Their business included the breeding, farrowing, finishing and marketing of hogs. In order to carry on this business, Puratone needed grain to be used in feed for its hogs.

3 This motion involves 17 farming operators who claim priority to some of the proceeds of sale of the assets of the companies covered by the within CCAA proceedings. The lead farming operator, Interlake Turkey Breeders Ltd. claims to be a part of the steering committee for a group of farmers who supplied grain to the Puratone Group of Companies within two weeks of the filing of this CCAA proceeding. I will hereinafter refer to the group of farmers as "the ITB Claimants".

  

4 The Initial Order contained many of the usual provisions, including stay provisions as follows:

> **NO PROCEEDINGS AGAINST THE APPLICANTS OR THE PROPERTY**
>
> 18. THIS COURT ORDERS that until and including October 12, 2012, or such later date as this Court may order (the "Stay Period"), no proceeding or enforcement process in any court or tribunal (each, a "Proceeding") shall be commenced or continued against or in respect of the Applicants or the Monitor, or affecting the Business or the Property, except with the written consent of the Applicants and the Monitor, or with leave of this Court, and any and all Proceedings currently under way against or in respect of the Applicants or affecting the Business or the Property are hereby stayed and suspended pending further Order of this Court.
>
> **NO EXERCISE OF RIGHTS OR REMEDIES**
>
> 19. THIS COURT ORDERS that during the Stay Period, all rights and remedies of any individual, firm, corporation, governmental body or agency, or any other entities (all of the foregoing, collectively being "**Persons**" and each being a "**Person**") against or in respect of the Applicants or the Monitor, or affecting the Business or the Property, are hereby stayed and suspended except with the written consent of the Applicants and the Monitor, or leave of this Court, provided that nothing in this Order shall (i) empower the Applicants to carry on any business which the Applicants are not lawfully entitled to carry on, (ii) affect such investigations, actions, suits or proceedings by a regulatory body as are permitted by Section 11.1 of the CCAA, (iii) prevent the filing of any registration to preserve or perfect a security interest, or (iv) prevent the registration of a claim for lien.
>
> **PROCEEDINGS AGAINST DIRECTORS AND OFFICERS**
>
> 26. THIS COURT ORDERS that during the Stay Period, and except as permitted by subsection 11.03(2) of the CCAA, no Proceeding may be commenced or continued against any of the former, current or future directors or officers of the Applicants with respect to any claim against the directors or officers that arose before the date hereof and that relates to any obligations of the Applicants whereby the directors or officers are alleged under any law to be liable in their capacity as directors or officers for the payment or performance of such obligations, until a compromise or arrangement in respect of the Applicants, if one is filed, is sanctioned by this Court or is refused by the creditors of the Applicants or this Court.

5 Although the Initial Order included the stay provisions for only 30 days ending October 12, 2012, the stays have been extended as a result of a series of motions whilst Puratone has been undergoing its "restructuring". The restructuring referred to has essentially involved the sale of substantially all of its assets to Maple Leaf Foods Inc. on a going concern basis. That sale was approved by the court on November 8, 2012 and closed on December 17, 2012. As part of the order approving the sale, I ordered that the proceeds of sale should be paid to the Monitor to be held pending receipt of a Distribution Order. On March 12, 2013, I granted an order authorizing the distribution of most of the net proceeds from the sale of the assets. The creditors who received funds from the Distribution Order were as follows:

| | |
|---|---|
| a) Bank of Montréal | $17,726,173; |
| b) Farm Credit Corporation | $15,817,303 |
| c) Manitoba Agricultural Services Corporation (MASC) | $1,041,524 |

6 The sworn pre-CCAA claim of Bank of Montréal before receiving this distribution was $43,322,558. The sworn pre-CCAA claim of the Farm Credit Corporation (FCC) before receiving this distribution was $41,025,891.76. The sworn pre-CCAA claim of MASC before receiving the distribution was $5,263,767.

7 There are therefore significant shortfalls being sustained by each of the major secured creditors.

8 The Monitor has retained a sum in an amount of $6,753,765 from the net proceeds. Of this amount, $1,573,765 has been withheld to deal with an issue that has arisen with the purchaser out of the sale and to that extent, as against Puratone and its

  

creditors, the purchaser has the first claim against those funds. A further $5,000,000 was also recommended to be held back. These monies, in addition to whatever might be obtained from the relatively small number of assets yet to be liquidated, are intended to serve as a general holdback pending completion of the CCAA proceedings including the continued realization of remaining assets, resolution of the dispute with the purchaser and potential legal actions.

9 One of the potential legal actions is a claim by the ITB Claimants ("the ITB Claim"). At the time of the application of the Monitor for a Distribution Order, a motion was brought by the ITB Claimants requesting that $903,250.50 be withheld from any distribution to the major secured creditors, and requesting leave to commence an action against Puratone and its directors and/or officers in order to make the said claim. On its initial return date, I adjourned the motion of the ITB Claimants while authorizing the distribution set out above, which contemplated the holdback that had been recommended by the Monitor. I set time frames for the parties to provide briefs and any further affidavit material. On April 10, 2013 the ITB Claimants filed a further notice of motion which amplified their requests. The matter came on for hearing on April 11, 2013 at which time, after hearing submissions, I reserved judgment.

10 The claim of the ITB claimants is that they supplied grain to Puratone on an individual contract basis on various dates between August 29 and September 11, 2012, a period within two weeks of the filing of the CCAA proceeding. It is alleged that the grain was used by Puratone to feed the hogs that were ultimately sold to Maple Leaf Foods Inc. as part of the going concern sale ultimately approved by the court. The ITB Claimants argue that at the time of the supply transactions, Puratone was gearing up for its CCAA application and must have then known that it would have been unable to pay for the grain once an Initial Order was pronounced. In essence, the claim of the ITB Claimants boils down to allegations that Puratone acquired the grain when it had no intention of paying for it. As a result, the ITB claimants argue that they have causes of action against Puratone entitling them to:

a) damages for fraudulent misrepresentation on the part of Puratone;

b) a claim [an order] under s. 234 of *The Corporations Act*, C.C.S.M. c. C225, that Puratone's conduct was oppressive as regards the plaintiffs;

c) a declaration that an implied or constructive trust exists in favour of the plaintiffs, and that Puratone and its secured creditors were unjustly enriched by the feed supplied by the plaintiffs;

d) a declaration that the secured creditors claims are subordinate to those of the plaintiffs, and/or that in equity they subordinated their security to the ITB Claimants;

e) a declaration that Puratone and its directors and officers wrongfully and/or fraudulently caused Puratone to obtain feed from the plaintiffs which they knew would not be paid for;

f) a declaration that the secured creditors colluded with Puratone and/or its directors and officers to, in effect, wrongfully obtain feed which they knew would not be paid for; and

g) a declaration that the secured creditors indemnified, in fact or at law, Puratone and/or its directors and officers by supporting and participating in a process that was designed to ensure that the secured creditors received the benefit of the feed without having to pay for it.

**Analysis**

11 A stay of proceedings is normally included in an Initial Order in order to permit an applicant to proceed with its restructuring (including, in some cases, its liquidation) without continually being harassed by creditors who are dissatisfied with the state of their outstanding accounts. The theory behind the stay order is that it will allow the applicant to devote its full time, efforts and resources to presenting and executing a restructuring plan which is in the best interests of the creditors generally, rather than fighting rearguard actions against individual creditors who are trying to collect their individual accounts.

  

12 A stay of proceedings however can be lifted in the appropriate case, but those cases will be the subject of judicial consideration which normally involves a balancing of stakeholder interests.

13 The CCAA does not set out a specific test identifying the circumstances in which the stay of proceedings should be lifted. Rather, it is in the discretion of the supervising CCAA judge whether a proposed action should be allowed to proceed. Apart from giving the judge the authority to grant the stay, the only guidelines expressed in the CCAA respecting such a stay order are found in section 11.02(3) which says:

> (3) The court shall not make the order unless
>
> (a) the applicant satisfies the court that circumstances exist that make the order appropriate; and
>
> (b) in the case of an order under subsection (2), the applicant also satisfies the court that the applicant has acted, and is acting, in good faith and with due diligence.

14 In *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*, 2007 SKCA 72, [2007] 9 W.W.R. 79 (Sask. C.A.), the Saskatchewan Court of the Appeal indicated that there must be "sound reasons", consistent with the scheme of the CCAA, to relieve against the stay. In the search for "sound reasons", the court suggested the following considerations:

> a) the balance of convenience;
>
> b) the relative prejudice to the parties; and
>
> c) the merits of the proposed action.

It also indicated that, "The supervising CCAA judge should also consider the good faith and due diligence of the debtor company as referenced in s. 11(6)".

15 In my respectful view, these considerations are all to be viewed together and in the context of the nature and timing of the CCAA process before the court. The same request may very well receive a different reception in the case of an application for the lifting of a stay early in a CCAA proceeding that contemplates a true restructuring than in the case of an application brought late in a CCAA proceeding that involves only the sale of assets. In the former situation, the existence of a contemporaneous action might jeopardize the ability of the company to restructure as intended. In the latter case, the restructuring, such as it is, has been accomplished and the only issue being left to sort through is who is entitled to the money. In my view, a court would be more receptive to lifting the stay in the latter case than in the former.

***The stay respecting claims against Puratone***

16 The motion of the ITB Claimants was opposed by Bank of Montréal and FCC. They essentially argued that the ITB Claimants had not demonstrated the existence of a cause of action with enough of a reasonable prospect of success to justify a delay in the distribution of the holdback monies to the secured creditors. In short they focused on the third of the considerations described in *ICR Commercial Real Estate (Regina) Ltd.*. They argued that the proposed claim of the ITB Claimants for a constructive trust respecting some of the assets of Puratone would fail for a number of reasons, namely:

> a) The sale of grain by the ITB Claimants involved transactions that do not qualify for the application of the doctrines of unjust enrichment, or equitable subordination. These transactions were essentially commercial transactions as between buyer and seller. It was argued that an unpaid seller is simply a debtor of Puratone. Although Puratone has received a benefit, the normal buyer-seller relationship provides a juristic reason for the benefit, and therefore the doctrine of unjust enrichment does not apply. Furthermore the banks argued that the doctrine of equitable subordination has never been recognized in Canada.

  

b) The secured creditors are to be viewed as *bona fide* third parties with a commercial interest in the assets of Puratone and the ITB Claimants should not be entitled to jump the queue from the status of unsecured creditors and receive a priority ahead of secured creditors who hold valid and properly registered securities.

c) It is impossible to trace the grain into the hogs that were ultimately sold during the CCAA proceedings. Therefore, the ITB Claimants have no claim to the proceeds of sale of the hogs.

17 Counsel for the ITB Claimants has argued that this situation is a relatively new phenomenon. Historically, CCAA proceedings involved the restructuring of a company to permit it to carry on its business. CCAA proceedings in days gone by were not intended to be used where there were no future plans for the company. Counsel for the ITB Claimants argued that in this case, the plan was always to liquidate the assets in a controlled way in order to maximize the return to the secured creditors, but with the expectation that a shortfall would invariably occur to the secured creditors. He submitted that it must have been well known to Puratone as well as its secured creditors and directors and officers that at the time that the grain was supplied by the ITB claimants, Puratone was deeply underwater to its secured creditors. He argued that the evidence of knowledge of such insolvent condition can be inferred by the large shortfall suffered by Bank of Montréal and FCC notwithstanding a going concern sale which was negotiated during the CCAA proceedings only two months after the feed was supplied by the ITB Claimants. Counsel submits that CCAA applications of the scale of this proceeding are not prepared overnight, and that at the time of the supply of grain, Puratone would have been preparing its CCAA materials and would have known that the CCAA proceedings would only yield a sale which resulted in large secured creditor deficiencies. He argued that at the time of these contracts of supply, there was no likelihood that the ITB claimants would receive any of their money. He argued that by ordering the grain under these circumstances, essentially Puratone was perpetrating a fraud on the ITB claimants.

18 It was urged upon me by counsel for the two banks that the case authorities require a judge to scrutinize the claim which a creditor intends to advance before lifting the stay in a CCAA proceeding. It was argued that the authorities suggest that the test to be employed in lifting a CCAA stay is more than the test used in striking out a statement of claim as disclosing no cause of action or being frivolous and vexatious, but does not require prospective plaintiffs to demonstrate a *prima facie* case. The terms "reasonable cause of action" or "tenable case" have sometimes been used.

19 In the *ICR* case, at paragraph 64 and 65, Jackson, JA wrote:

[64] Koch J. used *prima facie* case, which he equated with tenable cause of action. "Tenable cause of action" is taken from Ground J.'s decision in Ivaco, but Ground J. used "reasonable cause of action" or "tenable case," as comparable terms and as only one of four criteria to be considered. The use of "*prima facie* case" defined as "tenable cause of action" is not particularly helpful as the words have been used in different contexts with different purposes in mind. Even in the context of bankruptcy where specific guidelines are given, and the courts have had long experience with the application of the tests, the debate continues as to what is meant by *prima facie* case and whether it is too high of a standard to apply in determining whether an action may be commenced.

[65] Koch J. was clearly correct to hold that the threshold established by s. 173 of *The Queen's Bench Rules* is too low. On the other hand, it is also important not to decide the case. The purpose for passing on the claim is not to determine whether it will or will not succeed, but to determine whether the plan of arrangement should be delayed or further compromised to accommodate a future claim, or some other step need be taken to maintain the integrity of the CCAA proceeding.

(Emphasis added)

20 When I scrutinize the proposed claim of the ITB Claimants against Puratone, I conclude that its dismissal is not a foregone conclusion. The ITB Claimants raise a point which so far as I am aware has not been addressed by this court. Here, the court is faced with a CCAA proceeding which has had from the outset all of the earmarks of a liquidation proceeding. The affidavit of Raymond Hildebrand, sworn September 12, 2012 underlying the request for the Initial Order as well as the Pre-Filing Monitor's Report outlined the financial difficulties being experienced by Puratone, the reasons for those difficulties, as well as the efforts that had been made by Puratone and its restructuring professionals to deal with them. Some of the efforts had included a Sales

  

and Solicitation Process ("SISP"), a process designed to find people who were willing to inject money into Puratone either through a going concern sale of assets or in equity injection. Those efforts failed.

21 In the Pre-Filing Report of Deloitte & Touche Inc., the then Proposed Monitor wrote:

> 46 The Proposed Monitor has been advised that the SISP, as originally proposed, failed to result in a successful investment or sale transaction. Accordingly, the SISP has been terminated and replaced with a short-term, expedited strategy to complete a sale of the business, or parts thereof, which will be undertaken by the Applicants with the assistance of the Proposed Monitor (the "Sales Process").

22 The Initial Order was granted based on information, *inter alia*, that the major secured creditors were Bank of Montréal and FCC. As indicated earlier, less than three months later, the parties were recommending a sale which would result in large secured creditor shortfalls. The ITB Claimants argue that this result must have been contemplated by Puratone at the time that the ITB Claimants supplied their grain to Puratone. This raises the interesting question as to whether that expectation was in the mind of Puratone at the time that the grain was supplied, and if so, whether the ITB Claimants are entitled to any relief from Puratone other than a meaningless monetary judgment. It raises the issue whether a company with exposed secured creditors should be incurring credit at a time when it is preparing to make a CCAA application.

23 The ITB claimants request a constructive trust over the assets of Puratone that were sold during the CCAA proceeding which, if ordered, would erode the assets over which the banks claim security by the amount of the unpaid accounts of the ITB Claimants. A constructive trust has been recognized as a remedy against a debtor in the event that there has been a fraud. In Peter D. Maddaugh and John D. McCamus, The Law of Restitution, (looseleaf), Volume 1, at paragraph 5:200.30, the following is written:

> Chancery's willingness to impose a constructive trust in circumstances where a fraud has been perpetrated is by no means a modern development. No preexisting fiduciary relationship need be established for this category of constructive trust and, indeed, a breach of trust or other fiduciary obligation is, in itself, simply one form of equitable fraud. As Lord Westbury explained in *McCormick v. Grogan*: "it is a jurisdiction by which a Court of Equity, proceeding on the ground of fraud, converts the party who has committed it into a trustee for the party who is injured by that fraud." And, in *Westdeutsche Landesbank Girozentrale v. Islington L.B.C.*, Lord Browne-Wilkinson recognized that "when property is obtained by fraud equity imposes a constructive trust on the fraudulent recipient: the property is recoverable and traceable in equity". For example, one who acquires property by theft or fraudulent misrepresentation may be held a constructive trustee of the misappropriated property.

24 The question arises whether there is any practical reason for permitting the ITB Claimants to make their claim against Puratone at this time. Courts will generally not impose a constructive trust where the remedy jeopardizes the priority of innocent parties for value. In this regard, see *International Corona Resources Ltd. v. LAC Minerals Ltd.*, [1989] 2 S.C.R. 574 (S.C.C.), where LaForest J says:

> 197 ...In the vast majority of cases a constructive trust will not be the appropriate remedy. Thus, in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, *supra*, had the restitutionary claim been made out, there would have been no reason to award a constructive trust, as the plaintiff's claim could have been satisfied simply by a personal monetary award; a constructive trust should only be awarded if there is reason to grant to the plaintiff the additional rights that flow from recognition of a right of property. Among the most important of these will be that it is appropriate that the plaintiff receive the priority accorded to the holder of a right of property in a bankruptcy....

The banks argue that there is no evidence that they are anything but innocent parties in these circumstances. Counsel for the two banks argue that there is no affidavit evidence adduced by the ITB Claimants that indicates that the banks were knowledgeable about any fraudulent intent on the part of Puratone, even if such existed. They argue that the court should not lift the stay simply on the basis that the ITB Claimants make such an unsubstantiated allegation. Rather it is argued that the banks should, for the purpose of this motion, be assumed to have had no knowledge of any bad intent that is alleged to have been possessed on the

  

part of Puratone, and that being the case, there is no prospect, let alone a reasonable prospect, that the ITB Claimants will be successful in obtaining a constructive trust at the end of the day.

25 The problem which I see with this submission is that evidence of the knowledge of the banks at the material times is a factual matter that is not readily apparent. Evidence such as that would normally only surface during the discovery process in civil litigation. The banks have chosen to file no affidavit material in this motion. It seems too high a threshold to require the ITB Claimants to demonstrate the knowledge of the banks at the material times on this motion. For current purposes, it is sufficient to conclude that given the size of the troubled loans, a reasonable inference is that the two banks who appeared to oppose the ITB Claimants motion would have been aware of the pending CCAA proceedings before they were filed, and at the time that the grain was being supplied, bank representatives would have had more than a cursory understanding of the business of Puratone and its financial difficulties. Whether the banks were aware that Puratone was purchasing grain on other than a COD basis after the decision had been made to apply for a CCAA order, and if so, whether the banks were in any position to do anything about it, is currently unknown. I do not say that the ITB Claimants will prevail in demonstrating the necessary knowledge in the fullness of time, but they have a claim which raises interesting issues, and they should be given the opportunity to pursue it sooner rather than later, especially when the existence of the claim will not jeopardize any restructuring.

26 What then of the other considerations enumerated by Jackson JA in the *ICR* case?

27 The merits of the claim against Puratone aside for the moment, the ITB Claim essentially translates into a priority claim between competing creditors. There is no restructuring plan which is being put at risk in this case. This proceeding is almost over. There are a few assets left to be liquidated, but that process will not be put at risk by the existence of the proposed claim by the ITB Claimants. Indeed, the Monitor confirms as such when in its latest report, it observed:

> 20. The Monitor understands that the general purpose of a stay of proceedings under the CCAA is to maintain the *status quo* for a period of time in order that a debtor company (and its directors and officers) can focus on restructuring efforts without undue interference.
>
> 21. Substantially all of the undertaking, property and assets of the Applicants have been sold and it is not anticipated that any formal restructuring will occur. In these circumstances, subject to the proviso which follows with respect to the role of the Monitor should litigation ensue, the Monitor is of the view that there would be no particular prejudice to the CCAA Proceedings if the stay of proceedings is lifted to enable ITB to initiate and proceed with an action against the Applicants and the directors and/or officers of the Applicants.

28 The proviso of the Monitor was simply that it not be required to retain any role in the litigation, if it was allowed to proceed.

29 Accordingly, the balance of convenience favors the ITB Claimants.

30 What then is the prejudice to be suffered if the claim were permitted to proceed at this time? The real prejudice in this case is that if the ITB Claimants are entitled to commence their action now against Puratone and the secured creditors, there could be a delay in the distribution of the holdback monies to the secured creditors. The banks would essentially be deprived of their use of the monies during the litigation and the return on the monies while sitting in the Monitor's trust account would not match what the banks might earn on those monies were they in hand.

31 On the other hand, if I do not permit the claim to be made at this time, the ITB Claimants would be forced to await the end of the CCAA proceeding before commencing their claim. By that time, there would be no money left in Puratone. It all will have been paid to the secured creditors, with at least the tacit acknowledgment by the court that those creditors were entitled to those monies ahead of anyone else. A result such as this is inconsistent with the notion that in a CCAA proceeding, creditors have resort to the supervising court to adjudicate on priority disputes.

32 Any prejudice created by the delay in distribution of funds can easily be alleviated by analogy to the Court Rules respecting prejudgment garnishment. In effect, that is the result which is being sought by the ITB Claimants. Although *Queen's Bench Rule* 46.14 (1) permits garnishment before judgment, Rule 46.14 (3) reads as follows:

  

46.14(3) An order under subrule (1) (Form 46D) may include,

(a) a requirement that the plaintiff post security in a form and amount to be determined by the court; and

(b) such other terms and conditions as may be just.

33 There is no doubt that the secured creditors are *prima facie* entitled to the proceeds of these proceedings. They have valid security agreements which have been properly registered. The ITB Claimants seek to challenge their priority not on the basis that the banks are not secured creditors, but on the basis of factual circumstances that would make it equitable to provide the ITB Claimants with a priority over the secured creditors. There are factual impediments to their claim for unjust enrichment and potentially legal impediments to their claim for equitable subordination and tracing. If I give them the right to make those claims, and those claims are not successful, the delays which those claims might cause to the timely receipt of monies by the secured creditors should not go unaddressed. This can be done by requiring the ITB Claimants to each file an undertaking whereby they would be liable to pay either or both of the banks damages arising from the delay in the payment of the holdback monies attributable to their claim. I am therefore ordering that out of the general holdback monies the amount of $903,250.50 be dedicated to the ITB Claim and not be paid out without further order of court, which presumably will occur either after the claim has been resolved or upon sufficient evidence being demonstrated that it has not been prosecuted in a timely way. Counsel may try and agree on the form of the undertaking as to damages, but may come back to me should agreement not be reached.

34 As regards Puratone, I therefore make the following orders:

a) Out of the general holdback monies, the sum of $903,250.50 and any interest accrued thereon since March 12, 2013 shall be segregated in an interest bearing account designated as the ITB Claim Monies.

b) Leave is given to the ITB Claimants to commence the action against Puratone described at Schedule A of their notice of motion dated April 10, 2013, provided:

(1) they issue it within 40 days after the date of signing of the Order that evidences this decision, and

(2) Prior to the issuance of the Statement of Claim, each named plaintiff will file an undertaking as to damages for its pro rata share of any damages sustained by Bank of Montréal and/or FCC arising from any delay after July 31, 2013 in the distribution of its portion of the ITB Claim monies to Bank of Montréal and/or FCC caused by the issuance of the ITB Claim.

35 If a claimant does not file the requested undertaking as to damages, I will consider that such claimant has abandoned its claim and the ITB Claim Monies may be reduced by the amount of that claimant's claim.

***The Proposed Claim against the directors and/or officers***

36 The claim of the ITB Claimants against the directors and/or officers similarly finds its roots in the allegations of fraud made against Puratone. Counsel for the directors and officers relies upon the case of *People's Department Stores Ltd. (1992) Inc., Re*, 2004 SCC 68, [2004] S.C.J. No. 64 (S.C.C.), drawing from it the principle that deference ought to be given to the decisions that directors make as they fulfill their functions. Notwithstanding that case, there is an argument to be made that where a company has committed a fraud, be it legal or equitable, knowledge on the part of directors of such conduct by officers or employees of the company may make the directors vicariously and/or personally liable.

37 Again, evidence of the actual knowledge of the directors and/or the officers is not readily apparent without the ability to inquire into the records of the company through the discovery process. For the same reasons that I expressed as regards the two banks, requiring the ITB Claimants to adduce evidence on this motion of the directors' and officers' knowledge is too high a threshold to impose. A reasonable inference is that at least some of the directors and officers would have known that a CCAA proceeding was being prepared within the two week period prior to the CCAA filing, and at least some of the directors and officers would have had intimate knowledge of the financial constraints of the company and the efforts which the company was

  

employing to solve them during the two week period prior to the filing of the CCAA proceeding. That reasonable inference in my view is sufficient to conclude that the proposed claim against the directors and/or officers is not necessarily doomed to fail. This case, as with many, will depend on facts not currently available to the court.

38 Additionally, the balance of convenience favors the ITB Claimants, and I see no prejudice to the directors and officers facing the ITB claim sooner rather than later.

39 In my view there are sound reasons to justify lifting the stay to permit the ITB Claimants to issue the proposed claim against the officers and are directors, providing it is issued within 40 days after the date of signing of the Order that evidences this decision. It will however be necessary for the claimants to name the particular individuals who they propose to sue, recognizing that they may expose themselves to costs, possibly on a solicitor and own client basis, for every person that they unsuccessfully sue.

**Going Forward**

40 I have contemplated that the claim should be commenced by one statement of claim, naming at least Puratone and the named officers and directors. The normal Rules of the Court should be followed with the additional requirement that the action will be case managed. A case management conference before me shall be set up within 30 days of the close of pleadings, or earlier upon written request of any party.

41 If necessary, the costs of this motion shall be determined by me upon the resolution of the ITB Claims.

*Motion granted.*

**End of Document**

2014 MBCA 13
Manitoba Court of Appeal

Puratone Corp., Re

2014 CarswellMan 30, 2014 MBCA 13, [2014] M.J. No. 25, 237 A.C.W.S. (3d) 297, 303 Man. R. (2d) 15, 600 W.A.C. 15, 9 C.B.R. (6th) 59

# The Puratone Corporation, Pembina Valley Pigs Ltd. and Niverville Swine Breeders Ltd. (Applicants) Respondents and Farm Credit Canada (Respondent) Applicant

The Puratone Corporation, Pembina Valley Pigs Ltd. and Niverville Swine Breeders Ltd. (Applicants) Respondents and Bank of Montreal (Respondent) Applicant

MacInnes J.A., In Chambers

Heard: November 27, 2013
Judgment: January 27, 2014
Docket: AI 13-30-08010, AI 13-30-08011

Proceedings: allowing leave to appeal *Puratone Corp., Re* (2013), *(*sub nom. *Puratone, Re)* 295 Man. R. (2d) 55, 2013 CarswellMan 360, 2013 MBQB 171 (Man. Q.B.)

Counsel: J.M. Lee, Q.C. for Applicant, Farm Credit Canada
G.B. Taylor, J.J. Burnell for Applicant, Bank of Montreal
R.W. Schwartz, J.S. Harvey for Respondents, ITB Claimants
R.A. McFadyen for Deloitte & Touche Inc.

Subject: Civil Practice and Procedure; Insolvency
**Related Abridgment Classifications**
Bankruptcy and insolvency
XVII Practice and procedure in courts
XVII.7 Appeals
XVII.7.b To Court of Appeal
XVII.7.b.ii Availability
XVII.7.b.ii.C Leave by judge
**Headnote**
Bankruptcy and insolvency --- Practice and procedure in courts — Appeals — To Court of Appeal — Availability — Leave by judge
Companies ran commercial hog production business — Companies experienced financial difficulties and commenced proceedings under Companies' Creditors Arrangement Act (CCAA) — Initial order was made that granted stay of proceedings and appointed monitor — Judge made approval and vesting order that approved sale of substantially all of assets to ML free and clear of all encumbrances, including security interests of companies' creditors — Companies' primary secured lenders were FCC and bank — In two week period preceding granting of initial order, group of farmers supplied feed to companies for their hogs — Order was made that lifted stay of proceedings to allow farmers to sue officers and directors of companies, and $903,250.50 from general holdback was dedicated to farmers' proposed claim — FCC and bank brought motions for leave to appeal order — Motions granted — Decision was discretionary and should be accorded considerable deference but did not need to be given very substantial or special deference normally accorded to decision of CCAA judge, as CCAA proceedings were almost at end — Appeal would not unduly hinder progress of CCAA proceedings — Whether to grant holdback in respect of farmers' claim

 

raised question of law and judge did not expressly address or consider issue — Leave application raised question of importance to practice and was significant to action and parties — Appeal was not frivolous.

**Table of Authorities**

**Cases considered by *MacInnes J.A., In Chambers*:**

*Edgewater Casino Inc., Re* (2009), 446 W.A.C. 274, 265 B.C.A.C. 274, 2009 CarswellBC 213, 51 C.B.R. (5th) 1, *(*sub nom. *Canadian Metropolitan Properties Corp. v. Libin Holdings Ltd.)* 308 D.L.R. (4th) 339, 2009 BCCA 40 (B.C. C.A.) — followed

*Manning v. Chornoboy* (1994), 31 C.P.C. (3d) 131, 96 Man. R. (2d) 274, 1994 CarswellMan 66 (Man. Q.B.) — followed

*Pacific National Lease Holding Corp., Re* (1992), 72 B.C.L.R. (2d) 368, 19 B.C.A.C. 134, 34 W.A.C. 134, 15 C.B.R. (3d) 265, 1992 CarswellBC 524 (B.C. C.A. [In Chambers]) — followed

*Winnipeg Motor Express Inc., Re* (2008), 2008 MBCA 133, 2008 CarswellMan 564, 48 C.B.R. (5th) 202, 448 W.A.C. 3, 236 Man. R. (2d) 3, [2009] 7 W.W.R. 104, 15 P.P.S.A.C. (3d) 1 (Man. C.A. [In Chambers]) — followed

**Statutes considered:**

*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36

Generally — referred to

s. 13 — considered

s. 14(1) — considered

**Rules considered:**

*Queen's Bench Rules*, Man. Reg. 553/88

R. 45.02 — considered

MOTIONS for leave to appeal from judgment reported at *Puratone Corp., Re* (2013), *(*sub nom. *Puratone, Re)* 295 Man. R. (2d) 55, 2013 CarswellMan 360, 2013 MBQB 171 (Man. Q.B.) issuing lift stay and holdback order.

***MacInnes J.A., In Chambers*:**

1 Farm Credit Canada (FCC) and Bank of Montreal (BMO) each move for leave to appeal the order made July 8, 2013, (the lift stay and holdback order) in proceedings under the *Companies' Creditors Arrangement Act* (the *CCAA*).

**Background**

2 The Puratone Corporation, Pembina Valley Pigs Ltd., and Niverville Swine Breeders Ltd., each of whom carried on business as part of the Puratone Group of Companies (Puratone), ran a commercial hog production business, which included the breeding, farrowing, finishing and marketing of hogs.

3 Puratone was experiencing serious financial difficulties, and on September 12, 2012, it commenced proceedings under the *CCAA* to obtain protection from its creditors and to enable it to continue business operations while it attempted a financial restructuring or, failing that, a sale of the business.

4 An order (the initial order) was made that day, which granted a stay of proceedings by creditors against Puratone and its officers and directors. As well, the initial order appointed Deloitte & Touche Inc. monitor of Puratone (the monitor). Further, the judge who granted the initial order became the supervising judge (the judge) for all matters arising thereafter in the *CCAA* proceedings.

5 By order made November 8, 2012 (the approval and vesting order), the judge approved the sale of substantially all of Puratone's assets, including its hogs, to Maple Leaf Foods Inc. The sale closed December 17, 2012.

6 By the approval and vesting order, all of Puratone's rights, title and interest in and to the assets sold vested absolutely in Maple Leaf, free and clear of all encumbrances including security interests of Puratone's creditors. The order also provided

  

that, for the purpose of determining the nature and priority of encumbrances (including security interests) the net proceeds from the sale of the assets would stand in the place of the assets sold.

7 Puratone's primary secured lenders were FCC and BMO. FCC's primary security consisted of Puratone's real property and the operating assets. As at the date of the initial order, FCC was owed approximately 40.3 million dollars. BMO's primary security consisted of the sow and hog inventory, as well as the book debts (or accounts receivable) of Puratone. As at the date of the initial order, BMO was owed approximately 40.9 million dollars.

8 The ITB claimants are a group of 17 farmers represented by Interlake Turkey Breeders Ltd. who, in the approximate two-week period preceding the granting of the initial order, supplied feed to Puratone for its hogs. The value of the feed supplied totalled $903,250.50.

9 By motion dated March 7, 2013, the monitor sought an order (the interim distribution order) authorizing the interim distribution of the sale proceeds to each of FCC, BMO and Manitoba Agricultural Services Corporation (MASC), another secured creditor, subject to a general holdback of five million dollars pending completion of the *CCAA* proceedings. The monitor's motion was accompanied by a report that stated that FCC, BMO and MASC each had valid and enforceable security interests in the assets of Puratone, and that such security interests ranked in priority to all other claims that could be made to Puratone's assets. That report also indicated that each of FCC, BMO and MASC would incur significant shortfalls on their outstanding indebtedness.

10 By motion dated March 11, 2013, the ITB claimants sought an order lifting the stay of proceedings to allow the ITB claimants to sue the officers and directors of Puratone, and directing that $903,250.50 of the sale proceeds be imposed with a constructive trust in favour of the ITB claimants, or otherwise be withheld from distribution.

11 Both motions were dealt with on March 12, 2013. The judge granted the interim distribution order sought by the monitor and declined to hold back any additional sale proceeds (other than the general holdback). The judge adjourned the ITB claimants' motion for hearing to April 11, 2013.

12 The ITB claimants filed a second motion on April 10, 2013. An appendix was attached to the second motion outlining, very generally, the proposed action which would be commenced by the ITB claimants against the officers and directors of Puratone, and as well, possibly against FCC and BMO.

13 Both the second motion and the adjourned motion were heard on April 11, 2013. The judge reserved decision and on July 8, 2013, ordered (the lift stay and holdback order) that the stay of proceedings be lifted, thus permitting the ITB claimants to sue the officers and directors of Puratone, and that $903,250.50 from the general holdback be dedicated to the proposed claim of the ITB claimants and not be paid out without further order of the court.

14 It is from that decision that the motion for leave to appeal has been brought pursuant to ss. 13 and 14(1) of the *CCAA*, which provide:

> **Leave to appeal**
>
> **13.** Except in Yukon, any person dissatisfied with an order or a decision made under this Act may appeal from the order or decision on obtaining leave of the judge appealed from or of the court or a judge of the court to which the appeal lies and on such terms as to security and in other respects as the judge or court directs.
>
> **Court of appeal**
>
> **14.** (1) An appeal under section 13 lies to the highest court of final resort in or for the province in which the proceeding originated.

**The Test for Granting Leave to Appeal**

  

15 In *Winnipeg Motor Express Inc., Re*, 2008 MBCA 133, 236 Man. R. (2d) 3 (Man. C.A. [In Chambers]), Monnin J.A. wrote (at paras. 13-14):

> Prior to dealing with the merits of the leave application itself, it is useful to briefly review the underlying principles of the **CCAA**. Such guidance can be found in the Alberta Court of Appeal decision of **Smoky River Coal Ltd. et al., Re** (1999), 237 A.R. 326, 197 W.A.C. 326, 175 D.L.R. (4th) 703; 1999 ABCA 179 (C.A.). Writing for the court, Hunt, J.A., said (at paras. 51-53):
>
> > "This interpretation is supported by the legislative objectives underlying the **CCAA**. The purpose of the **CCAA** and the proper approach to its interpretation have been described as follows:
> >
> > > The **CCAA** is intended to facilitate compromises and arrangements between companies and their creditors as an alternative to bankruptcy and, as such, is remedial legislation entitled to a liberal interpretation. It seems to me that the purpose of the statute is to enable insolvent companies to carry on business in the ordinary course or otherwise deal with their assets so as to enable plan of compromise or arrangement to be prepared, filed and considered by their creditors and the court. In the interim, a judge has great discretion under the **CCAA** to make order [sic] so as to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors. [Per Farley, J., in **Lehndorff General Partner Ltd. (Re)** (1993), 17 C.B.R. (3d) 24 (Ont. Ct. (Gen. Div.)) at 31.]
> >
> > "As has been noted often, the **CCAA** was enacted by Parliament in 1933 during the height of the Depression. At that time, corporate insolvency led almost inevitably to liquidation because that was the only option available under legislation such as the **Bankruptcy Act**, R.S.C. 1927, c. 11, and the **Winding-Up Act**, R.S.C. 1927, c. 213. In the result, shareholder equity was destroyed, creditors received very little, and the social evil of unemployment was exacerbated. The **CCAA** was intended to provide a means of enabling the insolvent company to remain in business: **Hongkong Bank of Canada v. Chef Ready Foods Ltd.** (1990), 4 C.B.R. (3d) 311 (B.C.C.A.); **Quintette Coal**, [ (1991), 7 C.B.R. (3d) 165 (B.C.S.C.)].
> >
> > "The courts have underscored that the **CCAA** requires account to be taken of a number of diverse societal interests. Obviously, the **CCAA** is designed to 'provide a structured environment for the negotiation of compromises between a debtor company and its creditors for the benefit of both': **Lehndorff General Partner Ltd., Re**, supra, at 31. It is intended to 'prevent any manoeuvers for positioning among creditors during the interim period which would give the aggressive creditor an advantage to the prejudice of others who were less aggressive and would further undermine the financial position of the company making it less likely that the eventual arrangement would succeed': **Meridian**, [ (1984), 52 C.B.R. (N.S.) 109 (Alta. Q.B.)], at 114. But the **CCAA** also serves the interests of a broad constituency of investors, creditors and employees: **Chef Ready**, supra, at 320; **Quintette Coal**, supra, at 314. These statements about the goals and operation of the **CCAA** support the view that the discretion under s. 11(4) should be interpreted widely."
>
> Within the general context just described, the test to be applied on a leave application under the **CCAA** is a narrow one and, as will be demonstrated, it is to be applied selectively and sparingly. Wittmann, J.A., of the Alberta Court of Appeal sets out the test in **Canadian Airlines Corp., Re** (2000), 261 A.R. 120, 225 W.A.C. 120, 80 Alta. L.R. (3d) 213; 2000 ABCA 149, in these words (at paras. 6-7):
>
> > "The criterion to be applied in an application for leave to appeal pursuant to the **CCAA** is not in dispute. The general criterion is embodied in the concept that there must be serious and arguable grounds that are of real and significant interest to the parties: **Multitech Warehouse Direct Inc., Re** (1995), 32 Alta. L.R. (3d) 62 (Alta. C.A.), at 63; **Smoky River Coal Ltd., Re** (1999), 237 A.R. 83 (Alta. C.A.); **Blue Range Resource Corp., Re** (1999), 244 A.R. 103 (Alta. C.A.); **Blue Range Resource Corp., Re** (2000), 15 C.B.R. (4th) 160 (Alta. C.A. [In Chambers]); **Blue Range Resource Corp., Re** (2000), 15 C.B.R. (4th) 192 (Alta. C.A. [In Chambers]).

  

> "Subsumed in the general criterion are four applicable elements which originated in **Power Consolidated (China) Pulp Inc. v. British Columbia Resources Investment Corp.** (1988), 19 C.P.C. (3d) 396 (B.C.C.A.), and were adopted in **Med Finance Co. S.A. v. Bank of Montreal** (1993), 22 C.B.R. (3d) 279 (B.C.C.A.). McLachlin, J.A., (as she then was), set forth the elements in **Power Consolidated** as follows at p. 397:
>
> (1) whether the point on appeal is of significance to the practice;
>
> (2) whether the point raised is of significance to the action itself;
>
> (3) whether the appeal is prima facie meritorious or, on the other hand, whether it is frivolous; and
>
> (4) whether the appeal will unduly hinder the progress of the action.
>
> . . .

16 Clearly, and as a general rule, leave to appeal a decision given by a judge under the *CCAA* is to be granted sparingly. But that is not to say that leave cannot be granted. The application of the general rule will depend upon the circumstances of a given case, and particularly, the state of the *CCAA* proceedings.

17 In *Edgewater Casino Inc., Re*, 2009 BCCA 40, 265 B.C.A.C. 274 (B.C. C.A.), Tysoe J.A. considered the general rule in light of comments made by MacFarlane J.A. in *Pacific National Lease Holding Corp., Re* (1992), 19 B.C.A.C. 134 (B.C. C.A. [In Chambers]) at paras. 30-32, and the four factors to be considered on a leave application under the *CCAA*. He wrote (at paras. 18-22):

> This is not to suggest that I disagree with the above comments of Macfarlane, J.A., in **Pacific National Lease**. To the contrary, I agree with his comments, but I do not believe that he established a special test for **CCAA** orders. Rather, his comments are a product of the application of the usual standard used on leave applications to orders that are typically made in **CCAA** proceedings and a recognition of the special position of the supervising judge in **CCAA** proceedings. In particular, a consideration of the third and fourth of the above factors will result in leave to appeal from typical **CCAA** orders being given sparingly.
>
> The third of the above factors involves a consideration of the merits of the appeal. In non-**CCAA** proceedings, a justice will be reluctant to grant leave where the order constitutes an exercise of discretion by the judge because the grounds for interfering with an exercise of discretion are limited: see **Silver Standard Resources Inc. v. Joint Stock Co. Geolog et al.**, [1998] B.C.A.C. Uned. 140; [1998] B.C.J. No. 2298 [QL] (C.A. Chambers). Most orders made in **CCAA** proceedings are discretionary in nature, and the normal reluctance to grant leave to appeal is heightened for two reasons alluded to in the comments of Macfarlane, J.A.
>
> First, one of the principal functions of the judge supervising the **CCAA** proceeding is to attempt to balance the interests of the various stakeholders during the reorganization process, and it will often be inappropriate to consider an exercise of discretion by the supervising judge in isolation of other exercises of discretion by the judge in endeavouring to balance the various interests. Secondly, **CCAA** proceedings are dynamic in nature and the supervising judge has intimate knowledge of the reorganization process. The nature of the proceedings often requires the supervising judge to make quick decisions in complicated circumstances. These considerations are reflected in the comment made by Madam Justice Newbury in **New Skeena Forest Products** [ (2005), 210 B.C.A.C. 247] that "[a]ppellate courts also accord a high degree of deference to decisions made by Chambers judges in **CCAA** matters and will not exercise their own discretion in place of that already exercised by the court below" (para. 20).
>
> The fourth of the above factors relates to the detrimental effect of an appeal on the underlying action. In most non-**CCAA** cases, the events giving rise to the underlying action have already occurred, and a consideration of this factor involves the prejudice to one of the parties if the trial is adjourned or if the action cannot otherwise move forward pending the

  

> determination of the appeal. **CCAA** proceedings are entirely different because events are unfolding as the proceeding moves forward and the situation is constantly changing - some refer to **CCAA** proceedings as "real-time" litigation.
>
> The fundamental purpose of **CCAA** proceedings is to enable a qualifying company in financial difficulty to attempt to reorganize its affairs by proposing a plan of arrangement to its creditors. The delay caused by an appeal may jeopardize these efforts. The delay may also have the effect of upsetting the balance between competing stakeholders that the supervisory judge has endeavoured to achieve.

18 Tysoe J.A. continued (at para. 24):

> As a result of these considerations, the application of the normal standard for granting leave will almost always lead to a denial of leave to appeal from a discretionary order made in an ongoing **CCAA** proceeding. However, not all of the above considerations will be applicable to some orders made in **CCAA** proceedings. Thus, in **Westar Mining** [ (1993), 22 B.C.A.C. 106], McEachern, C.J.B.C., while generally agreeing with the comments made in **Pacific National Lease**, believed that the considerations mentioned by Macfarlane, J.A., were not applicable in that case because the **CCAA** proceeding had effectively come to an end with the sale of the principal assets of the debtor company. Madam Justice Newbury made a similar point in **New Skeena Forest Products** at para. 25 (which was a hearing of an appeal, not a leave application), although she found it unnecessary to decide the appeal on the point.

19 In the circumstances here, it is my view that the judge's decision, being a discretionary decision, should be accorded considerable deference, but it is also my view that it need not be given the very substantial or special deference normally accorded a decision of a *CCAA* judge, as the *CCAA* proceedings are virtually at an end and it is conceded by all parties that an appeal, if granted, will not unduly hinder the progress of the *CCAA* proceedings.

20 In their respective motions for leave to appeal, FCC and BMO advanced various grounds, including as regards that portion of the lift stay and holdback order lifting the stay so as to permit the ITB claimants to sue the officers and directors of Puratone. Both advised, however, that they were not seeking leave to appeal that portion of the lift stay and holdback order and, accordingly, I do not propose to deal with it.

21 Rather, I will address only the actual issue which both FCC and BMO propose to appeal, if leave is granted; namely, that portion of the lift stay and holdback order which required that, out of the general holdback monies, the sum of $903,250.50 be dedicated to the proposed claim of the ITB claimants and segregated in an interest-bearing account, not to be paid out without further order of the court.

**Argument**

22 FCC asserts that the judge proceeded on the erroneous assumption that, were he to grant an order lifting the stay, an order to hold back the funds would automatically follow. It argues that whether to lift a stay of proceedings to permit litigation to proceed, and whether to withhold from distribution the amount claimed in that litigation, are two separate and distinct issues.

23 FCC submits that the judge erred by awarding the ITB claimants a prejudgment remedy as part of the lift stay and holdback order, without any consideration of whether such a remedy was appropriate.

24 It says that the effect of dedicating $903,250.50 from the general holdback to the proposed claim of the ITB claimants is to improperly reorder priorities in the *CCAA* proceedings. This, it argues, is a point of significance to *CCAA* practice, as such an order is unprecedented in the *CCAA* jurisprudence and will create a heightened level of uncertainty for secured creditors who may, thus, be less inclined to support a company seeking either to reorganize or to sell its assets as a result of financial difficulties. It says that without support from their secured creditors, debtor companies will be unable to restructure under the *CCAA*.

25 FCC also asserts that the proposed appeal with respect to the order for holdback of the funds is a point of significance to the action itself. It argues that the practical effect of the holdback portion of the lift stay and holdback order is to elevate the unproven unsecured claim of the ITB claimants ahead of the proven secured claim of FCC and BMO. It says that the judge

  

found that FCC and BMO were *prima facie* entitled to all of the sale proceeds. However, having done so, he then effectively denied each of them access to nearly one million dollars by effectively elevating the unsecured claim of the ITB claimants to a status ahead of, or at least equal to, the proven secured claims of FCC and BMO.

26 FCC submits that, if leave to appeal were granted, the appeal to follow is *prima facie* meritorious by reason of the fact that the judge made the holdback portion of the lift stay and holdback order without giving any consideration to whether there was a legal basis for so doing, which it asserts there was not, on the evidence before the judge. Lastly, it says that the proposed appeal will not unduly hinder the progress of the *CCAA* proceedings, which are at an end. Thus, there are no ongoing restructuring efforts that would be put at risk.

27 BMO also argues that the point on the proposed appeal is of great significance to the *CCAA*. It says that there is no necessary connection between the two orders, that is, the lifting of the stay of proceedings and the holding back of proceeds. It asserts that the two matters require consideration of quite separate issues and factors, and the conduct of distinct parties; namely, Puratone and its officers and directors on the one hand, and BMO and FCC on the other.

28 BMO submits that the lifting of the stay of proceedings did not involve it or FCC, as there was never a stay of proceedings against either of them. The ITB claimants could have sued them at any time. But, it says the matter of the holdback required independent consideration by the judge of the factors relevant to the exercise of his discretion as regards the holdback of funds from BMO and FCC.

29 BMO asserts that the judge's reasons for judgment demonstrate no separate consideration of the proper circumstances under which the proven and accepted interest of a secured creditor ought to be interfered with in the context of a motion for such relief by an unsecured or subordinate creditor; no reference to a test of any kind to be applied to a motion for such relief from a subordinate or unsecured creditor to justify interference with the established rights of a secured creditor in receiving the proceeds of its security; and no consideration of any of the elements of such a test.

30 BMO argues that the judge's decision is important to the *CCAA* practice for its precedential value. It says that, on the basis of the decision, it appears open for any subordinate or unsecured creditor that has supplied goods or services in some period reasonably proximate to the *CCAA* filing, to obtain an order that funds, to which a secured creditor has proven its prior ranking and entitlement, be held back and not distributed to the secured creditor pending action over an indeterminate period.

31 BMO asserts that without the application of a qualifying test of some substance, there is the meaningful risk that the supervisory function of the *CCAA* court could be overwhelmed by creditors trying to position themselves for settlement.

32 BMO argues that the point of the intended appeal is significant to this *CCAA* proceeding as the holdback of funds delays distribution to BMO and FCC, whose *prima facie* entitlements were accepted by the judge, and delays, for an indeterminate period, the completion and winding up of the *CCAA* process, all in circumstances where both BMO and FCC are capable of funding judgments against them should the ITB claimants succeed in an action against them.

33 BMO submits that an order to hold back funds from a party *prima facie* entitled to such funds, is not one which ought to be made lightly. It refers to Queen's Bench Rule 45.02, which 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.

34 BMO refers to *Manning v. Chornoboy* (1994), 96 Man. R. (2d) 274 (Man. Q.B.) at para. 8, where the court considered the four criteria in arriving at its decision on a motion for the preservation of funds under Rule 45.02, namely:

> a) whether there is a serious issue with regard to the entitlement of the funds;
>
> b) whether it is reasonably possible that the funds would otherwise be put beyond the reach of this court should the plaintiff succeed;

  

c) the hardship that may be suffered by the parties; and

d) the balance of convenience.

35 BMO argues that while *Manning* was not decided in the context of a *CCAA* application, the criteria ought to be the same. Parties *prima facie* entitled to their property ought not to be deprived of that property unless (1) there is a serious issue as to entitlement; (2) there is some reasonable risk that the property will be dissipated or otherwise inaccessible should the moving party be successful at trial; and (3) there should be a consideration of the hardship to each party. It submits that the judge ought to have demonstrably considered and applied a test at least as stringent as the aforementioned in the exercise of discretion to hold back funds from BMO and FCC and that, had he done so, the ITB claimants would have wholly failed, on the record, to meet this test.

36 BMO argues that the fundamental basis upon which the money was held back was the judge's determination that when he scrutinized the proposed claim of the ITB claimants against Puratone, he concluded that its dismissal was not a foregone conclusion. However, argues BMO, in the circumstances here, that is not enough. While the ITB claimant's might be entitled to establish a constructive trust *vis-à-vis* Puratone, which BMO denies, in order to have an entitlement to the monies held back, the ITB claimants must also displace the priority interests of BMO and FCC.

37 To that end, BMO argues that, in order to succeed in a claim for unjust enrichment, the ITB claimants will need to establish:

a) an enrichment;

b) a corresponding deprivation; and

c) an absence of any juristic reason for the enrichment.

38 It notes, in particular, that with respect to criterion c), a two-stage test is to be employed. First, the ITB claimants must establish that no juristic reason for the enrichment, from an "established category" existed to deny recovery, but even if they were able to meet that hurdle, it creates only a presumption of unjust enrichment which, at the second stage of the test, is rebuttable.

39 BMO asserts that it and FCC, on the record before the judge, would be able to rebut the presumption in stage two of the analysis, as both BMO and FCC are arm's-length parties with first ranking prior, registered security interests. BMO says that the juristic reason referred to in criterion c) for the establishment of an unjust enrichment is not limited to the person enriched and the person deprived, that is Puratone and the ITB claimants. Rather, the juristic reason may arise out of a relationship between the person enriched and some other person, and need not be tied to the person who asserts the unjust enrichment. That is, in this case, the juristic reason may be found in the pre-existing legal rights held by BMO and FCC to the ITB claim money. This, argues BMO, was a point never averted to or considered by the judge in making the holdback portion of the lift stay and holdback order and in failing to do so, it submits that he erred.

40 The ITB claimants agree that the test articulated in *Winnipeg Motor Express Inc., Re* (at para. 14) is the relevant test to be applied when considering whether to grant leave to appeal a decision of a supervising judge in a *CCAA* proceeding. It argues that the test is a narrow one to be applied selectively and sparingly, and that great deference is to be provided to the *CCAA* supervising judge.

41 The thrust of their argument pertains to the judge's decision that the dismissal of the proposed claim of the ITB claimants against Puratone was not a foregone conclusion. But the ITB claimants agree that the holdback portion of the lift stay and holdback order is a distinct issue from the decision to lift the stay, and concede that the judge did not embark upon any separate analysis of whether or when it would be appropriate to hold back any such proceeds from distribution. They assert that, in the circumstances of this case, and once the stay was lifted, it naturally followed that the value of ITB claimants' claim would continue to be held back, while the rest of the general holdback money would be distributed accordingly.

42 They also acknowledge that an appeal of the judge's decision would not hinder the *CCAA* application.

  

**Analysis and Decision**

43 I am prepared to grant leave to FCC and BMO. I must, therefore, be circumspect in the comments which I make, as the case will now proceed to appeal before a panel of this court.

44 As I stated previously, this is a discretionary decision of the judge and the starting point for review is, and on appeal will be, one of considerable discretion.

45 Nonetheless, it is agreed by all parties that the issue of holdback is a discrete issue from that of the lifting of the stay. In my view, the issue whether to grant a holdback in respect of the ITB claimants' claim raises a question of law. And, it is agreed that the judge did not expressly address that issue. Nor does it appear that he considered the issue.

46 For purposes of this leave application, I am satisfied that FCC and BMO have met the criteria for leave as enunciated by Monnin J.A. in *Winnipeg Motor Express Inc., Re* (and by other judges in other cases arising under the *CCAA*).

47 I am of the view that the leave application raises a question of importance to the practice, and of significance to the action and the parties. As well, I am satisfied that the appeal is not frivolous, and I note that all parties agree, given the state of the instant proceedings, that an appeal will not hinder their progress.

48 Thus, I am prepared to grant leave on the following question:

> Did the judge err in ordering that the sum of $903,250.50, being the ITB claimants' claim, be segregated within the general holdback money and withheld from distribution to FCC and BMO?

49 FCC and BMO will have their costs of this motion.

*Motions granted.*

C. A.
1879
FRY, J.
*July* 10, 12.
C. A.
*Nov.* 26;
*Dec.* 3.
1880
*Feb.* 11.

## *In re* HALLETT'S ESTATE.
## KNATCHBULL *v.* HALLETT.

[1878 H. 147.]

*Banker—Lien—Following Trust Money—Entry by Banker—Order of Payment—Appropriation—Rule in Clayton's Case—Trustee.*

If money held by a person in a fiduciary character, though not as trustee, has been paid by him to his account at his bankers, the person for whom he held the money can follow it, and has a charge on the balance in the bankers' hands.

*Ex parte Dale & Co.* (1) dissented from.

If a person who holds money as a trustee or in a fiduciary character pays it to his account at his bankers, and mixes it with his own money, and afterwards draws out sums by cheques in the ordinary manner:—

*Held*, by the Court of Appeal (*dissentiente Thesiger*, L.J.), that the rule in *Clayton's Case* (2), attributing the first drawings out to the first payments in, does not apply; and that the drawer must be taken to have drawn out his own money in preference to the trust money.

*Pennell* v. *Deffell* (3) on this point not followed.

*Held*, by *Fry*, J., that, as between two *cestuis que trust* whose money the trustee has paid into his own account at his bankers, the rule in *Clayton's Case* applies, so that the first sum paid in will be held to have been first drawn out.

THIS case came on upon claims by several persons against money in the hands of the bankers of *Henry Hughes Hallett*, deceased. The action was brought by a general creditor for the administration of his estate.

As to a claim by the trustees of *Hallett's* settlement. By the marriage settlement of *Henry Hughes Hallett*, made in 1847, a sum of £2300 was settled for the benefit of *Hallett*, his wife and his children. Several changes were made in the investment of this fund, and the trustees had allowed the fund to come into the hands of *Hallett*. These changes were effected by *Hallett*, and were noted in a memorandum in his handwriting in the fold of the draft settlement, which terminated as follows: "The money remained in the *Great George Street* mortgage until September,

(1) 11 Ch. D. 772. (2) 1 Mer. 572.
(3) 4 D. M. & G. 372.

1865, when it was invested in Mr. *Walker's* estate. *Walker's* mortgage was paid off in November, 1870, and invested in £2590 Russian 5 per Cent. Stock." This was not strictly correct, as *Walker's* mortgage was really paid off in 1869.

*Hallett* held a considerable number of Russian bonds, and in the opinion of the Court it was proved that he had in 1877 allotted Russian bonds of the nominal amount of £1554 and £1036, making together £2590, as representing the trust funds under the settlement. The bonds for £1554 he retained in his own hands; and his son, shortly before his death, found them and delivered them to the trustees of the settlement by whom they were sold. The bonds for £1036 were deposited by *Hallett* with his bankers, Messrs. *Twining*, and were afterwards sold as mentioned below.

As to a claim by Mrs. *Cotterill*. *Henry Hughes Hallett* had for many years been employed by Mrs. *Cotterill* as her solicitor, and she had been in the habit of depositing with him securities for money, and in the opinion of the Court it was proved that he had bought or appropriated and did in 1877 hold for her Russian bonds of £450 and £2242, nominal amount. The facts of her case are fully stated in the judgment of Mr. Justice *Fry*.

In November, 1877, *Hallett*, without any authority from the trustees or from Mrs. *Cotterill*, directed his bankers, Messrs. *Twining*, to sell, and they accordingly sold, one of the sets of bonds representing the trust fund and both sets of Mrs. *Cotterill's* bonds. The following entries (with other entries of cash, &c.) appeared to his credit in the books of the bankers:—

| | | £ | s. | d. |
|---|---|---|---|---|
| Nov. 3. | Sale £450 Russian 5 per cent. 1871, at 76 less commission . . . . | 341 | 8 | 9 |
| Nov. 14. | Sale £1036 Russian 5 per cent. 1822, at 74½ less commission . . . | 770 | 10 | 5 |
| „ | Sale £2442 Russian 5 per cent. 1822, at 74 less commission . . . . | 1804 | 0 | 7 |

*Hallett* had before his death drawn out different sums for his own purposes, so that the balance to his credit at the time of his death (if nothing more had been paid in by him after the 14th of November) would have been £1708 16*s*. He had, however, paid

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in other sums, so that he had at the time of his death, which was in February, 1878, a balance at his bankers of £3029 15*s.* 1*d.*, of which £2600 had been paid into Court to the credit of an action for the administration of his estate.

The trustees of the settlement applied by summons in the action for payment of £770 10*s.* 5*d.* out of the £2600, and for a declaration that the produce of the sale of the bonds for £1554 belonged to them. Mrs. *Cotterill* applied for payment of the £1708 16*s.* balance. A Mrs. *Gatliff* also applied for payment of some of the money as having arisen from the sale of Russian bonds belonging to her. The summonses came on for hearing together before Mr. Justice *Fry* on the 10th of July, 1879.

*E. Beaumont*, for Mrs. *Cotterill*:—

Mrs. *Cotterill* claims £1708 16*s.* as the sum remaining in the bankers' hands out of the produce of the sales of her £2442 Russian bonds. These bonds were simply deposited with *Hallett*, and he had no right to sell them. He has, however, sold them, but the money can be traced and is ear-marked. He is said to have similarly sold the bonds of his trustees, but if he did so the £770 10*s.* 5*d.* for which he sold them has, like the produce of the sale of Mrs. *Cotterill's* £450, been already drawn out under his cheques, and the balance left is not enough even to satisfy Mrs. *Cotterill's* claim for the produce of her £2442 Russian bonds. That is the rule in *Clayton's Case* (1); *Brown* v. *Adams* (2).

*Phear*, for Mrs. *Gatliff*.

*J. Pearson*, Q.C., and *D. Gardiner*, for the trustees of the settlement:—

We claim the £770 10*s.* 5*d.* as the produce of the sale of our Russian bonds, and we also claim the produce of the bonds for £1554. As to the £770 10*s.* 5*d.*, *Clayton's Case* does not apply, as both sums were paid in on the 14th of November; and at all events the remaining money must be rateably apportioned between the trustees and Mrs. *Cotterill*.

(1) 1 Mer. 572. (2) Law Rep. 4 Ch. 764.

*Higgins*, Q.C., and *B. Fossett Lock*, for the Plaintiff in the suit:—

The applicants have no priority; and this case is exactly like *Ex parte Dale & Co.* (1), which shews that when money has been paid to a general account at a bankers it cannot be followed. *Ex parte Cooke* (2) was different, as the person paying in was a broker. The law is shewn by *Pennell* v. *Deffell* (3) and *Middleton* v. *Pollock* (4).

*A. T. Watson*, for *Hallett's* executrix, cited *Taylor* v. *Plumer* (5).

FRY, J., after expressing his intention of giving counsel an opportunity of arguing Mrs. *Cotterill's* summons on the cases which had been cited, and after stating the facts as to the claim of *Hallett's* trustees, and deciding that they were entitled to retain the proceeds of the sale of the £1554 Russian bonds, and that they had proved that the Russian bonds for £1036 were part of the trust fund, continued:—

The second question is whether *Clayton's Case* (6) applies. Now, if the matter were unfettered by authority, it would appear to me clear that where a man has a balance to his credit consisting in part of funds which are his own, and which he may lawfully draw out and apply for his own purposes, and in part of funds which he may not lawfully draw out and apply for his own purposes, his drawings for his own purposes ought to be attributed to his own funds, and not to the trust funds. But it appears to me that I am not at liberty, in the existing state of the authorities, to act according to the inclination of my own mind. In *Pennell* v. *Deffell* (7), Lord Justice *Knight Bruce* said, "It may be, however, and, as I think, is true, that cheques drawn by the trustee in a general manner upon the bank would, for every purpose, be ascribed and affect the account in the mode explained and laid down by Sir *W. Grant* in *Clayton's Case*. The principles there stated would, I conceive, be applicable, notwithstanding the different nature and character of the sums

(1) 11 Ch. D. 772.
(2) 4 Ch. D. 123.
(3) 4 D. M. & G. 372.
(4) 4 Ch. D. 49.
(5) 3 M. & S. 562.
(6) 1 Mer. 572.
(7) 4 D. M. & G. 372, 384.

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forming together the balance due from the bank to the trustee, whatever the purposes and objects of the cheques." On that view the Court of Appeal acted, and held that as between the persons who intrusted the testator with trust moneys and his general creditors the claims of the former must prevail. In *Frith* v. *Cartland* (1) Vice-Chancellor *Wood* said, "The Court attributes the ownership of the trust property to the *cestui que trust* so long as it can be traced. Here there is no difficulty in identifying it. Throughout the whole series of transformations the bankrupt always held a fund available to meet the claim of the trust. . . . So long, however, as the fund can be traced, the trustee cannot assert his own title to it." That case was followed by *Brown* v. *Adams* (2), where the trust money paid in had been drawn out, and it was held that it had been appropriated to answer the cheques. The rights of the different parties must be governed by *Clayton's Case* (3).

His Lordship then gave his decision that Mrs. *Gatliff's* claim was not maintained by the evidence.

July 12. *E. Beaumont*, continuing the argument for Mrs. *Cotterill*:—

This case is distinguishable from *Ex parte Dale & Co.* (4), especially as *Hallett* was a trustee for Mrs. *Cotterill*. But even if *Hallett* was only an agent the money can be followed: *Taylor* v. *Plumer* (5). If the money can only be followed in the hands of a trustee, *Brown* v. *Adams* would not have been arguable. In many cases there is a physical difficulty in tracing the money, but when that has been got over the law is clear: *Ex parte Cooke* (6). Why should the trustees of the settlement take the balance? *Hallett* was not a banker, and the moneys were not mixed up in his hands, and each sum can be and has been traced. Even if *Hallett* was not technically trustee for Mrs. *Cotterill* he stood in a fiduciary relation to her, and the result would be the same.

*Higgins*, in reply, on the cases cited.

(1) 2 H. & M. 417, 422.
(2) Law Rep. 4 Ch. 764.
(3) 1 Mer. 572.
(4) 11 Ch. D. 772.
(5) 3 M. & S. 562.
(6) 4 Ch. D. 123.

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FRY, J.:—

In this case Mrs. *Cotterill* claims to have such portion of the residue of the balance standing to the credit of the late Mr. *Hallett's* banking account as may be attributable to her after applying the rule in *Clayton's Case* (1) to that account.

For more than twenty years before the death of Mr. *Hallett* in 1878 he had acted as the solicitor for this lady, and in the year 1860 he had purchased for her Russian bonds to the nominal value of £1251, and on the 10th of February, 1868, Mrs. *Cotterill* deposited those bonds with Mr. *Hallett*, together with £1000 stock of the *Midland Waggon Company* of *Birmingham*, and thereupon he gave her a receipt for those bonds. It appears from the evidence before me that Mr. *Hallett* was in the habit of receiving the dividends on these and the other bonds which afterwards came to his hands for safe custody, and paying them to Mrs. *Cotterill*. In March, 1871, the *Midland Waggon Company's* bond was paid off; and it appears that the sum of £1010 9*s*. 4*d*. reached *Hallett's* hands, and on the 23rd of March that was invested in £1184 Russian bonds. I hesitate to say "in the purchase," because it appears that Mr. *Hallett* had at that time in his hands Russian bonds to a considerable amount, and he probably appropriated to her, bonds to the value of £1184, which he acknowledged himself to hold on that day for her safe custody, for on that day he gave her a receipt in these terms, "Received of Mrs. *Amelia Cotterill* for safe custody £1258 Russian bonds of 1862, also £1184 like bonds, the investment of the *Midland Waggon Company's* bond paid off." The result was that he held for her £2442 Russian bonds. It has been said that these Russian bonds were not appropriated; but it appears to me that I am bound to hold that they were appropriated. He gave her that receipt, and there are entries in his books which also support the appropriation by him of certain specific bonds on her behalf. He appears, further, to have received the dividends on the bonds to that extent, and to have paid them to her. In 1871 she further deposited with him some other bonds, including £450 Russian bonds.

So matters went on from 1871 down to 1877. On the 3rd of November, 1877, Mr. *Hallett* sold the £450 Russian bonds through

(1) 1 Mer. 572.

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the intervention of his bankers, Messrs. *Twining*, and the amount produced by that sale was entered in his bankers' book specifically as the produce of the sale of £450 Russian 5 per Cent. Bonds. Then, on the 14th of November, he sold the £2242 bonds which he held for Mrs. *Cotterill*, and he sold on the same day another bond belonging to the trustees of his settlement. The entry in his bankers' book keeps separate those two amounts; and with regard to the amount now claimed by Mrs. *Cotterill*, it is entered as the produce of £2242 5 per Cent. Russian Bonds. The money, therefore, is as clearly ear-marked in the bankers' account as it is possible to be by means of an entry.

Further than that, it is to be borne in mind that *Hallett* charges himself on the 14th of November with a sum of £2994 9*s.* 4*d.* as the produce of Russian bonds, £2442 and £450. And that sum was the exact result of adding together the two sums I have mentioned as passing into his bankers' account. There is, therefore, no doubt that that sum was the produce of Mrs. *Cotterill's* bonds. It is not necessary to say much more than that on the 2nd of February, 1878, Mr. *Hallett* died, leaving a balance of about £3000 at his bankers.

In that state of circumstances the question arises whether Mrs. *Cotterill* is entitled to follow this money. It has been argued that Mr. *Hallett* was a trustee for Mrs. *Cotterill*. In that view I cannot concur; but it appears to me that he was solicitor for her, that he was agent for her, and that he was bailee for her. I think, therefore, that he stood in what has been called a fiduciary relation towards her. Now if he had been merely the agent and bailee, and had received from her an authority to sell these bonds —an authority which, according to the proper interpretation to be put on it by the course of dealing between them, implied a right in him to mix the produce of the sale with his own moneys, I should very probably have held that Mrs. *Cotterill* was merely a creditor of Mr. *Hallett*. But that is not the case here. The authority which she gave him was merely to hold these bonds for her; and the sale of these bonds was, in my judgment, a distinct violation of the duty he had undertaken. Therefore there was no authority from her which would justify him in mixing the produce of the bonds with his own moneys. There was nothing from which

you could infer that she was minded that the property should be converted, or that she would look to him as the mere paymaster of the produce of the securities. Those circumstances, in my judgment, make the case entirely different from the series of authorities to which I referred in *Ex parte Dale & Co.* (1), where I came to the conclusion, rightly or wrongly, that the factor properly converted the goods into money, and that the money got mixed with his own money in accordance with the intention of the parties, and that in such a case the money could not be followed. That appears to me to be the law, both at Common Law and in Equity; some of the decisions to which I then referred being decisions of a Court of Equity. But for the reasons I have indicated, that line of authority does not appear to me to touch this matter, and therefore I think that in this case—finding the fiduciary relationship, and finding the violation of that duty in the manner I have described—I am bound to give Mrs. *Cotterill* the same relief as if Mr. *Hallett* had been a trustee for her. That being so, the result is that she is entitled to follow the balance standing to his credit in his bankers' account, in the manner indicated when I gave judgment on the summons of the trustees.

I will only make this further observation, that it may very well be that the distinction which I have now drawn, and to which necessarily my attention was not so fully directed when I gave judgment in *Ex parte Dale & Co.*, may remove some of the force of the observations which I made at the end of that judgment as to the difficulty of reconciling the other authorities with the case of *Pennell* v. *Deffell* (2).

*J. Pearson*, Q.C., and *Dundas Gardiner* then claimed that the balance in the bank should be divided rateably between *Hallett's* trustees and Mrs. *Cotterill*. A banker pays the cheques drawn on him out of the general balance, and does not appropriate the money first paid to the first cheque drawn. The rights of claimants cannot depend on the accident of which entry is made first by the banker's clerk. At all events a day cannot be divided, and all payments on one day must be treated as one. Suppose the clerk had entered them on one line. If the cheques are held to

(1) 11 Ch. D. 772. (2) 4 D. M. & G. 372.

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have been paid out of our £770 10*s.* 5*d.* alone, the trustees will get nothing, and all the balance will go to Mrs. *Cotterill*, although she is in the same position as the trustees.

FRY, J., said in the course of the discussion :—

As to the £341 8*s.* 9*d.*, that sum was gone, and Mrs. *Cotterill* would get no part of it. According to *Clayton's Case* (1) the result depends upon the entries. Sir *W. Grant* in that case said: "But this is the case of a banking account where all the sums paid in form one blended fund, the parts of which have no longer any distinct existence. Neither banker nor customer ever thinks of saying, This draft is to be placed to the account of the £500 paid in on Monday, and this other to the account of the £500 paid in on Tuesday. There is a fund of £1000 to draw upon, and that is enough. In such a case there is no room for any other appropriation than that which arises from the order in which the receipts and payments take place and are carried into the account. Presumably it is the sum first paid in that is first drawn out. It is the first item on the debit side of the account that is discharged or reduced by the first item on the credit side. The appropriation is made by the very act of setting the two items against each other." The difficulty seems to be that the rule in that case has been applied by the Court of Appeal to a case between trustee and *cestui que trust*. I have already stated how I should be inclined to act if I had liberty, but I am not at liberty. It is for the payer to appropriate, but, failing that, the payee may appropriate and may enter the payments as he likes. As between banker and customer the banker is the payee and the customer is the payer, and if the customer says nothing the banker may appropriate. The Courts have said that that principle binds trustee and *cestui que trust*. If the two sums had been entered in one line of a double column, that might have shewn that it was the same sum, but that has not been done. The trustees have failed, and will get nothing.

C. A. From this judgment appeals were brought by the Plaintiff, by the trustees of *Hallett's* settlement, and by Mrs. *Cotterill*.

(1) 1 Mer. 572, 608.

The appeals came on for hearing on the 26th of November, 1879.

The Plaintiff's appeal was heard first.

As to the claim of the trustees of *Hallett's* settlement,

*Higgins*, Q.C., and *B. Fossett Lock*, for the Plaintiff:—

The trustees have no priority over the general creditors. There is no sufficient evidence that the Russian bonds were purchased with trust money, or that there was any appropriation of them to the trust. The memorandum in the fold of the settlement did not amount to a declaration of trust. It was never communicated to the trustees of the settlement.

*J. Pearson*, Q.C., and *Dundas Gardiner*, for the trustees of *Hallett's* settlement:—

There is sufficient evidence of the appropriation of Russian bonds to the trusts of the settlement. It was *Hallett's* duty to invest the fund, and less evidence is required in the case of a person who is bound to appropriate than in the case of one who is not. The memorandum is a good declaration of trust by *Hallett:* at all events it is an admission against his own interest: *In re Strahan* (1).

*Higgins*, in reply.

THE COURT reserved judgment on this claim.

As to Mrs. *Cotterill's* claim,

*Higgins*, Q.C., and *B. Fossett Lock*, for the Plaintiff:—

In this case *Hallett* was not a trustee at all. He was a mere bailee of Mrs. *Cotterill's* money. He was not even in a fiduciary position. Therefore the money cannot be followed into his hands. The fact of his receiving the dividends for her makes no difference. A banker does not become a trustee because bonds are deposited with him, but he may receive the coupons: *Ex parte Dale & Co.* (2); *Scott* v. *Surman* (3); *Whitecomb* v. *Jacob* (4).

[JESSEL, M.R.:—The decision in *Whitecomb* v. *Jacob* is based

(1) 8 D. M. & G. 291.
(2) 11 Ch. D. 772.
(3) Willes, 400.
(4) 1 Salk. 161.

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upon a wrong reason. It is said there, "In regard that money has no ear-mark, equity cannot follow that in behalf of him that employed the factor." It has been often held since that money may be ear-marked.]

*De Gex*, Q.C., and *E. Beaumont*, for Mrs. *Cotterill*, were not called on.

Dec. 3. The judgments on these two claims were delivered this day.

CLAIM OF THE TRUSTEES OF HALLETT'S SETTLEMENT.

JESSEL, M.R.:—

In the first appeal from Mr. Justice *Fry* the question is purely one of facts, or rather, as there is no dispute about the facts, what is the proper inference to be derived from the undisputed facts. Substantially the question is whether a considerable sum of trust money was invested by *Hallett* along with other trust money in the purchase of £2590 Russian bonds. Mr. Justice *Fry* has come to the conclusion that it was, and I am not disposed to differ from him. *Hallett* was a solicitor, and the case unfortunately presents one more instance of a solicitor betraying his trust; and the question is whether his numerous other clients, whose money he had misappropriated, or the trustees of his marriage settlement, whose money he had also misappropriated, are to suffer. The trust money appears to have been invested by *Hallett* at first in some mortgages. That was not made payable to the trustee, but to *Hallett*, and he received the interest, as he was entitled to do under the settlement, during his life. The last mortgage on which the money was invested was on the estate of a Mr. *Walker*. That mortgage was paid off in 1869. *Hallett* received the money. What he did with it is not clear, but there can be no doubt he appropriated it in some way to his own use. He had in his possession a large quantity of Russian bonds, and among them the £2590 Russian bonds in question, and whereas he used before 1870 to enter the interest on them in a lump sum, he now carried the bonds for £2590 to a separate account, and made entries of them as "self trust," entering the interest separately from the

interest on the other bonds. At some time or other he made a memorandum in the fold of the draft of his marriage settlement which contained this sentence: "The money remained in *Great George Street* until September, 1865, when it was invested in *Walker's* estate. *Walker's* mortgage was paid off in November, 1870, and invested in £2590 Russian £5 per Cent. Stock." This being in his handwriting is evidence against him. There is in addition this singular fact. He took to his bankers a large quantity of Russian bonds in two parcels. The envelope of one parcel has not been found, but the envelope of the other has an indorsement on it shewing that it contained bonds for £2412, the correct amount of bonds which he held in trust for another person, Mrs. *Cotterill;* and this amount, added to the bonds for £2590 claimed by *Hallett's* trustees, would make up the £5032 which he deposited on that occasion. When you see that he had other Russian bonds of his own, and took out some and deposited them in separate parcels, and that one of those parcels contained bonds held by him in a fiduciary relation, we may conclude that the other parcel was kept separate for no other purpose but appropriation. This is a circumstance corroborating the statement in his own handwriting. I am therefore of opinion that the trustees are entitled to the bonds which they claim, and are entitled to the produce of the sale of them. The judgment of Mr. Justice *Fry* on this point must therefore be affirmed.

BAGGALLAY and THESIGER, L.JJ., concurred.

CLAIM OF MRS. COTTERILL.

JESSEL, M.R.:—

The second appeal from Mr. Justice *Fry* in this case raises, in my opinion, not a question of fact, for the fact is indisputable, but a question of law of very considerable importance. The facts necessary to be stated are very few. A Mrs. *Cotterill* either had some money, which Mr. *Hallett* had invested for her in the purchase of Russian bonds, which I think is the more probable version of the transaction, for her memory does not appear to be very accurate, or she had some Russian bonds which he had de-

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livered to her and she re-delivered to him; it is utterly immaterial. What is proved in the case is that he gave her a receipt, which of course is binding against him and his estate, for a *Russian Bond and Waggon Company* debenture bonds. It appears that he had bonds to that amount in his possession, and it also appears that the exact amount was deposited by him with his bankers in a separate parcel in 1873. I think Mrs. *Cotterill* is not called upon to prove any more, and therefore as against Mr. *Hallett* and his legal personal representative these bonds are her bonds deposited with Mr. *Hallett*, according to the receipt, for safe custody, which would make him, no doubt, an ordinary bailee. In addition to that, it appears that Mr. *Hallett* was in the habit of receiving the income arising from these bonds on behalf of Mrs. *Cotterill*. I suppose he or the bankers cut off the coupons, and he received the money and accounted for the exact amount to her every half year. This receivership, of course, was the receivership of an agent—it was as bailee; therefore he was bailee of the bonds, and an agent to receive the dividends on the bonds. There is no doubt, therefore, that Mr. *Hallett* stood in a fiduciary position towards Mrs. *Cotterill*. Mr. *Hallett*, before his death, I regret to say, improperly sold the bonds and put the money to his general account at his bankers. It is not disputed that the money remained at his bankers mixed with his own money at the time of his death; that is, he had not drawn out that money from his bankers. In that position of matters Mrs. *Cotterill* claimed to be entitled to receive the proceeds, or the amount of the proceeds, of the bonds out of the money in the hands of Mr. *Hallett's* bankers at the time of his death, and that claim was allowed by the learned Judge of the Court below, and I think was properly so allowed. Indeed, as I understand the doctrines of Equity, it would have been too clear a case for argument, except for another decision of that learned Judge himself, *Ex parte Dale & Co.* (1). The modern doctrine of Equity as regards property disposed of by persons in a fiduciary position is a very clear and well-established doctrine. You can, if the sale was rightful, take the proceeds of the sale, if you can identify them. If the sale was wrongful, you can still take the proceeds of the sale, in a sense adopting the sale for the purpose of

(1) 11 Ch. D. 772.

taking the proceeds, if you can identify them. There is no distinction, therefore, between a rightful and a wrongful disposition of the property, so far as regards the right of the beneficial owner to follow the proceeds. But it very often happens that you cannot identify the proceeds. The proceeds may have been invested together with money belonging to the person in a fiduciary position, in a purchase. He may have bought land with it, for instance, or he may have bought chattels with it. Now, what is the position of the beneficial owner as regards such purchases? I will, first of all, take his position when the purchase is clearly made with what I will call, for shortness, the trust money, although it is not confined, as I will shew presently, to express trusts. In that case, according to the now well-established doctrine of Equity, the beneficial owner has a right to elect either to take the property purchased, or to hold it as a security for the amount of the trust money laid out in the purchase; or, as we generally express it, he is entitled at his election either to take the property, or to have a charge on the property for the amount of the trust money. But in the second case, where a trustee has mixed the money with his own, there is this distinction, that the *cestui que trust*, or beneficial owner, can no longer elect to take the property, because it is no longer bought with the trust-money simply and purely, but with a mixed fund. He is, however, still entitled to a charge on the property purchased, for the amount of the trust-money laid out in the purchase; and that charge is quite independent of the fact of the amount laid out by the trustee. The moment you get a substantial portion of it furnished by the trustee, using the word "trustee" in the sense I have mentioned, as including all persons in a fiduciary relation, the right to the charge follows. That is the modern doctrine of Equity. Has it ever been suggested, until very recently, that there is any distinction between an express trustee, or an agent, or a bailee, or a collector of rents, or anybody else in a fiduciary position? I have never heard, until quite recently, such a distinction suggested. It cannot, as far as I am aware (and since this Court sat last to hear this case, I have taken the trouble to look for authority), be found in any reported case even suggested, except in the recent decision of Mr. Justice *Fry*, to which I shall draw attention presently. It can have no foundation in principle,

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because the beneficial ownership is the same, wherever the legal ownership may be. If you have goods bargained and sold to a man upon trust to sell and hand over the net proceeds to another, that other is the beneficial owner; but if instead of being bargained and sold, so as to vest the legal ownership in the trustee, they are deposited with him to sell as agent, so that the legal ownership remains in the beneficial owner, can it be supposed, in a Court of Equity, that the rights of the beneficial owner are different, he being entire beneficial owner in both cases? I say on principle it is impossible to imagine there can be any difference. In practice we know there is no difference, because the moment you get into a Court of Equity, where a principal can sue an agent as well as a *cestui que trust* can sue a trustee, no such distinction was ever suggested, as far as I am aware. Therefore, the moment you establish the fiduciary relation, the modern rules of Equity, as regards following trust money, apply. I intentionally say modern rules, because it must not be forgotten that the rules of Courts of Equity are not, like the rules of the Common Law, supposed to have been established from time immemorial. It is perfectly well known that they have been established from time to time—altered, improved, and refined from time to time. In many cases we know the names of the Chancellors who invented them. No doubt they were invented for the purpose of securing the better administration of justice, but still they were invented. Take such things as these: the separate use of a married woman, the restraint on alienation, the modern rule against perpetuities, and the rules of equitable waste. We can name the Chancellors who first invented them, and state the date when they were first introduced into Equity jurisprudence; and, therefore, in cases of this kind, the older precedents in Equity are of very little value. The doctrines are progressive, refined, and improved; and if we want to know what the rules of Equity are, we must look, of course, rather to the more modern than the more ancient cases.

Now that being the established doctrine of Equity on this point, I will take the case of the pure bailee. If the bailee sells the goods bailed, the bailor can in Equity follow the proceeds, and can follow the proceeds wherever they can be distinguished, either being actually kept separate, or being mixed up with other

moneys. I have only to advert to one other point, and that is this—supposing, instead of being invested in the purchase of land or goods, the moneys were simply mixed with other moneys of the trustee, using the term again in its full sense as including every person in a fiduciary relation, does it make any difference according to the modern doctrine of Equity? I say none. It would be very remarkable if it were to do so. Supposing the trust money was 1000 sovereigns, and the trustee put them into a bag, and by mistake, or accident, or otherwise, dropped a sovereign of his own into the bag. Could anybody suppose that a Judge in Equity would find any difficulty in saying that the *cestui que trust* has a right to take 1000 sovereigns out of that bag? I do not like to call it a charge of 1000 sovereigns on the 1001 sovereigns, but that is the effect of it. I have no doubt of it. It would make no difference if, instead of one sovereign, it was another 1000 sovereigns; but if instead of putting it into his bag, or after putting it into his bag, he carries the bag to his bankers, what then? According to law, the bankers are his debtors for the total amount; but if you lend the trust money to a third person, you can follow it. If in the case supposed the trustee had lent the £1000 to a man without security, you could follow the debt, and take it from the debtor. If he lent it on a promissory note, you could take the promissory note; or the bond, if it were a bond. If, instead of lending the whole amount in one sum simply, he had added a sovereign, or had added £500 of his own to the £1000, the only difference is this, that instead of taking the bond or the promissory note, the *cestui que trust* would have a charge for the amount of the trust money on the bond or promissory note. So it would be on the simple contract debt; that is, if the debt were of such a nature as that, between the creditor and the debtor, you could not sever the debt into two, so as to shew what part was trust money, then the *cestui que trust* would have a right to a charge upon the whole. Therefore, there is no difficulty in following out the rules of Equity and deciding that in a case of a mere bailee, as Mr. Justice *Fry* has decided, you can follow the money.

Having said so much, I feel bound to say something about the authorities, and for two reasons. First of all, this decision of Mr. Justice *Fry's* to which I have referred is reported, and, there-

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fore, in my opinion, may do mischief if not corrected; and, secondly, because it appears to me, speaking with the greatest possible respect of such an eminent master of Equity as Mr. Justice *Fry*, that he has entirely misconceived the proper use of authorities in holding himself to be bound by a long line of authorities, to decide against that which he saw most clearly was good equity; in other words, he decided against his own opinion as to the rules of Equity, in obedience, as he thought, to a series of authorities, opposed, as he conceived, to all principle, because he thought he was bound so to do, as it appears to me, in utter oblivion of what I will take the liberty of stating is the right mode of viewing authorities, and also in oblivion of that salutary provision of the *Judicature Act* which says that where there is a difference between the principles of Law and Equity, the rules of Equity are to prevail.

First of all, what is the proper use of authorities? This is almost elementary, but I am bound to state it, because, as I will shew presently, that use has not been made in the case on which I am going to comment. The only use of authorities, or decided cases, is the establishment of some principle which the Judge can follow out in deciding the case before him. There is, perhaps, nothing more important in our law than that great respect for the authority of decided cases which is shewn by our tribunals. Were it not for that our law would be in a most distressing state of uncertainty; and so strong has that been my view, that where a case has decided a principle, although I myself do not concur in it, and although it has been only the decision of a tribunal of co-ordinate jurisdiction, I have felt bound to follow it where it is of respectable age and has been used by lawyers as settling the law, leaving to the Appellate Court to say that case is wrongly decided, if the Appellate Court should so think.

Now when we come to look at the case which was before Mr. Justice *Fry*, the case of *Ex parte Dale & Co.* (1), we shall find him saying this: "Does it make any difference that instead of trustee and *cestui que trust* it is a case of fiduciary relationship? What is a fiduciary relationship? It is one in respect of which, if a wrong arise, the same remedy exists against the wrongdoer on

(1) 11 Ch. D. 772, 778.

behalf of the principal as would exist against a trustee on behalf of the *cestui que trust*. If that be a just description of the relationship, it would follow that wherever fiduciary relationship exists, and money coming from the trust lies in the hands of persons standing in that relationship, it can be followed and separated from any money of their own. That seems to me to be the logical result of *Pennell* v. *Deffell*" (1). Up to that point I agree with every syllable, and I think it would be impossible to express the doctrine more clearly than it is there expressed by Mr. Justice *Fry*. But now comes the unfortunate result, "but that result is opposed to the long line of authorities to which I have referred, and from which I do not feel myself justified upon any reasoning of my own in departing." So he here decided the case wrongly and against his own opinion and against the case of *Pennell* v. *Deffell* in deference to a long line of authorities. That being so, I feel bound to examine his supposed long line of authorities, which are not very numerous, and shew that not one of them lends any support whatever to the doctrine or principle which he thinks is established by them.

The first case is the well-known case of *Whitecomb* v. *Jacob* (2). I may say the cases are so fully extracted, if I may use the word, in Mr. Justice *Fry's* judgment as regards the material portions of them, that it is more convenient to read them from that than it is from the reports themselves, which I have looked at. "If one employs a factor and entrusts him with the disposal of merchandise, and the factor receives the money and dies indebted in debts of a higher nature, and it appears by evidence that this money was vested in other goods and remains unpaid, those goods shall be taken as part of the merchant's estate and not the factor's" (that is, you may follow the money or the goods); "but if the factor have the money, it shall be looked upon as the factor's estate, and must first answer the debts of a superior creditor, &c.; for, in regard that money has no ear-mark, Equity cannot follow that in behalf of him that employed the factor" (3). Now let us see, therefore, what *Whitecomb* v. *Jacob* decides. It decides that the equity as to following the proceeds attaches to the case of a factor

(1) 4 D. M. & G. 372. (2) 1 Salk. 161.
(3) 11 Ch. D. 775.

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as well as to the case of *cestui que trust* and trustee. That is what it decides; but it decides, secondly, that you could not follow money because it had no ear-mark. The first part is good law at the present day; the second is not. Whether it was good law or not at the time of *Salkeld* it is immaterial to consider. It is very doubtful whether Equity had got quite so far at that date as since, and therefore I will not say it was not: but it is not so now. The first part is good law and the second part is not, and therefore *Whitecomb* v. *Jacob* (1) is no authority at all on the second point on which it was decided, and so Mr. Justice *Fry* said. Then Mr. Justice *Fry* proceeds in his judgment to say, "Now, with the single exception that it appears to have been held subsequently that money may be so far ear-marked that it may be followed if it has been kept separate, that case appears to have been always held to be an authority;" that is to say, with the single exception that the sole ground for the decision has been overruled, it is to be an authority! Did ever any one hear anything, if I may say so, so extraordinary as such a comment on an old case? The sole ground of that decision was that, although as a general rule you may follow the proceeds as against the factor, as you may against the trustee in Equity, yet, because money has no ear-mark, you cannot follow it. That is overruled, and still the Judge holds it to be an authority. It appears to me no authority at all, the sole ground of the decision having been long since overruled—indeed it was overruled by some of the authorities which Mr. Justice *Fry* cites. He goes on, "In the celebrated case of *Ryall* v. *Rolle* (2) Mr. Justice *Burnet*, in delivering judgment, says: 'Suppose goods are consigned to a factor who sells them and breaks, the merchant for the money must come in as a creditor under the commission; but if the money is laid out in other goods these goods will not be subject to the bankruptcy.'" It is the same as *Whitecomb* v. *Jacob*. You may follow the goods, but you cannot follow the money. That is no longer law. In bankruptcy no part of the law is better settled than that if the money be kept separate it does not fall into the general estate. It has been decided by a long line of cases in bankruptcy, and there is no doubt about it if it is kept separate; but Mr. Justice *Burnet* only said what was said in the

(1) 1 Salk. 161. (2) 1 Atk. 165.

case in *Salkeld;* the notion being that you could not follow money, a notion which was prevalent at that time. That part of *Ryall* v. *Rolle* (1) is as much overruled as the case of *Whitecomb* v. *Jacob* (2). But it is to be observed that the Judges thought then that you could not follow money in Equity, not that you could not follow it between principal and agent or merchant and factor, they thought that you could not follow it at all, even as between trustee and *cestui que trust,* because money had no ear-mark. It is not an authority for a distinction between the case of principal and agent and the case of *cestui que trust* and trustee; it is an authority, if it is an authority for anything, that you cannot follow money in that way. Then Mr. Justice *Fry* says, "In another case of *Ex parte Dumas* (3), before Lord *Hardwicke,* the petitioners were certain persons who had claimed bills arising from the produce of certain goods transmitted to them, and the Lord Chancellor said: 'Suppose the petitioners had consigned over goods to *Jullian* as their factor, and he had sold them and turned them into money, the principal then could only have come in as a general creditor under the commission; but if the goods had continued in specie and had been found in *Jullian's* hands at the time of his bankruptcy, it would have been otherwise, and has been so determined in several cases.'" There it is to be noticed that the expression is "turned them into money," but nothing is said about the money being kept separate or not. I looked into the late Mr. *Lewin's* book on Trustees to see what he said about this case, because it is very odd that Lord *Hardwicke* should say so, and what Mr. *Lewin* says is that it seems in the time of Lord *Hardwicke* it was supposed that you could not follow money in Equity, which perhaps is the explanation, namely, that the doctrine is more modern than his decision. This is certainly not law now. As I said before there is no doubt in bankruptcy if the money is kept separate it can be followed; but it is the same proposition. It is not as if there were any difference between the position of factor and the position of trustee, but it is that you cannot follow the money. That he treats as well ascertained law at that time. Then Mr. Justice *Fry* goes on to say this, "Mr. Justice *Willes,* in delivering the considered

(1) 1 Atk. 165. (2) 1 Salk. 161.
(3) 1 Atk. 232.

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judgment of the Court of Common Pleas in the case of *Scott* v. *Surman* (1)"—I do not understand that a judgment is any better for being held over a long time, for I think judgments are perhaps best if delivered when the facts are fresh in the Judge's mind; but I do not say that they are either better or worse—"says: 'We are all agreed that if the money for which the tar had been sold had been all paid to the bankrupt before his bankruptcy, and had not been laid out again by him in any specific thing to distinguish it from the rest of his estate, in that case the Plaintiffs could not have recovered anything in this action, but must have come in as creditors under the commission, as is laid down in the case of *Whitecomb* v. *Jacob* (2) and in many other cases.'"

Now, first of all, that is merely a *dictum* of that very eminent Judge, Mr. Justice *Willes*, and he has not adverted to the distinction between money ear-marked and money not ear-marked. He has simply quoted from *Whitecomb* v. *Jacob* without considering it at all. If you read it literally, it means if it has not been laid out on any specific thing. Now that was not law in his time in bankruptcy, and I am quite sure if Mr. Justice *Willes'* attention had been called to the phrase used he would have said it was too general. If the money had been laid aside by the bankrupt, and put into a bag, and marked, you could take the money. I think Mr. Justice *Willes* would have qualified it. It is a mere *dictum*, and it really only follows *Whitecomb* v. *Jacob*. Then Mr. Justice *Fry* says: "In the year 1800 the Lord Chancellor, in *Ex parte Sayers* (3), adopted the same view." That was Lord *Thurlow*. "He considered that there were in that case special circumstances which shewed that, although the money had got into the general fund constituting the estate of the bankrupt, it had got out again; and he said it had acquired an identity and a distinction from the rest of the fund. Still he adopted the general principle that if it had been in the form of money at the time of the bankruptcy, the creditor could only rank with the other creditors." It is quite true he said so, but again the same observation applies. He states it generally on the supposition of the factor having turned the goods into money, without distinguishing between the cases of the

(1) Willes, 400. (2) 1 Salk. 161.
(3) 5 Ves. 169.

money being kept separate and the cases where it was mixed with his own, and could not be followed.

Now we come to a case which I am glad to say is the last—the well-known case of *Taylor* v. *Plumer* (1), where we have the decision of a great Judge, no doubt, Lord *Ellenborough*; and there he entirely throws over all the prior decisions as to money not ear-marked not being followed. At that time it was well known it could be ear-marked in Equity; and therefore when you come to look at it you will find it an express decision in conflict with all the others cited as to the ear-marking of money. Lord *Ellenborough* says this: "It makes no difference in reason or law into what other form different from the original the change may have been made"—there I agree with him most cordially in reason and in law—"whether it be into that of promissory notes for the security of the money which was produced by the sale of the goods of the principal, as in *Scott* v. *Surman* (2)"—and I say whether it be a simple contract debt or not it is the same thing—"or into other merchandise, as in *Whitecomb* v. *Jacob* (3), for the product of or substitute for the original thing still follows the nature of the thing itself as long as it can be ascertained to be such." That, if I may say so, is law at the present moment; and though I cannot say it always was law, it always ought to have been law, because it is consonant with principle. Now comes the point, "and the right only ceases when the means of ascertainment fail." That is correct. Now there comes a point which is not correct, but which I am afraid only ceases to be correct because Lord *Ellenborough's* knowledge of the rules of Equity was not quite commensurate with his knowledge of the rules of Common Law, "which is the case when the subject is turned into money, and mixed and confounded in a general mass of the same description." He was not aware of the rule of Equity which gave you a charge—that if you lent £1000 of your own and £1000 trust money on a bond for £2000, or on a mortgage for £2000, or on a promissory note for £2000, Equity could follow it, and create a charge; but he gives that, not as law—the law is that it only fails when the means of ascertainment fail—he gives it as a case

(1) 3 M. & S. 562. (2) Willes, 400.
(3) 1 Salk. 161.

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in which the means of ascertainment fail, not being aware of this refinement of Equity by which the means of ascertainment still remain. With the exception of that one fact, which is rather a fact than a statement of law, the rest of the judgment is in my opinion admirable. It goes on: "The difficulty which arises in such a case is a difficulty of fact, and not of law, and the *dictum* that money has no ear-mark must be understood in the same way, *i.e.*, as predicated only of an undivided and undistinguishable mass of current money." There, again, as I say, he did not know that Equity would have followed the money, even if put into a bag or into an undistinguishable mass, by taking out the same quantity.

Now, I have finished the authorities cited by Mr. Justice *Fry*. Is there one of them (and I say there is not) which suggests there is any difference in the position of the factor and the position of the trustee as regards following money? So far from that being the case, they all proceed on the ground that there is no such distinction, and the only reason of the difficulty was that which was so lucidly expressed by Lord *Ellenborough*, the difficulty of ascertainment.

Now I come, before parting with the case, to the decision of *Pennell* v. *Deffell* (1), which is an Equity case decided by the Court of Appeal in Chancery, and therefore of as high authority as any of those cases cited, and of greater weight, because it is more modern than the decisions of Lord *Hardwicke* and Lord *Thurlow;* and, if inconsistent with them, would have overruled them. What is said in *Pennell* v. *Deffell?* Lord Justice *Knight Bruce* there supposes the case of a trust fund kept separate, and he then refers to the case of a trust fund mingled with the other money; that is, if the trustee in the case I suppose put the money in a box with his other money, it would make no difference to the *cestui que trust* except that he would have the right to take the first money out of the box; and then he says, "But not in either case, as I conceive, would the blending together of the trust moneys, however confusedly, be of any moment as between the various *cestuis que trustent* on the one hand and the executors, as representing the general creditors, on the other."

Now, in addition to that, I will only refer to one other case. It

(1) 4 D. M. & G. 372.

is a very good case, and it is again the decision of a well-known Equity Judge, whom we are delighted still to have living among us. It is the case of *Frith* v. *Cartland* (1).] I will read the marginal note: "The rules as to following trust funds in the hands of a defaulting trustee apply against the assignees of a defaulting trustee as fully as against the trustee himself" (that is, they apply in bankruptcy as well as they do on death), "and the circumstance that the trust fund was acquired on the eve of the bankruptcy, and when the bankrupt was about to abscond with that and his other moneys: held, not to raise any equity in favour of the assignees." Now I read that because the man, as it will be seen, was an agent, and Vice-Chancellor *Wood* never dreamt it made any difference, nor anybody else. The facts of the case are these. [His Lordship then referred to the facts as stated in the report, and continued:—] Now the Vice-Chancellor says this (2): "*Pennell* v. *Deffell* (3) is a very instructive case upon all questions of this kind." I am citing the case for the next remark which, I think, would have presented itself to Mr. Justice *Fry*. "It does not, indeed, lay down any new principle, but it contains a particularly clear and able enunciation of established doctrines in their bearing upon circumstances of some difficulty. The guiding principle is, that a trustee cannot assert a title of his own to trust property. If he destroys a trust fund by dissipating it altogether there remains nothing to be the subject of the trust. But so long as the trust property can be traced and followed into other property into which it has been converted that remains subject to the trust. A second principle is, that if a man mixes trust funds with his own, the whole will be treated as the trust property, except so far as he may be able to distinguish what is his own," that is, that the trust property comes first. Now, I think it would have been well if this, which was stated as established Equity law in *Frith* v. *Cartland* by Vice-Chancellor *Wood*, had been accepted and adopted in the case of *Ex parte Dale & Co.* (4). Then he says: "If a man has £1000 of his own in a box on one side and £1000 of trust property in the same box on the other side, and then takes out £500 and applies it to his own

(1) 2 H. & M. 417.
(2) Ibid. 420, 421.
(3) 4 D. M. & G. 372.
(4) 11 Ch. D. 772.

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purposes, the Court will not allow him to say that that money was taken from the trust fund. The trust must have its £1000 so long as a sufficient sum remains in the box. So here, *Edwards* could not be allowed to say that the £284 deposited in the *Bank of England* was his own, and that the trust portion of the fund was that which he took abroad with him, and from which he drew as he required for his own purposes. There is therefore no difficulty in treating that sum at the bank as belonging to the trust together with what remains of the sum which he took abroad."

I think after those authorities it must now be considered settled that there is no distinction, and never was a distinction, between a person occupying one fiduciary position or another fiduciary position as to the right of the beneficial owner to follow the trust fund, and that those cases which have been cited at Law so far from establishing a distinction, establish the contrary; and that the mere error of supposing that Equity could not follow or distinguish money in the cases supposed, if error it was, and perhaps it was not so originally (I am not sure that the doctrine of equity had got so far at the first start, but it was certainly an error at a later period), is attributable really to the fact that the Judges who followed the earlier cases were not aware of what I may call the gradual refinement of the doctrine of equity. Therefore, looking at the authorities to find out the principle, you do not find out any such distinction established as that suggested by Mr. Justice *Fry*, or anything of the kind even mentioned in them; and I do not know of anything more mischievous than for a Judge to say, "The cases before me establish no principle, but they quite establish something else which I will now enunciate, and therefore hold myself bound by those cases to establish another principle which was never suggested or thought of by the Judges who decided the original cases." It is only out of my great respect and esteem for the learned Judge from whom this appeal comes that I have thought it right to go so fully into the cases to shew that there is no foundation whatever for the suggested distinction, and therefore his decision in this case rests on no trivial or slight distinction between this case and the case of *Ex parte Dale & Co.* (1), but is grounded on the well-ascertained doctrines of equity.

(1) 11 Ch. D. 772.

Before I part with the case I will only say a word or two more. There was cited to Mr. Justice *Fry* a decision of the Appeal Court. It is reported in a note to the case of *Ex parte Dale & Co.* (1), and the name of it is *Birt* v. *Burt*. That was a case of money put into the bank. The only reason why I have not referred to it in the course of my judgment is, that I took part in the decision of the appeal, together with Chief Justice *Coleridge* and Lord Justice *Baggallay*, and we considered the case too clear for argument, and dismissed the appeal with costs.

BAGGALLAY, L.J. :—

I am also of opinion that this appeal should be dismissed. It appears to me sufficient, to support the conclusion at which I have arrived, to say that I entirely agree with Mr. Justice *Fry* in opinion that, upon the facts and the law of the case, *Hallett* stood in a fiduciary position, that he violated his duty, that Mrs. *Cotterill* consequently had the same right to relief against him as if he had been a trustee under the more common designation of the term, and that under those circumstances she had a right to follow the produce of the sale of the bonds. Nor should I have thought it necessary to have at all adverted to the case of *Ex parte Dale & Co.*, which had been previously decided by Mr. Justice *Fry*, had it not been that the Master of the Rolls has very closely examined the judgment in that case, and expressed his disapprobation of the decision arrived at. Now I cannot forget that *Ex parte Dale & Co.* is a decision of very recent date, and that it may possibly come before the Court of which I am a member by way of appeal; and for this reason I should desire to keep my mind as free from any bias or prejudice upon it as possible; but at the same time, so far as the grounds of the decision in that case appear in the printed report of the judgment, and accepting that report as being perfectly and in all respects correct, I think it right to express an opinion upon it. It must be borne in mind that Mr. Justice *Fry* arrived at the conclusion, at which he did arrive in that case, with much hesitation, and that he apparently would have arrived at a different conclusion, had he not felt himself bound by certain authorities, to which he alluded,

(1) 11 Ch. D. 772.

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and from which he stated that he did not feel himself justified in departing, though he regarded them as inconsistent with the general principles of equity applicable to cases involving fiduciary relationship. Assuming there to have been nothing more in the case than appears in the printed report, I feel bound to say that I cannot concur in the view expressed by Mr. Justice *Fry* as to the binding character of the authorities to which he referred.

THESIGER, L.J. :—

The facts of this case are undisputed, and the inference to be drawn from them is so clear, that I need say no more than that I entirely agree with the view that was taken by Mr. Justice *Fry* with reference to that inference. With regard to the law applicable to the case, we have had an elaborate exposition of that law from the Master of the Rolls, and in the main features of that exposition I entirely agree; but I must add, at the same time, that the principles which have been laid down to-day are no new principles, and have been laid down recently in this Court, not only in the case to which the Master of the Rolls has referred of *Birt* v. *Burt* (1), but also in the case of *Ex parte Cooke* (2). If the judgment of Lord Justice *Bramwell* is looked at in that case, it will appear that even to the mind of a Common Law Judge the principles of law which have been applied now for some time in Equity have been made perfectly plain. It has been established for a very long period, in cases at Law as well as in cases in Equity, that the principles relating to the following of trust property are equally applicable to the case of a trustee, using the term in the narrow and technical sense which is applied to it in the Court below, and to the case of factors, bailees, or other kinds of agents. It has been also established, and for a long period, and I think, notwithstanding the observations of the Master of the Rolls that that has been present to the mind of the Common Law Judges as well as to the mind of Equity Judges, that those principles may, under certain circumstances, be applicable to money as well as to specific chattels. The principle of law may be stated, as it appears to me, in the form of a very simple, although at the same time very wide and general proposition. I would state that proposition in these

(1) 11 Ch. D. 773, n. (2) 4 Ch. D. 123.

terms, namely, that wherever a specific chattel is intrusted by one man to another, either for the purposes of safe custody or for the purpose of being disposed of for the benefit of the person intrusting the chattel; then, either the chattel itself, or the proceeds of the chattel, whether the chattel has been rightfully or wrongfully disposed of, may be followed at any time, although either the chattel itself, or the money constituting the proceeds of that chattel, may have been mixed and confounded in a mass of the like material. I may say that that proposition, wide as it is, was adopted almost in those terms by Lord Justice *Bramwell* in the case to which I have referred. There is no doubt that there are to be found here and there in the books, *dicta*, principally of Common Law Judges, which would appear to militate against the generality of that proposition, and which would appear to shew that in the minds of those Judges there was the view, that while chattels might be followed, or money so long as it could be looked upon as a specific chattel, as moneys numbered and placed in a bag, yet when those moneys had been mixed with other moneys that there was no ear-mark, and neither at Law nor in Equity could they be followed. With reference, however, to those *dicta*, it appears to me there are two observations to be made. In the first place I cannot find any decision which has followed out those *dicta* to their consequence, assuming that those *dicta* are to be treated as having the generality which at first sight attaches to them. And, in the second place, it appears to me that in many cases those *dicta*, looking to the facts of the particular case, may be restrained to those facts, and possibly may have a more limited meaning than that which has been attached to them by Mr. Justice *Fry* in the case of *Ex parte Dale & Co.* (1), or by the Master of the Rolls in his judgment in the present case. As far as I can judge, the only exception to the general proposition which I have stated is not a real exception, but an apparent exception, for all cases where it has been held that moneys mixed and confounded, but still existing, in a mass cannot be followed, may, I think, be resolved into cases where, although there may have been a trust with reference to the disposition of the particular chattel which those moneys subsequently represented, there was no trust, no

(1) 11 Ch. D. 772.

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duty in reference to the moneys themselves beyond the ordinary duty of a man to pay his debts; in other words, that they were cases where the relationship of debtor and creditor had been constituted, instead of the relation either of trustee and *cestui que trust*, or principal and agent. I think it unnecessary, and to my mind it is undesirable, to give an opinion upon the case of *Ex parte Dale & Co.* (1) until we see upon a case properly brought upon appeal, and when it is necessary to decide the point, whether that case does or does not come within the exception to which I have referred.

The appeals of the trustees of *Hallett's* settlement and Mrs. *Cotterill* were then heard.

*J. Pearson*, Q.C., and *Dundas Gardiner*, for the Appellants:—

We appeal from so much of Mr. Justice *Fry's* order as directed that the claim of the trustees is to be governed by *Clayton's Case* (2). Mrs. *Cotterill* appeals from the same decision, and if the Court allows the appeal, the balance left to *Hallett's* credit at his bankers will be sufficient for both of us; but if the Court is against us, a further question will arise as to the division of what is applicable to our claims between us and Mrs. *Cotterill*.

We contend, then, that the rule in *Clayton's Case*, by which the earliest drawings are to be appropriated to the earliest payments, does not apply to a case like this, in which trust moneys were mixed with the customer's own moneys. It is only a general rule based on a presumption of law which may be rebutted by the intention of the parties or the circumstances: *City Discount Company* v. *McLean* (3). It is well settled that if an act which has been done may have been done honestly, the man who does it cannot say that he has done it dishonestly. If a man mixes his own money with trust money, and draws some out, he must be taken to have drawn out his own money, and cannot be allowed to say that he has stolen the money deposited with him: *Pinkett* v. *Wright* (4); *Ex parte Kelly & Co.* (5). There is no difference in

(1) 11 Ch. D. 772.
(2) 1 Mer. 572.
(3) Law Rep. 9 C. P. 692.
(4) 2 Hare, 120.
(5) 11 Ch. D. 306.

principle between money kept by a trustee himself, and any deposits by him at a banker's to his own account. Mr. Justice *Fry* agreed with us in principle, but felt himself bound by the authority of *Pennell* v. *Deffell* (1). But the decision of the Lords Justices on that particular point is not borne out by the principles stated by them in the rest of their judgment. At all events this Court is not bound to follow that decision if it is contrary to the principles on which the Court has always acted.

*De Gex*, Q.C., and *E. Beaumont*, for Mrs. *Cotterill*, supported the same view.

*Higgins*, Q.C., and *B. Fossett Lock*, for the Plaintiff:—

The point in dispute was solemnly decided in *Pennell* v. *Deffell* after full argument, and this Court is bound by that authority. The principle of the decision has been recognised in subsequent cases: *Merriman* v. *Ward* (2); *Ex parte Dickin* (3); *Hooper* v. *Keay* (4); *Frith* v. *Cartland* (5); *Brown* v. *Adams* (6); *Middleton* v. *Pollock* (7); *Ex parte Cooke* (8). That decision was consistent with the law as previously recognised. The appropriation of payments is a question of fact, and is the same in Equity as Law. If one party wishes to appropriate, he must communicate his election to the other party: *Simson* v. *Ingham* (9). If neither party appropriates, the earliest sums paid and repaid are set against one another. There is a broad distinction between sovereigns placed in a bag and money deposited with a banker. The latter ceases to exist in specie, and becomes a debt due from the banker. The principle of following trust money has never been carried to this extent. *Lord Chedworth* v. *Edwards* (10) is a distinct authority against it. If you can follow trust money into a banker's account, where can you stop? The account might be carried back to any length of time. The Plaintiff, who is a creditor of *Hallett*, is not estopped from saying that *Hallett* acted dishonestly, even though *Hallett* may have been estopped himself.

(1) 4 D. M. & G. 372, 384.
(2) 1 J. & H. 371.
(3) 8 Ch. D. 377, 384.
(4) 1 Q. B. D. 178.
(5) 2 H. & M. 417.
(6) Law Rep. 4 Ch. 764.
(7) 4 Ch. D. 49.
(8) Ibid. 123.
(9) 2 B. & C. 65.
(10) 8 Ves. 46.

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This is an appeal from a decision of Mr. Justice *Fry*, and the singularity of the appeal is this, that it is an appeal in favour of Mr. Justice *Fry's* opinion and against his decision; the explanation of that being, that the learned Judge conceived himself bound by some decisions of the Appeal Court to decide against his own opinion; and I am far from saying that I dissent from him on either point—either on principle, as to how he thought the case ought to be decided, or on the question whether a Judge in his position as a Judge of first instance could very well have decided otherwise.

The question we have to consider depends on very few facts. I will first state all those which I think material, and on which it appears to me my judgment ought to be based. A Mr. *Hallett*, a solicitor, was a trustee of some bonds. Without authority and improperly he sold them, and on the 14th of November, 1877, by his direction the proceeds of these bonds were paid to his credit at Messrs. *Twinings' Bank*, and there mixed with moneys belonging to himself, to the credit of the same banking account, and he also drew out by ordinary cheque moneys from the banking account, which he used for his own purposes. He died in February, 1878, and at his death the account stood in this way: that there was more money to the credit of the account than the sum of trust money paid into it; but if you applied every payment made after November, 1877, to the first items on the credit side in order of date, a large portion of the trust money would have been paid out. The question really is, whether or not, under these circumstances, the beneficiaries—that is, the persons entitled to the trust moneys, who are the present Appellants—are or are not entitled to say that the moneys subsequently drawn out—that is, drawn out by Mr. *Hallett* subsequently to November, 1877—and applied for his own use, are to be treated as appropriated to the repayment of his own moneys, or whether the Respondents, the executors, are right in their contention that they are to be treated as appropriated in the way I have mentioned, so as to diminish the amount now applicable to the repayment of the trust funds.

I will first of all consider the case on principle, and then I will

consider how far we are bound by authority to come to a decision opposed to principle. It may well be, and sometimes does so happen, that we are bound to come to a decision opposed to principle. Now, first upon principle, nothing can be better settled, either in our own law, or, I suppose, the law of all civilised countries, than this, that where a man does an act which may be rightfully performed, he cannot say that that act was intentionally and in fact done wrongly. A man who has a right of entry cannot say he committed a trespass in entering. A man who sells the goods of another as agent for the owner cannot prevent the owner adopting the sale, and deny that he acted as agent for the owner. It runs throughout our law, and we are familiar with numerous instances in the law of real property. A man who grants a lease believing he has sufficient estate to grant it, although it turns out that he has not, but has a power which enables him to grant it, is not allowed to say he did not grant it under the power. Wherever it can be done rightfully, he is not allowed to say, against the person entitled to the property or the right, that he has done it wrongfully. That is the universal law.

When we come to apply that principle to the case of a trustee who has blended trust moneys with his own, it seems to me perfectly plain that he cannot be heard to say that he took away the trust money when he had a right to take away his own money. The simplest case put is the mingling of trust moneys in a bag with money of the trustee's own. Suppose he has a hundred sovereigns in a bag, and he adds to them another hundred sovereigns of his own, so that they are commingled in such a way that they cannot be distinguished, and the next day he draws out for his own purposes £100, is it tolerable for anybody to allege that what he drew out was the first £100, the trust money, and that he misappropriated it, and left his own £100 in the bag? It is obvious he must have taken away that which he had a right to take away, his own £100. What difference does it make if, instead of being in a bag, he deposits it with his banker, and then pays in other money of his own, and draws out some money for his own purposes? Could he say that he had actually drawn out anything but his own money? His money was there, and he had a right to draw it out, and why should the natural act of simply drawing

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out the money be attributed to anything except to his ownership of money which was at his bankers.

It is said, no doubt, that according to the modern theory of banking, the deposit banker is a debtor for the money. So he is, and not a trustee in the strict sense of the word. At the same time one must recollect that the position of a deposit banker is different from that of an ordinary debtor. Still he is for some purposes a debtor, and it is said if a debt of this kind is paid by a banker, although the total balance is the amount owing by the banker, yet considering the repayments and the sums paid in by the depositor, you attribute the first sum drawn out to the first sum paid in. That was a rule first established by Sir *William Grant* in *Clayton's Case* (1); a very convenient rule, and I have nothing to say against it unless there is evidence either of agreement to the contrary or of circumstances from which a contrary intention must be presumed, and then of course that which is a mere presumption of law gives way to those other considerations. Therefore, it does appear to me there is nothing in the world laid down by Sir *William Grant* in *Clayton's Case*, or in the numerous cases which follow it, which in the slightest degree affects the principle, which I consider to be clearly established.

Then I come to the great difficulty in the case, the difficulty which, as I shall shew from an extract or two from Mr. Justice *Fry's* judgment, weighed with him. What he says is this: "If the matter were unfettered by authority, it would appear to me clear that where a man has a balance to his credit consisting in part of funds which are his own, and which he may legally draw out and apply for his own purposes, and in part of trust funds which he cannot lawfully draw out and apply for his own purposes, his drawings for his own purposes ought to be attributed to his own funds and not to the trust funds. But it appears to me that I am not at liberty, in the existing state of the authorities, to act according to the inclination of my own mind;" and then he refers to *Pennell* v. *Deffell* (2), and one or two cases that have followed it. In a second judgment in the same case, Mr. Justice *Fry* says this: "I have already expressed the opinion I should have been inclined to act on if I had been at liberty, but I

(1) 1 Mer. 572. (2) 4 D. M. & G. 372.

am not at liberty." So it is plain that, as far as Mr. Justice *Fry* was concerned, he would have decided otherwise if he had not been fettered by authority.

Now, the only authority worth considering for this purpose is the case of *Pennell* v. *Deffell* (1) itself. I will, in a moment, say a word about the subsequent decisions. First of all *Pennell* v. *Deffell*, one must remember, is the decision of a Court of co-ordinate jurisdiction with this Court, namely, the Court of Appeal in Chancery, and was decided several years ago. But, on the other hand, we must remember that the law ascertained or laid down in the decision or judgment which guides a future Judge or another Judge in applying it, is simply the expression of principle which is to be ascertained from the judgment. No doubt a part of the decision in *Pennell* v. *Deffell* was exactly this case, and the Court applied the law, as correctly stated by Mr. Justice *Fry*, by applying *Clayton's Case* (2) even to such a case as this, and to that extent destroyed the claim of the *cestui que trust*. But that was not the whole case of *Pennell* v. *Deffell*. The main part of *Pennell* v. *Deffell* was giving effect to the right of *cestuis que trust* in the case of blended trust moneys, and upon the very principle which I have endeavoured to explain, and which, if I may say so, was so clearly explained by Mr. Justice *Fry* in his judgment. If, therefore, we are to ascertain the principle on which *Pennell* v. *Deffell* is decided, we must look at the whole of the judgment, and not at one part of it only. That being so, I have come to this conclusion, that the principle is rightly laid down, and it is rightly applied throughout the judgment except as to this portion, and that as to this portion of the case there has been a mistake, not in the principle, but in the application of the principle. Therefore, if I am to be guided by the principle as laid down, I think the principle must prevail without regard to a mere slip in its application.

But it will be said that this part of *Pennell* v. *Deffell* has been followed in subsequent cases. So it has. As regards subsequent cases in the inferior Courts we need not trouble ourselves with them. Judges of first instance would not have overruled the mistaken application of principle. As regards the Court of Appeal,

(1) 4 D. M. & G. 372. (2) 1 Mer. 572.

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it seems to have been followed certainly in one, if not in two cases, without question; but although there are cases in our law where erroneous decisions, not reconcilable even with the judgment on which the decision proceeded, have created a rule of conduct, and as to which, after the lapse of years, Judges have not felt themselves at liberty to review the decision even by the light of the judgment on which the first decision was pronounced, yet no such considerations apply to this case. No human being ever gave credit to a man on the theory that he would misappropriate trust money, and thereby increase his assets. No human being ever gave credit, even beyond that theory, that he should not only misappropriate trust moneys to increase his assets, but that he should pay the trust moneys so misappropriated to his own banking account with his own moneys, and draw out after that a larger sum than the first sums paid in for the trust moneys. It never could have been made a rule of conduct, or have affected the transactions of mankind, and therefore it does not come within the line of cases which, having established a rule of conduct, no Judge could interfere with. It appears to me we should not be deferring to authority but making a misuse of authority, which is to declare the law, if by reason of this, which appears to me a mere slip in the case of *Pennell* v. *Deffell* (1), and which, it must be recollected, was a very small portion of the contest in that case, we were to consider ourselves bound to decide against what is the settled principle. Therefore, in my opinion, the appeal must be allowed.

BAGGALLAY, L.J.:—

The circumstances under which this appeal is brought may be concisely stated as follows: on the morning of the 14th of November, 1877, there was a balance of £1796 5*s.* 2*d.* to the credit of Mr. *Hallett* on his banking account with Messrs. *Twining*, this balance was in no respect composed of trust moneys over which he had control, but had been entirely derived from his own resources. On that day he paid in to the credit of the account two sums, one of £770 10*s.* 5*d.* and the other of £1804 0*s.* 7*d.*, as to which I entirely concur in the opinion expressed by Mr. Justice *Fry*, that for the purposes of those proceedings they must be regarded as trust

(1) 4 D. M. & G. 372.

moneys. With reference to these two sums it is to be observed that, though both were paid in on the same day, the entry of the receipt of the £770 10*s.* 5*d.* preceded that of the £1804 0*s.* 7*d.* in the books of Messrs. *Twining* and also in Mr. *Hallett's* pass-book. The account was continued until the death of Mr. *Hallett* on the 2nd of February, 1878, during which period Mr. *Hallett* drew out and paid in further sums, all of which were in respect of his private affairs. The banking account did not contain on either side any entry in respect of trust moneys other than the two already mentioned as having been paid in on the 14th of November. The sums drawn out amounted in the aggregate to £2662 0*s.* 2*d.*, whilst those paid in amounted to £1320 19*s.* 1*d.* only, and the balance to the credit of the account on the day of Mr. *Hallett's* death was £3029 15*s.* 1*d.* It is further to be noted, and it is to my mind a material circumstance, that the balance to the credit of the account never fell below the aggregate of the two sums of trust moneys.

An action having been commenced for the administration of Mr. *Hallett's* estate, summonses were taken out by the trustees of his marriage settlement and by a lady named *Cotterill*, who were respectively interested in the two trust funds, the former claiming payment in full of the sum of £770 10*s.* 5*d.* out of the balance which at the time of Mr. *Hallett's* death was standing to the credit of his banking account, and the latter claiming payment, out of the same balance, of £1708 16*s.*, part of the before-mentioned sum of £1804 0*s.* 7*d.* The claim of the trustees was based upon this, that the drawings of Mr. *Hallett* ought to be appropriated to such portions of the balances from time to time standing to his credit as had arisen from his own moneys, as distinguished from those of which he was a trustee; if this claim is well founded an application of the same principle would have entitled Mrs. *Cotterill* to the full sum of £1804 0*s.* 7*d.*, and not to the portion of it only which she claimed; her claim, however, was based upon an application of the well-known rule in *Clayton's Case* (1) that the drawings out from a banking account should be appropriated in strict order of date to the payments in, a rule which, it was contended, had been extended to cases similar to that under consider-

(1) 1 Mer. 572.

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ation by the decisions of the Lords Justices in the case of *Pennell* v. *Deffell* (1), and in other cases which have followed it. If the rule was applicable to the present case, the aggregate amount of Mr. *Hallett's* drawings was sufficient, as will appear from the figures I have quoted, to exhaust not only the original balance of £1796 5*s.* 2*d.* which had arisen from Mr. *Hallett's* private moneys, but the whole of the sum of £770 10*s.* 5*d.* which consisted of trust moneys. Mr. Justice *Fry* considered himself bound by the decisions referred to and disallowed the claim of the trustees, but allowed that of Mrs. *Cotterill.* Thus of the two trust funds paid in on the same day the *cestui que trust* of the one would lose everything whilst the *cestui que trust* of the other one would lose to the extent only of a very small sum. Whilst, however, Mr. Justice *Fry* felt bound to follow these decisions, he distinctly intimated that, if he had been unfettered by authority, he would have been prepared to hold that, where a man has a balance to his credit at his banker's, consisting in part of funds which he may properly apply to his own purposes and in part of trust funds which he cannot lawfully so apply, his drawings for his own purposes ought to be attributed to his own funds and not to the trust funds. From this decision of Mr. Justice *Fry* the trustees of Mr. *Hallett's* settlement have appealed.

Now, inasmuch as my own views as to what ought to be done in respect of the claim of the trustees are, except so far as I may feel that they ought to be controlled by authority, entirely in accordance with those expressed by Mr. Justice *Fry*, I propose to examine somewhat in detail the case of *Pennell* v. *Deffell* with the view of ascertaining, first, what principles were enunciated by the Lords Justices in the course of their judgments in that case; secondly, how those principles were applied by them to the circumstances of that case; and, thirdly, having regard to the principles enunciated and to the decision arrived at, how far the case of *Pennell* v. *Deffell* is an authority binding upon us in our dealing with the case now under consideration.

Mr. *Green*, whose estate was in course of administration in *Pennell* v. *Deffell*, died on the 22nd of October, 1849; for some time previously to his death he had two banking accounts, one

(1) 4 D. M. & G. 372.

with the *Bank of England* and the other with the *London Joint Stock Bank;* at the time of his death there was a balance to his credit of £1988 11*s.* 8*d.* at the former, and of £2174 0*s.* 10*d.* at the latter. I shall have occasion later to examine these accounts more closely, as they varied considerably in the character of their details, but for the present it is sufficient to say that each of these accounts embraced moneys paid in and drawn out by *Green*, partly on account of the trust estates which he represented, and partly on his own private account. Inquiries as to the balances having been directed by the decree, the Master found that the whole of one balance and the greater part of the other belonged to the trust estates, but, upon exceptions to the Master's report, the Master of the Rolls held that the trust moneys could not be followed into either of the banking accounts, and directed that the whole of both balances should be treated as part of *Green's* general estate, and the substantial question involved in the appeal to the Lords Justices was whether the Master of the Rolls was right in holding that the trust moneys could not be followed into the banking accounts. Upon this question Lord Justice *Turner* in the course of his judgment expressed himself as follows (1): "It is, I apprehend, an undoubted principle of this Court that as between *cestui que trust* and trustee, and all parties claiming under the trustee otherwise than by purchase for valuable consideration without notice, all property belonging to a trust, however much it may be changed or altered in its nature or character, and all the fruit of such property, whether in its original or in its altered state, continues to be subject to or affected by the trust." And after illustrating this principle by a reference to the way in which the Court was in the habit of dealing with cases in which trust property had been invested in trade, the Lord Justice proceeded as follows: "But of course in those cases as in other cases the property which is the subject of the trust must in some manner be ascertained." He then refers to the judgment of the Master of the Rolls as having proceeded upon a supposed impossibility of ascertaining what portions of the balances belonged to the trusts, and what portions to *Green's* general estate, and answers, in the terms I am about to read, an inquiry suggested by himself,

(1) 4 D. M. & G. 388.

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whether there were not rules and principles for ascertaining what belonged to the trusts in such a case as that under consideration. "Suppose," said the Lord Justice, "a trustee pays into a bank moneys belonging to his trust to an account not marked or distinguished as a trust account and pays in no other moneys, could it for one moment be denied that the moneys standing to the account of the debt due from the bankers, arising from the moneys so paid in, would belong to the trust, and not to the private estate of the trustee? Then, suppose the trustee subsequently pays in moneys of his own not belonging to the trust to the same account, would the character of the moneys which he had before paid in—of the debt which had before accrued—be altered? Again, suppose the trustee, instead of subsequently paying moneys into the bank, draws out part of the trust moneys which he has before paid in, would the remainder of those moneys and of the debt contracted in respect of them lose their trust character? Then can the circumstance of the account consisting of a continued series of moneys paid in and drawn out alter the principle? It may, indeed, increase the difficulty of ascertaining what belongs to the trust, but I can see no possible ground on which it can affect the principle." And Lord Justice *Knight Bruce*, in the course of his judgment, after some previous suggestions leading up to that to which I am about to refer, put the case of a trustee placing in a particular repository, such as a chest, certain moneys held by him in trust, and also certain other moneys of his own, and of his so mixing and blending the two that the particular notes or coins of which each consisted could not be identified, and of his taking a sum of money from the repository after such mixing and blending and applying it to his own purposes, and in expressing his opinion as to the conclusion to be arrived at in such a case the Lord Justice used the following language (1): "I apprehend that, in Equity at least if not at Law also, what he so took would be solely or primarily ascribed to those contents of the repository, which were in every sense his own. He would in the absence of any evidence that he intended a wrong be deemed to have intended and done what was right, and if the act could not in that way be wholly justified, it would be deemed to have been just to the utmost amount possible,"

(1) 4 D. M. & G. 382.

The Lord Justice added, and no one will, I think, dissent from what he said, that the proposition which he had just stated was founded on principle and supported by authority. But is there any reason why, if the proposition is founded on principle, it should be limited to moneys placed in and taken out of a particular repository? Why should it not be applicable also to a case of moneys paid into and drawn out from a banking account kept in the sole name of the trustee? It is true that in *Sleech's Case* (1), which immediately preceded *Clayton's Case* (2), Sir *W. Grant* held that, as between the banker and the customer, the payment of a sum of money into a banking account created a debt, and was not a mere deposit, but, as between the customer who is a trustee and his *cestui que trust*, is there any reason why an honest intention should not, as far as possible, be attributed to him in the one case as well as in the other?

Let me illustrate my meaning. On a certain day I receive £10 of trust money in sovereigns, and place them in a drawer in my desk, the next day I receive £10 of my own moneys, also in sovereigns, and place them in the same drawer; on the third day I require £5 for my own private purposes, and I take out five sovereigns from the mixed fund in the drawer—an application of the principle embodied in the proposition of Lord Justice *Knight Bruce* would appropriate the five sovereigns taken out on the third day to the £10 of my own moneys placed in the drawer on the second day, and not to the £10 of trust money placed there on the first day. Again, I receive a cheque for £100 on a trust account, it will not be required for a few days, and it is too large a sum to be kept in my desk, I pay it into a bank, and on the following day receive £100 on my own private account, and not wanting it for a few days I pay it into the same account; I require £50 or £100 for my own purposes before the time arrives for requiring any money for trust purposes, and I accordingly draw against the mixed fund for the £50 or £100. Can any reason be assigned why in this latter case, as well as in the former, I should not, as between myself and my *cestui que trust*, have the honest intention attributed to me of drawing against my own private funds, and not against the trust fund, though it was the first paid in?

(1) 1 Mer. 539. (2) 1 Mer. 572.

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That Lord Justice *Knight Bruce* saw no distinction in principle between the two cases is, I think, clear from the next proposition, which he enunciated in the following terms: "When a trustee pays trust money into a bank to his credit, the account being a simple account with himself, not marked or distinguished in any other manner, the debt thus constituted from the bank to him is one which, as long as it remains due, belongs specifically to the trust as much and as effectually as the money so paid would have done had it specifically been placed by the trustee in a particular repository and so remained; that is to say, if the specific debt shall be claimed on behalf of the *cestui que trust*, it must be deemed specifically theirs as between the trustee, and his executors and the general creditors after his death, on the one hand, and the trust on the other;" and, after some observations not material to be now noted, the Lord Justice continued as follows: "This state of things would not, I apprehend, be varied by the circumstance of the bank holding also for the trustee, or owing also to him money in every sense his own."

The language of this latter sentence is, perhaps, somewhat vague. The previous sentence had reference to a trustee paying in trust moneys to a banking account; did the Lord Justice, when speaking of the bank holding also for the trustee money in every sense his own, refer to, or intend to include, private moneys of the trustee paid in by him to the same account? This appears to me to be the reasonable construction of the language used, and for the following reason: in the various steps by which the Lord Justice had arrived at his previous proposition he had taken, first, the case of trust money placed in a particular repository, then the addition to such trust moneys of the trustee's own moneys; thirdly, the abstraction from the mixed fund of moneys applied to his own purposes; and in advancing his second proposition, he first takes the case of trust moneys paid into a banking account, and insists upon their being regarded as if placed in a particular repository; and then follows the passage the effect of which I am now considering. The inference appears to me to be irresistible that the Lord Justice intended to adopt exactly the same steps in connection with a banking account as he had previously suggested with reference to moneys placed in a particular repository. If

the proposition as a whole is so read, it has the effect of extending to blended funds in a banking account the like rule or principle of attributing, where possible and as far as possible, an honest intention to a trustee drawing out money for his private purposes, as the Lord Justice had previously enunciated with reference to blended funds in a particular repository.

The principles thus enunciated by the Lords Justices (for the Lord Justice *Turner* expressed his full concurrence in the views expressed by Lord Justice *Knight Bruce*), taken and considered by themselves, amount to this: first, that trust moneys may be followed into a banking account; and, secondly, that in dealing with an account composed in part of trust and in part of private funds, an honest intention should, if and as far as possible, be attributed to a trustee; apart from the application of a third principle, also enunciated by the Lords Justices, and which I will consider presently, they would have fully justified the order which Mr. Justice *Fry* expressed himself ready to make, had he not felt himself fettered by authority.

The third principle was enunciated by the Lords Justices in the following terms. Lord Justice *Knight Bruce* said: "It may be, however, and, as I think is true, that cheques drawn by the trustee in a general manner upon the bank would for every purpose be ascribed to and affect the account in the mode explained and laid down by Sir *W. Grant* in *Clayton's Case* (1). The principles there stated would, I conceive, be applicable, notwithstanding the different nature and character of the sums forming together the balance due from the bank to the trustee, whatever the purposes and objects of the cheques." And Lord Justice *Turner* enunciated the same principle in the following terms (2): "We must see, however, whether the law does not furnish the means of meeting even the difficulty arising from such a continued series of moneys paid in and drawn out. I think that it does. I take it to be now well settled that moneys drawn out on a banking account are to be applied to the earlier items on the opposite side of the account. By every payment which he makes, the banker discharges so much of the debt which he first contracted. If that debt arose from trust moneys paid in by the customer, so much of

(1) 1 Mer. 572.

(2) 4 D. M. & G. 391.

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those trust moneys is paid off, and unless otherwise invested on account of the trust, falls into the customer's general estate and is lost to the trust, because it cannot be distinguished from the general estate of which it has become part. If, on the other hand, the earliest debt due from the bank arose from the customer's own moneys paid in by him, that debt is *pro tanto* discharged, and the trust moneys subsequently paid in remain unaffected. The same principle runs through the whole account. Each sum drawn out goes to discharge the earliest debt due from the banker which is remaining unpaid; and thus, when it is ascertained what moneys have been paid in belonging to the trust, it becomes clear to what portion of the balance which remains the trust estate is entitled."

In these clear and forcible terms the Lords Justices enunciated the proposition that, as a general principle, the rule in *Clayton's Case* (1) must be applied to the banking accounts of trustees for the purpose of determining the proportions in which the *cestuis que trust* and general creditors, or the several classes of their *cestuis que trust*, are entitled to the debt due from the bankers in closing the account. To the general principle so enunciated I readily accede. But was it more than the enunciation of a general principle; that is to say, a principle to be applied in the absence of special circumstances, but liable to be modified in its application by reason of the necessity or propriety of applying some other general principle of equal or paramount importance?

In *Clayton's Case* Sir *W. Grant* held that in dealing with an account between a banker and his customer, and in the absence of any evidence of contrary intention, the law would imply an appropriation in the order of their respective dates of the items drawn out to the items of debt constituted by the several payments of the customer; and he further held, that the respective liabilities of successive partnerships in the banking firm must be regulated by the results of taking the accounts in the manner he had previously indicated.

Now *Clayton's Case* was decided upon the principle that in the absence of any expressed intention to the contrary, or of special circumstances from which such an intention could be implied, the appropriation of drawings out to the payments in as adopted in

(1) 1 Mer. 572.

that case represented what must be presumed to have been the intention of the parties concerned; and so viewed the decision is quite consistent with the like presumption being rebutted or modified in another case in which the circumstances were such as to negative any intention to make such an appropriation of the drawings out to the payments in. That such presumption could be so rebutted was held in the cases of *Henniker* v. *Wigg* (1), decided by the Court of Queen's Bench before the decision in *Pennell* v. *Deffell* (2), and more recently in the case of the *City Discount Co.* v. *McLean* (3), in the Exchequer Chamber, in which latter case, however, no reference appears to have been made to *Pennell* v. *Deffell*. In *Clayton's Case* (4) there were no circumstances from which it could be inferred that, either as between the bankers and their customers, or as between the successive partnerships in the banking firm, the parties had any intention other than that presumably to be attributed to them of appropriating, in order of date, the drawings out to the payments in; but the adjustment of the liabilities of the several partnerships which was effected in that case by the application of the general principle enunciated by Sir *W. Grant*, might have been materially modified had there been any special contracts between the parties or any equities affecting them.

And so, also, in my opinion, the general principle enunciated by the Lords Justices in *Pennell* v. *Deffell* was based, or ought to be regarded as having been based, upon the like presumption as that acted upon by Sir *W. Grant* in *Clayton's Case;* and that such presumption was liable to be rebutted, or its effects modified, by any equities affecting Mr. *Greenwood*, and those claiming through him, unless there was sufficient reason to the contrary. The questions then arise, did any such equities exist in *Pennell* v. *Deffell?* and if so, was there any sufficient reason for not giving effect to them?

That an equity might have existed sufficient to very materially modify the application of the general rule that the drawings out should be appropriated in order of date to the payments in, I cannot doubt; that equity was the obligation so forcibly insisted

(1) 4 Q. B. 492.
(2) 4 D. M. & G. 372.
(3) Law Rep. 9 C. P. 692, 701.
(4) 1 Mer. 572.

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upon by Lord Justice *Knight Bruce*, of attributing to the trustee, when the circumstances would admit of it, an intention to act honestly. It is, however, equally clear that the Lords Justices did not modify the application of the general rule by reason of the existence of this equity: and upon this circumstance the Respondents have laid much stress, and in support of their contention they have relied upon the following passage in the judgment of Vice-Chancellor *Wood* in the case of *Merriman* v. *Ward* (1), in which, referring to *Pennell* v. *Deffell* (2), that learned Judge said: "The Lords Justices had to consider whether the doctrine of appropriation could be overruled by another principle, namely, that the assignee must be presumed, so far as possible, to have drawn against his own fund, because the opposite presumption would be a presumption of fraud. Nevertheless the Court held that the ordinary rule must apply of appropriating the earlier payments to the earlier debts."

If the Lords Justices had the question alluded to by the Vice-Chancellor present to their minds when they delivered their judgments in *Pennell* v. *Deffell*, and deliberately solved it in the manner mentioned by him, it is much to be regretted that they did not make some specific reference to it; but I can find no reason, assigned in the judgment of either Lord Justice, why the rule, which had been so elaborately laid down, of attributing honest motives to a trustee was treated as having no application when the order to be made upon the facts of the case came under consideration; the absence of any such assigned reason leads me to the conclusion that either the suggested question was neither solved nor discussed as one in controversy, or that some special circumstances existed which are not noticed in the report.

And the comparative unimportance to the parties concerned of having this question decided or discussed may perhaps explain the omission. I have already referred to the fact that *Green* had two banking accounts, upon each of which there was a considerable balance in his favour when it was closed. As regards the account with the *London Joint Stock Bank*, the two first items to his credit consisted entirely of his own moneys and amounted together to upwards of £800, whilst the aggregate of all the moneys drawn

(1) 1 J. & H. 371. (2) 4 D. M. & G. 372.

out by him, whether on trust account or on private account, fell short of £800, so that it was wholly immaterial as regarded the result whether the account was taken upon the principle of appropriating the sums drawn out to the earlier items paid in, or to that portion of the balance which was composed of his own private moneys; whichever principle was adopted the result would have been the same, viz., that the *cestui que trust* would recover the full amount of all the trust moneys paid in.

But as regards the account with the *Bank of England* the facts were somewhat different; that account had commenced with a balance entirely composed of trust moneys, from which, on the 4th of October, 1849, *Green* had drawn out for his private purposes several sums amounting together to £107. Had the account been then closed there would have been no blending of trust moneys with private funds; the sums drawn out would have been simply a misapplication of trust moneys to the extent of £107. On the following day, however, *Green* paid in to the credit of the account a sum of £72 16*s.* 3*d.* of his private moneys, and another sum of £442 12*s.* of trust moneys, and on the same day drew out £18 18*s.* for his private purposes and £49 17*s.* 10*d.* for trust purposes. The sum of £72 16*s.* 3*d.* was the only sum paid in by *Green* to the credit of this account in respect of his private moneys, but subsequently to the 5th of October he drew out and applied for his private purposes various sums which, being added to the £18 18*s.*, exceeded by a small sum the amount of £72 16*s.* 3*d.* paid in by him on the 5th.

By the decision of the Lords Justices, the drawings of *Green*, as well before as on and after the 5th of October, were appropriated to the part extinguishment of the original balance consisting entirely of trust moneys, and the general creditors were allowed out of the ultimate balance the full amount of the £72 16*s.* 3*d.* paid in by *Green* on the 5th of October. With this result, therefore, the rule in *Clayton's Case* (1) was acted upon in dealing with the balance at the *Bank of England*. Had it been argued on the part of the Appellants that the payment of the £72 16*s.* 3*d.* by *Green* on the 5th of October ought to be treated as a repayment *pro tanto* of the £107 improperly drawn out by him

(1) 1 Mer. 572.

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on the 4th, before any blended account existed, the contention could hardly have been deemed unreasonable; no such contention however, appears to have been raised.

But the difference between the result of the system of appropriation adopted by the Lords Justices and what would have been the result if, on both accounts, the moneys drawn out by *Green* had been set off against the moneys paid in from his private resources, is very trifling. Had the latter system been adopted, the Appellants would have been entitled to £4077 5*s.* 4*d.*, whilst under the order of the Lords Justices they took £4011 13*s.* 5*d.*, a difference of £65 only. They had succeeded in reversing the decision of the Master of the Rolls who had deprived them of everything, and, as before observed, the substantial question argued was not, whether the Respondents were entitled to the £72 16*s.* 3*d.*, but whether the Appellants were entitled to anything. It is not an improbable view of the case that at the close of a judgment which had given them within a fraction all that they had claimed, the Appellants should have abstained from questioning a portion of that judgment with the view of obtaining an allowance of the additional fraction. And this view of the case appears to be borne out by the fact that, although judgment was reserved, it was eventually given without hearing a reply from the Appellants, which would hardly have been the case if the Appellants had objected to the allowance of the £72 16*s.* 3*d.* to the Respondent; and it may fairly be inferred, as well from the opening words of Lord Justice *Knight Bruce*, who offered to the counsel for the Appellants a right of reply after judgment, if they thought fit to claim it, as from the concluding words of Lord Justice *Turner*, that a claim on behalf of the Appellants for something more than was given them was at least arguable. Lord Justice *Turner's* observation was, that he had no doubt Lord *Eldon* would have gone at least as far as the Lords Justices were then going, and that his only doubt was, whether he would not have gone further. Upon what was the doubt based? Upon what could it have been based? The Lords Justices could only have gone further than they did go by depriving the Respondents of the £72 16*s.* 3*d.*, and giving it to the Appellants.

But, dealing with the decision of the Lords Justices in *Pennell*

v. *Deffell* (1), as I find it reported, I cannot regard it as satisfactory, if it is to be considered as establishing as a general proposition that in all such cases as that then under their consideration the presumption of an honest intention on the part of the trustee is to be altogether disregarded, however favourable to such a presumption the circumstances of any particular case may be, and that the rule of appropriating in strict order of date the drawings out to the payments in is alone to be applied. On the contrary, I entertain a very decided opinion that in cases like *Pennell* v. *Deffell*, or in such as that which is the subject of the present appeal, full effect should be given to the principle of attributing the honest intention whenever the circumstances of the case admit of such a presumption. It may, of course, happen that, through the acts of a trustee, whether wilfully dishonest or not, the ultimate balance may not be sufficient to meet the full amounts of all the trust moneys which may have been paid into a blended banking account, and the question then raised may be as to the various claims in respect of distinct trusts; in such a case the strict application of the general rule of appropriating in order of date the drawings out to the payments in may, and probably would, be correct. But in a case of another class, in which, as in that under consideration, the trustee has paid in trust moneys to the credit of his private account, and in his subsequent dealings with that account for his private purposes has never reduced his balance below the amount of the trust moneys so paid in, it is, to my mind, difficult to attribute to the trustee any other intention than that of appropriating his drawings to his own private moneys, so as to leave the trust moneys intact. If it is ever proper to follow trust moneys into a banking account in the interests of the *cestuis que trust*, I am unable to suggest a case more proper than that which we are now considering for the application of the principle that an honest intention should be attributed to the trustee. Now, if it can properly be considered that the decision in *Pennell* v. *Deffell* proceeded upon the special circumstances of that case, it is, of course, not an authority by which this Court is bound in dealing with the present appeal; but, however strong may be the impression upon my own mind, and it is very strong, that all the

(1) 4 D. M. & G. 372.

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circumstances of that case necessary for rightly appreciating it are not to be found in the report, I cannot ignore the fact that for nearly thirty years it has been recognised as an authority in no way depending on special circumstances, but as establishing a general principle applicable to all cases of a similar character. In the case of *Brown* v. *Adams* (1), to which our attention has been directed in argument, Lord Justice *Giffard* not only held himself bound by the authority of *Pennell* v. *Deffell* (2), but stated that he should have arrived at the same conclusion in the case before him even if not bound by that authority. With reference, however, to the case of *Brown* v. *Adams*, it is to be observed that Lord Justice (then Vice-Chancellor) *James*, from whose decision the appeal was brought, had arrived at a different conclusion. The question, then, remains whether *Pennell* v. *Deffell* is an authority so binding upon this Court that, however decided may be the collective or individual opinions of its members as to what, in the absence of authority, should be done in the matter of this appeal, we are bound to disregard them, and to shape our decision in accordance with what was decided in that case. My answer to that question must be in the negative. I fully recognise and appreciate the evils which in many cases would arise if the Judges of the Court of Appeal, or, indeed, if any other Court or Judge, were to act upon their individual views, regardless of what is generally understood by the expression "authority." Repeated decisions have established rules for determining the construction of particular words when used in wills, and other wills have been prepared and executed upon the faith of such words receiving the like construction. Titles have been acquired and lands dealt with upon the footing of the law being as enunciated in the judgments pronounced in other cases. And so, again, in matters of commercial business, contracts have been entered into upon the faith of certain rules, originating in the decisions of the Courts, being recognised as conclusive. Now, in such cases as these, and in others which will readily suggest themselves, the greatest injustice might be occasioned by a Court or a Judge treating such decisions as having been erroneously arrived at, and thereby creating doubt and uncertainty as to a rule of law which had previously been

(1) Law Rep. 4 Ch. 764. (2) 4 D. M. & G. 372.

treated as well and clearly defined. But no such injustice could arise in consequence of our dissenting from the decision in *Pennell* v. *Deffell* (1), and giving effect to such dissent. It can hardly be suggested that since that decision any trustee has kept and dealt with a blended banking account upon the faith that, as between his general creditors and his *cestuis que trust*, the rule adopted in that case would also be adopted after his death in dealing with his ultimate balance. If a trustee had acted upon any such view, he could hardly be considered as having had an honest intention. If, however, the actual decision in *Pennell* v. *Deffell* had been a logical consequence of an application of the principles enunciated by the Lords Justices, I should certainly have felt myself bound to follow it; but, having to decide between the general principles enunciated in that well-known case in which, as understood by me, I entirely concur, and the decision arrived at in the same case, and apparently upon an intended application of the same principles, but which would give to those principles a construction and an effect in which I cannot concur, I feel myself bound to adopt and give effect to the general principles, and to treat myself as unfettered by the actual decision. For these reasons I agree with the Master of the Rolls in thinking that the appeal should be allowed.

THESIGER, L.J.:—

I feel myself bound by authority to affirm the judgment of Mr. Justice *Fry*. Upon principle there is great strength in the argument for the Appellants. If specific coins, the proceeds of trust property, are deposited by a trustee in a box, either in his own custody or in that of another person, and in that box are mixed confusedly with coins, in every sense the property of the trustee, and being so mixed are subjected to dealings analogous to the drawings out and payings in of moneys standing in a banker's account, the trust is impressed upon the coins remaining in the box to the full amount of the proceeds of the trust property, if it be that at no time the mixed fund has been reduced below that amount, or if the mixed fund has at any time been reduced below that amount, then to any lesser amount below which it can be shewn that the mixed fund has never been reduced. So much is

(1) 4 D. M. & G. 372.

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admitted by Lord Justice *Knight Bruce* in *Pennell* v. *Deffell* (1). But in that case, and in other cases, it has been held that the proceeds of that trust property may be traced, followed, and claimed by the trust creditor when, instead of their being placed in a box or other special repository, they are paid to a banker to be placed by him to the credit of the trustee's private account, and are so placed subject to the qualification at least that upon an appropriation of payment in accordance with the rule laid down in *Clayton's Case*, (2) it appears that the money claimed has not been drawn out. It has been argued that the qualification cannot be supported, and that when once it is admitted that money may be followed into a banker's account equally with money placed in a special repository, the money so followed must be subject to the same conditions and be recoverable under the same circumstances in the one case as in the other. True it is that in the case of money paid into the banker's account it is converted into a debt, while in the case of money placed in a special repository it remains in specie; but it may be said with reason that this distinction would rather afford a ground for not following the money into the banker's account at all, than a ground, when it is held that it may be followed, for not carrying out to their logical consequences considerations drawn from the analogy of the money placed in the special repository; and it is no doubt difficult to see why the rule as to appropriation of payments, which is a rule which embodies a presumption of fact rather than of law, and is founded upon the notion that in the absence of any expression of intention an appropriation of drawings out and payings in of moneys upon a banker's account in order of date would in most cases meet the intentions of the parties, should not bend before the fact that in the particular case such an appropriation would involve a breach of trust, if not a distinct fraud. That the rule is what I have stated it to be is shewn by the cases of *Henniker* v. *Wigg* (3) and the *City Discount Company* v. *McLean* (4), and those cases are good illustrations of the character of circumstances which would be sufficient to prevent the application of the rule. A bond in one case, a guarantee in the other, given by third parties, and covering a portion of the

(1) 4 D. M. & G. 381.
(2) 1 Mer. 572.
(3) 4 Q. B. 492.
(4) Law Rep. 9 C. P. 692.

customer's account with his bankers, was held to rebut the presumption that the balance covered by the security had been paid.

In each of these cases the presumption, if it had been acted upon, would have put an end to a civil remedy which from the facts of the case it was manifest was intended by all parties to be kept active. In the present case, and in cases of a similar kind, if the presumption is acted upon it would not only result in trust property, the proceeds of which are traced to the banking account, being lost to its proper owners, but would entail the further consequence of the customer being presumed to have committed a fraud, and this by an arbitrary rule not founded upon any equitable considerations (for general creditors have no equity as against the equity of a *cestui que trust* to trace and follow into a banking account the moneys arising from the sale of the trust property: *Frith* v. *Cartland* (1) ), but established for the purpose of dealing with general accounts in the absence of special indications by the parties of their intentions.

The presumption of a man's innocence of crime may reasonably be set off against the presumption that he intended such an appropriation of payments upon his banking account as could only exist if he intended to commit a crime; and to the argument adduced by Mr. *Hallett's* representatives in the present case that the facts proved indicate that he did in fact intend to misappropriate, and had misappropriated, the trust property, the answer might be given, as it might have been given to Mr. *Hallett* himself if he had been alive to use the argument, "*Allegans suam turpitudinem non est audiendus.*" Giving, however, full effect to this reasoning, which, be it observed, is reasoning that is not difficult for even an uncultivated mind to follow, it remains to be seen how eminent Judges have dealt with the matter.

*Clayton's Case* (2) is capable of being, and has been, distinguished from the present. It with other similar cases shews, according to Mr. Justice *Blackburn*, in *City Discount Company* v. *McLean* (3), "that when a partner dies, and there is a change of the partnership, and the transactions with the new and old firms are all mixed up together in one account, the law treats the whole

(1) 2 H. & M. 417.
(2) 1 Mer. 608.
(3) Law Rep. 9 C. P. 701.

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as one entire account, and it applies the items of credit to those of debit according to date in favour of the estate of the deceased partner." The decision of Sir *W. Grant* so explained is quite consistent with the general rule clearly laid down in the Common Law cases, that accounts rendered are only evidence of the appropriation of payments to the earlier items, which may be rebutted by evidence to the contrary. The two cases already cited of *Henniker* v. *Wigg* (1) and *City Discount Company* v. *McLean* (2) affirmed, as already pointed out, that general rule, and although they contained special features which might distinguish them to some extent from the present case, their *ratio decidendi* was wide enough to apply to the case of a person following his trust property into a banking account, and claiming to have that account adjusted so as to preserve his rights. Still it must be borne in mind that in these Common Law cases the inference arising upon the facts was that banker, customer, and third party all actually intended that the payments in and out of the account should not be taken in order of date, while here, bankers and third party could have had no intention in the matter, for they were ignorant of the fact that the trust funds had got into the account, and the intention of the customer is only derived from a presumption of law contrary to the probable facts of the case. This being so, we have in the case of *Pennell* v. *Deffell* (3), and in a Court of co-ordinate jurisdiction with this Court, or rather in a Court, to the functions of which, among other functions, this Court has succeeded, a decision by which, not only the principles applicable to a case like the present, were considered and laid down, but in which the very point raised upon this appeal was discussed and decided. The steps which, as pointed out at the commencement of my judgment, seem to lead to the conclusion, as a matter of logical argument, in favour of the Appellant's contention, were the steps taken by Lord Justice *Knight Bruce* in *Pennell* v. *Deffell*, and which led him to an exactly opposite conclusion, arrived at also by his colleague, Lord Justice *Turner*. Their judgment was given in 1853. In 1860, Vice-Chancellor *Wood*, in the case of *Merriman* v. *Ward* (4), following, as he was no doubt bound to do, that judgment, epito-

(1) 4 Q. B. 492.
(2) Law Rep. 9 C. P. 692.
(3) 4 D. M. & G. 372.
(4) 1 J. & H. 377.

mised it in these terms: "The Lords Justices had to consider whether the doctrine of appropriation could be over-ruled by another principle, namely, that the assignee must be presumed, so far as possible, to have drawn against his own fund, because the opposite presumption would be a presumption of fraud. Nevertheless, the Court held that the ordinary rule must apply of appropriating the earlier payments to the earlier debts." The effect of *Pennell* v. *Deffell* (1) could not be put in terms more clear, or more distinctly negativing the argument as regards the presumption of fraud which I have used. In *Frith* v. *Cartland* (2) again, the same learned Vice-Chancellor, while distinguishing the case before him from that of *Pennell* v. *Deffell*, said of the latter that in it part of the trust fund had been paid into a bank, but it was not ear-marked, and was wiped out by subsequent drawings, and the whole ultimate balance could not be fixed with the trust any more than a second £1000 of stock which a trustee might happen to acquire after selling £1000 of trust stock and spending the proceeds. In the year 1869 the point arose before Lord Justice *Giffard* in *Brown* v. *Adams* (3) in the same simple form in which it has been discussed before us, for the only question the Lord Justice had to decide was whether in a banker's account the appropriation of payments according to the rule in *Clayton's Case* (4) was to take place, so as to wipe off an item of £5000, which was admittedly trust moneys, and the case came before the Lord Justice under circumstances favourable to the reconsideration of the decision upon the point in *Pennell* v. *Deffell*, for the present Lord Justice, then Vice-Chancellor *James*, had granted an interlocutory injunction in favour of the trust creditor. But Lord Justice *Giffard* dissolved the injunction, not merely saying that he considered himself bound by the authority of *Pennell* v. *Deffell*, but adding that, even without that authority, he should have had no doubt in the case before him. Again, in *Ex parte Cooke* (5), decided in 1876, Lord Justice *Bramwell*, one of the Judges who took part in the decision in 1874 of the case of the *City Discount Company* v. *McLean* (6), is reported to have said in refer-

(1) 4 D. M. & G. 372.
(2) 2 H. & M. 417.
(3) Law Rep. 4 Ch. 764.
(4) 1 Mer. 572.
(5) 4 Ch. D. 123.
(6) Law Rep. 9 C. P. 692.

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ence to the point under consideration (1), "If the whole of the money had remained in the hands of the bankers without being drawn out, I think it clear that the *cestui que trust* could have claimed it as trust money traced into their hands, and if on properly attributing the payments any part of it is found to remain there the same rule must apply to what so remains." In that case the matter was referred to the Registrar, and we are informed by Mr. *De Gex*, who was engaged as counsel in the case, that upon the Registrar appropriating the payments in accordance with those observations, and upon an appeal from the Registrar to this Court, the case of *Pennell* v. *Deffell* (2) was treated as binding authority, and the appeal was dismissed.

I have purposely refrained from citing, as authority in the same direction, the case of *Lord Chedworth* v. *Edwards* (3), before Lord *Eldon*, as Chancellor, in 1802, because there may possibly be a doubt as to what he meant when he spoke of it being too much to infer that money at the bankers was the same money unconverted which had been paid in two years before, and the point does not appear to have been particularly argued before him. Putting aside, however, that case, the matter, as regards authority, stands thus: For a period of twenty-one years the judgment in *Pennell* v. *Deffell* stood unchallenged, and was followed as laying down a correct rule, and even when at the end of that period the case of the *City Discount Company* v. *McLean* (4) was decided, it was decided without reference to *Pennell* v. *Deffell*. As regards this last observation, it may be pointed out that the Lords Justices decided *Pennell* v. *Deffell* without reference to the previous case of *Henniker* v. *Wigg* (5); and it may be said that they had proceeded upon a misapprehension of the principle of Common Law applicable to the appropriation of payments in a banking or any other account. This may possibly be so, and if it was so, I am inclined to think that the misapprehension was shared by Sir *William Grant*, in laying down the rule in *Clayton's Case* (6), and although his decision may be distinguished, as it has been distinguished in the Common Law cases already cited, I cannot but think that the terms in

(1) 4 Ch. D. 127.
(2) 4 D. M. & G. 372.
(3) 8 Ves. 46.
(4) Law Rep. 9 C. P. 692.
(5) 4 Q. B. 492.
(6) 1 Mer. 572.

which he laid down the rule were intended by him to go beyond the limits of the particular case before him, and were wide enough, as they were assumed by the Lords Justices *Knight Bruce* and *Turner* to be, to cover the later case of *Pennell* v. *Deffell* (1). The character of the banking account where, to use the words of Sir *William Grant* himself, "all the sums paid in form one blended fund, the parts of which have no longer any distinct existence," was the keynote of his decision, and would have been scarcely necessary to be dwelt upon so prominently if any equity of the retired or deceased partner had been sufficient in itself to call for an appropriation of payments at least not contrary to any rule of law.

In this state of the authorities, I cannot feel myself justified in acceding to the Appellants' contention, and thereby taking upon myself to overrule judgments by which I think that in this Court we ought to consider ourselves bound. I fully realize that in overruling those judgments no injustice or inconvenience would be worked such as would arise in cases where, upon the faith and footing of a particular rule of law having been correctly laid down, business affairs have been for some time conducted, the practice of conveyancers has been regulated, or titles to property of any kind have been acquired. But that consideration appears to me to be one proper to influence the mind of a superior tribunal asked to overrule the judgment of inferior tribunals, although of long standing and often followed, rather than to afford a ground for this or any other Court disregarding such judgments when given by and followed in tribunals of co-ordinate jurisdiction. In other words, it constitutes a reason for holding that a decision in a particular Court has not so passed into and become part of the common and recognised law of the land as to prevent any Court overruling it, rather than for holding that it is not a binding decision upon all Courts of co-ordinate jurisdiction. It is said, further, that the point for our decision formed so insignificant a part of the judgment of the Lords Justices in *Pennell* v. *Deffell*, and may, perhaps, have been, or even probably was, so little dwelt upon in the argument before them, especially as no reply was heard by them, that their decision upon it is entitled to less weight than might other-

(1) 4 D. M. & G. 372.

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wise have been given to it. The fact is manifest that the sum which was affected by the particular decision was a mere nothing compared with the amount of which the then Master of the Rolls' judgment had deprived the Appellants, upon the ground that the trust moneys could not be traced and followed into the banker's account at all, and which amount the Lords Justices held was recoverable by the trust creditor. Granting, however, this fact, it is still equally manifest that the Lords Justices did not overlook the minor point, or, indeed, treat it as a minor point. Their judgments contain on the face of them signs from which one cannot but collect that the point was carefully considered by them. It is lastly said that the principles they themselves laid down in their judgment so clearly demonstrate the erroneousness of their conclusion upon the particular point in question, that it is just one of those cases in which no Court ought to be bound by such a conclusion. But here, again, however desirable it may be, as suggested in argument, that a Judge should have the courage of his convictions, it is equally desirable that he should have respect for those of other Judges, and I should attribute to myself another quality than that of courage if I were to hold that a conclusion which appeared a rational one to no less eminent Judges than the late Lords Justices *Knight Bruce* and *Turner*, the present Lord *Hatherley*, and the late Lord Justice *Giffard*, and which did not appear open to review to the learned Judges before whom upon the second occasion the case of *Ex parte Cooke* (1) came to be discussed, was necessarily illogical and absurd. Equity has gone very far in aid of trust creditors when it holds that they may follow and obtain, in priority to general creditors, moneys paid to a banker, and therefore no longer existing in specie, as moneys numbered and ear-marked, but converted into a debt; and it may be that the distinguished Judges I have referred to may have thought that Equity had gone far enough, and that, in the absence of express appropriation, the general rule of appropriation of payments in and out of a banker's account should apply to that debt when forming part of a larger debt made up as to the rest of moneys, not trust moneys, paid into the bank. However this may be, and notwithstanding the hesitation which I naturally feel in differing upon

(1) 4 Ch. D. 123.

the question of the binding effect of the authorities from the other members of the Court, I must express my opinion that the law laid down in *Pennell* v. *Deffell* (1) is binding upon this Court, and that the appeal ought, therefore, to be dismissed.

Appeal allowed.

Solicitor for Plaintiff: *H. A. Dowse.*
Solicitors for Mrs. *Cotterill*: *Fladgate & Co.*
Solicitors for *Hallett's* Trustees: *Fairfoot & Webb.*
Solicitors for other parties: *Humphreys & Son; F. Howse.*

(1) 4 D. M. & G. 372.

2009 NSSC 136
Nova Scotia Supreme Court

ScoZinc Ltd., Re

2009 CarswellNS 229, 2009 NSSC 136, 177 A.C.W.S. (3d) 293, 277 N.S.R. (2d) 251, 53 C.B.R. (5th) 96, 882 A.P.R. 251

# 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 Compromise or Arrangement of ScoZinc Ltd. (Applicant)

D.R. Beveridge J.

Heard: April 3, 2009
Judgment: April 3, 2009
Written reasons: April 28, 2009
Docket: Hfx. 305549

Counsel: John G. Stringer, Q.C., Mr. Ben R. Durnford for Applicant
Robert MacKeigan, Q.C. for Grant Thornton

Subject: Insolvency
**Related Abridgment Classifications**
Bankruptcy and insolvency
XIX Companies' Creditors Arrangement Act
XIX.2 Initial application
XIX.2.g Monitor
**Headnote**
Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Miscellaneous issues
Company was granted protection pursuant to s. 11 of Companies' Creditors Arrangement Act ("CCAA") — Monitor was appointed pursuant to s. 11.7 of CCAA — Determination of creditors' claims was set by claims procedure order ("order") — Three creditors submitted proofs of claim by claims bar date set out in order and then submitted revised proofs of claim after claims bar date, but before date set for monitor to complete assessment of claims — Monitor determined errors in proofs of claims were due to inadvertence and issued notice of revision or disallowance, allowing claims as revised if it was determined monitor had power to do so — Monitor brought motion for directions on whether it had authority to allow revision of claim by increasing it after claim's bar date but before date set for monitor to complete assessment of claims — Monitor had necessary authority — Court creates claims process by court order — Determination that claims had to initially be identified and assessed by monitor, and heard first by claims officer, was valid exercise of court's inherent jurisdiction — Logical and practical that monitor, as officer of court, be directed to fulfil analogous role to that of trustee under Bankruptcy and Insolvency Act, and order accomplished this — Provision in order mandated monitor to review all proofs of claim filed on or before claims bar date and accept, revise or disallow them — While normally monitor's revision would be to reduce proof of claim, nothing in order so restricted monitor's authority — It did not matter that revised claims were submitted after claims bar date — In essence, monitor simply acted to revise proofs of claim already submitted to conform with evidence elicited by monitor or submitted to it.
**Table of Authorities**
**Cases considered by *D.R. Beveridge J.*:**
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*Blue Range Resource Corp., Re* (2000), 2000 CarswellAlta 30, (sub nom. *Blue Range Resources Corp., Re)* 250 A.R. 239, (sub nom. *Blue Range Resources Corp., Re)* 213 W.A.C. 239, 15 C.B.R. (4th) 192, 2000 ABCA 16 (Alta. C.A. [In Chambers]) — referred to

*Blue Range Resource Corp., Re* (2000), 2000 ABCA 285, 2000 CarswellAlta 1145, [2001] 2 W.W.R. 477, (sub nom. *Enron Canada Corp. v. National-Oilwell Canada Ltd.)* 193 D.L.R. (4th) 314, 271 A.R. 138, 234 W.A.C. 138, 87 Alta. L.R. (3d) 352 (Alta. C.A.) — followed

*Carlen Transport Inc. v. Juniper Lumber Co. (Monitor of)* (2001), 21 C.B.R. (4th) 222, (sub nom. *Juniper Lumber Co., Re)* 233 N.B.R. (2d) 111, (sub nom. *Juniper Lumber Co., Re)* 601 A.P.R. 111, 2001 CarswellNB 21 (N.B. Q.B.) — referred to

*Federal Gypsum Co., Re* (2007), 2007 NSSC 384, 2007 CarswellNS 630, 261 N.S.R. (2d) 314, 835 A.P.R. 314, 40 C.B.R. (5th) 39 (N.S. S.C.) — referred to

*Freeman, Re* (1922), 55 N.S.R. 545, [1923] 1 D.L.R. 378, 1922 CarswellNS 57 (N.S. C.A.) — considered

*Laidlaw Inc., Re* (2002), 2002 CarswellOnt 790, 34 C.B.R. (4th) 72 (Ont. S.C.J. [Commercial List]) — referred to

*Muscletech Research & Development Inc., Re* (2006), 25 C.B.R. (5th) 231, 2006 CarswellOnt 6230 (Ont. S.C.J.) — referred to

*Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 17 C.B.R. (3d) 1, (sub nom. *Olympia & York Developments Ltd., Re)* 12 O.R. (3d) 500, 1993 CarswellOnt 182 (Ont. Gen. Div.) — referred to

*Pine Valley Mining Corp., Re* (2008), 2008 CarswellBC 579, 2008 BCSC 356, 41 C.B.R. (5th) 43 (B.C. S.C.) — referred to

*Siscoe & Savoie v. Royal Bank* (1994), 1994 CarswellNB 14, 29 C.B.R. (3d) 1, 157 N.B.R. (2d) 42, 404 A.P.R. 42 (N.B. C.A.) — considered

*Skeena Cellulose Inc., Re* (2003), 2003 CarswellBC 1399, 2003 BCCA 344, 184 B.C.A.C. 54, 302 W.A.C. 54, 43 C.B.R. (4th) 187, 13 B.C.L.R. (4th) 236 (B.C. C.A.) — considered

*Stelco Inc., Re* (2005), 253 D.L.R. (4th) 109, 75 O.R. (3d) 5, 2 B.L.R. (4th) 238, 9 C.B.R. (5th) 135, 2005 CarswellOnt 1188, 196 O.A.C. 142 (Ont. C.A.) — considered

*Triton Tubular Components Corp., Re* (2005), 2005 CarswellOnt 4439, 14 C.B.R. (5th) 264 (Ont. S.C.J.) — referred to

**Statutes considered:**

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

Generally — referred to

s. 135(2) — referred to

*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36

Generally — referred to

s. 4 — considered

s. 5 — considered

s. 6 — considered

s. 11 — pursuant to

s. 11.7 [en. 1997, c. 12, s. 124] — considered

s. 11.7(1) [en. 1997, c. 12, s. 124] — considered

s. 11.7(2) [en. 1997, c. 12, s. 124] — considered

s. 11.7(3) [en. 1997, c. 12, s. 124] — considered

s. 11.7(3)(d) [en. 1997, c. 12, s. 124] — considered

s. 12 — considered

s. 12(1) "claim" — considered

  

s. 12(2) — considered
*Probate Act*, R.S.N.S. 1900, c. 158
Generally — referred to

MOTION by monitor appointed under *Companies' Creditors Arrangement Act* for directions on whether it had authority to allow revision of claim after claim's bar date but before date set for monitor to complete its assessment of claims.

***D.R. Beveridge J.*** **(orally):**

1 On December 22, 2008 ScoZinc Ltd. was granted protection by way of a stay of proceedings of all claims against it pursuant to s.11 of the *Companies' Creditors Arrangement Act* R.S.C. 1985, c. C-36. The stay has been extended from time to time. Grant Thornton was appointed as the Monitor of the business and financial affairs of ScoZinc pursuant to s.11.7 of the *CCAA*.

2 The determination of creditors' claims was set by a Claims Procedure Order. This order set dates for the submission of claims to the Monitor, and for the Monitor to assess the claims. The Monitor brought a motion seeking directions from the court on whether it has the necessary authority to allow a revision of a claim after the claim's bar date but before the date set for the Monitor to complete its assessment of claims.

3 The motion was heard on April 3, 2009. At the conclusion of the hearing of the motion I concluded that the Monitor did have the necessary authority. I granted the requested order with reasons to follow. These are my reasons.

**Background**

4 The procedure for the identification and quantification of claims was established pursuant to my order of February 18, 2009. Any persons asserting a claim was to deliver to the Monitor a Proof of Claim by 5:00 p.m. on March 16, 2009, including a statement of account setting out the full details of the claim. Any claimant that did not deliver a Proof of Claim by the claims bar date, subject to the Monitor's agreement or as the court may otherwise order, would have its claim forever extinguished and barred from making any claim against ScoZinc.

5 The Monitor was directed to review all Proofs of Claim filed on or before March 16, 2009 and to accept, revise or disallow the claims. Any revision or disallowance was to be communicated by Notice of Revision or Disallowance, no later than March 27, 2009. If a creditor disagreed with the assessment of the Monitor, it could dispute the assessment before a Claims Officer and ultimately to a judge of the Supreme Court.

6 The three claims that have triggered the Monitor's motion for directions were submitted by Acadian Mining Corporation, Royal Roads Corp., and Komatsu International (Canada) Inc.

7 ScoZinc is 100% owned by Acadian Mining Corp. Theso two corporations share office space, managerial staff, and have common officers and directors. Acadian Mining is a substantial shareholder in Royal Roads and also have some common officers and directors.

8 Originally Royal Roads asserted a claim as a secured creditor on the basis of a first charge security held by it on ScoZinc's assets for a loan in the amount of approximately $2.3 million. Acadian Mining also claimed to be a secured creditor due to a second charge on ScoZinc's assets securing approximately $23.5 million of debt. Both Royal Roads and Acadian Mining have released their security. Each company submitted Proofs of Claim dated March 4, 2009 as unsecured creditors.

9 Royal Roads claim was for $579, 964.62. The claim by Acadian Mining was for $23,761.270.20. John Rawding, Financial Officer for Acadian Mining and ScoZinc, prepared the Proofs of Claim for both Royal Roads and Acadian Mining. It appears from the affidavit and materials submitted, and the Monitor's fifth report dated March 31, 2009 that there were errors in each of the Proofs of Claim.

  

10 Mr. Rawding incorrectly attributed $1,720,035.38 as debt by Acadian Mining to Royal Roads when it should have been debt owed by ScoZinc to Royal Roads. In addition, during year end audit procedures for Royal Roads, Acadian Mining and ScoZinc, other erroneous entries were discovered. The total claim that should have been advanced by Royal Roads was $2,772,734.19.

11 The appropriate claim that should have been submitted by Acadian Mining was $22,041,234.82, a reduction of $1,720,035.38. Both Royal Roads and Acadian Mining submitted revised Proofs of Claim on March 25, 2009 with supporting documentation.

12 The third claim is by Komatsu. Its initial Proof of Claim was dated March 16, 2009 for both secured and unsecured claims of $4,245,663.78. The initial claim did not include a secured claim for the equipment that had been returned to Komatsu, nor include a claim for equipment that was still being used by ScoZinc. A revised Proof of Claim was filed by Komatsu on March 26, 2009.

13 The Monitor, sets out in its fifth report dated March 31, 2009, that after reviewing the relevant books and records, the errors in the Proofs of Claim by Royal Roads, Acadian Mining and Komatsu were due to inadvertence. For all of these claims it issued a Notice of Revision or Disallowance on March 27, 2009, allowing the claims as revised "if it is determined by the court that the Monitor has the power to do so".

14 The request for directions and the circumstances pose the following issue:

**Issue**

15 Does the Monitor have the authority to allow the revision of a claim by increasing it based on evidence submitted by a claimant within the time period set for the monitor to carry out its assessment of claims?

**Analysis**

16 The jurisdiction of the Monitor stems from the jurisdiction of the court granted to it by the *CCAA*. Whenever an order is made under s.11 of the *CCAA* the court is required to appoint a monitor. Section 11.7 of the *CCAA* provides:

> 11.7(1) When an order is made in respect of a company by the court under section 11, the court shall at the same time appoint a person, in this section and in section 11.8 referred to as "the monitor", to monitor the business and financial affairs of the company while the order remains in effect.
>
> (2) Except as may be otherwise directed by the court, the auditor of the company may be appointed as the monitor.
>
> (3) The monitor shall
>
> > (a) for the purposes of monitoring the company's business and financial affairs, have access to and examine the company's property, including the premises, books, records, data, including data in electronic form, and other financial documents of the company to the extent necessary to adequately assess the company's business and financial affairs;
> >
> > (b) file a report with the court on the state of the company's business and financial affairs, containing prescribed information,
> >
> > > (i) forthwith after ascertaining any material adverse change in the company's projected cash-flow or financial circumstances,
> > >
> > > (ii) at least seven days before any meeting of creditors under section 4 or 5, or
> > >
> > > (iii) at such other times as the court may order;

  

(c) advise the creditors of the filing of the report referred to in paragraph (b) in any notice of a meeting of creditors referred to in section 4 or 5; and

(d) carry out such other functions in relation to the company as the court may direct.

...

17 It appears that the purpose of the *CCAA* is to grant to an insolvent company protection from its creditors in order to permit it a reasonable opportunity to restructure its affairs in order to reach a compromise or arrangement between the company and its creditors. The court has the power to order a meeting of the creditors or class of creditors for them to consider a compromise or arrangement proposed by the debtor company ( s. 4, 5 ). Where a majority of the creditors representing two thirds value of the creditors or class of creditors agree to a compromise or arrangement, the court may sanction it and thereafter such compromise or arrangement is binding on all creditors, or class of creditors (s. 6).

18 Section 12 of the *Act* defines a claim to mean "any indebtedness, liability or obligation of any kind that, if unsecured, would be a debt provable in bankruptcy within the meaning of the *Bankruptcy and Insolvency Act*." However, as noted by McElcheran in *Commercial Insolvency in Canada* (LexisNexis Canada Inc., Markham, Ontario, 2005 at p. 279-80) the *CCAA* does not set out a process for identification or determination of claims; instead, the Court creates a claims process by court order.

19 The only guidance provided by the *CCAA* is that in the event of a disagreement the amount of a claim shall be determined by the court on summary application by the company or by the creditor. Section 12(2) of the *Act* provides:

Determination of amount of claim

(2) For the purposes of this Act, the amount represented by a claim of any secured or unsecured creditor shall be determined as follows:

(a) the amount of an unsecured claim shall be the amount

(i) in the case of a company in the course of being wound up under the Winding-up and Restructuring Act, proof of which has been made in accordance with that Act,

(ii) in the case of a company that has made an authorized assignment or against which a bankruptcy order has been made under the Bankruptcy and Insolvency Act, proof of which has been made in accordance with that Act, or

(iii) in the case of any other company, proof of which might be made under the Bankruptcy and Insolvency Act, but if the amount so provable is not admitted by the company, the amount shall be determined by the court on summary application by the company or by the creditor; and

(b) the amount of a secured claim shall be the amount, proof of which might be made in respect thereof under the Bankruptcy and Insolvency Act if the claim were unsecured, but the amount if not admitted by the company shall, in the case of a company subject to pending proceedings under the Winding-up and Restructuring Act or the Bankruptcy and Insolvency Act, be established by proof in the same manner as an unsecured claim under the Winding-up and Restructuring Act or the Bankruptcy and Insolvency Act, as the case may be, and in the case of any other company the amount shall be determined by the court on summary application by the company or the creditor.

20 The only parties who appeared on this motion were the Monitor, ScoZinc and Komatsu. No specific submissions were requested nor made by the parties with respect to the nature of the court's jurisdiction to determine the mechanism and time lines to classify and quantify claims against the debtor company.

  

21 Under the *Bankruptcy and Insolvency Act* the Trustee is the designated gatekeeper who first determines whether a Proof of Claim submitted by a creditor is valid. The trustee may admit the claim or disallow it in whole or in part (s.135(2) *BIA)*. A creditor who is dissatisfied with a decision by the trustee may appeal to a judge of the Bankruptcy Court.

22 In contrast, the *CCAA* does not set out the procedure beyond the language in s.12. The language only accomplishes two things. The first is that the debtor company can agree on the amount of a secured or unsecured claim; and secondly, if there is a disagreement, then on application of either the company or the creditor, the amount shall be determined by the court on "summary application".

23 The practice has arisen for the court to create by order a claims process that is both flexible and expeditious. The Monitor identifies, by review of the debtor's records, all potential claimants and sends to them a claim package. To ensure that all creditors come forward and participate on a timely basis, there is a provision in the claims process order requiring creditors to file their claims by a fixed date. If they do not, subject to further relief provided by the claims process order, or by the court, the creditor's claim is barred.

24 If the Monitor disagrees with the claim, and the disagreement cannot be resolved, then a claimant can present its case to a claims officer who is usually given the power to adjudicate disputed claims, with the right of appeal to a judge of the court overseeing the *CCAA* proceedings.

25 The establishment of a claims process utilizing the monitor and or a claims officer by court order appears to be a well accepted practice ( See for example *Federal Gypsum Co., Re*, 2007 NSSC 384 (N.S. S.C.); *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 17 C.B.R. (3d) 1 (Ont. Gen. Div.); *Air Canada, Re* (2004), 2 C.B.R. (5th) 23 (Ont. S.C.J. [Commercial List]); *Triton Tubular Components Corp., Re*, [2005] O.J. No. 3926 (Ont. S.C.J.); *Muscletech Research & Development Inc., Re*, [2006] O.J. No. 4087 (Ont. S.C.J.); *Pine Valley Mining Corp., Re*, 2008 BCSC 356 (B.C. S.C.); *Blue Range Resource Corp., Re*, 2000 ABCA 285 (Alta. C.A.); *Carlen Transport Inc. v. Juniper Lumber Co. (Monitor of)* (2001), 21 C.B.R. (4th) 222 (N.B. Q.B.).)

26 I could find no reported case that doubt the authority of the court to create a claims process. Kenneth Kraft in his article "The CCAA and the Claims Bar Process", (2000), 13 *Commercial Insolvency Reporter* 6, endorsed the utilization of a claims process on the basis of reliance on the court's inherent jurisdiction, provided the process adhered to the specific mandates of the *CCAA*. In unrelated contexts, caution has been expressed with respect to reliance on the inherent jurisdiction of the superior court as the basis for dealing with the myriad issues that can arise under the *CCAA* (See: *Skeena Cellulose Inc., Re* (2003), 43 C.B.R. (4th) 187 (B.C. C.A.)) and *Stelco Inc., Re*, [2005] O.J. No. 1171 (Ont. C.A.)).

27 Sir J.H. Jacob, Q.C. in his seminal article "The Inherent Jurisdiction of the Court", (1970) *Current Legal Problems* 23, concluded that it has been clear law from the earliest times that superior courts of justice, as part of their inherent jurisdiction, have the power to control their own proceedings and process. He wrote:

> Under its inherent jurisdiction, the court has power to control and regulate its process and proceedings, and it exercises this power in a great variety of circumstances and by many different methods. Some of the instances of the exercise of this power have been of far-reaching importance, others have dealt with matters of detail or have been of transient value. Some have involved the exercise of administrative powers, others of judicial powers. Some have been turned into rules of law, others by long usage or custom may have acquired the force of law, and still others remain mere rules of practice. The exercise of this power has been pervasive throughout the whole legal machinery and has been extended to all stages of proceedings, pre-trial, trial and post-trial. Indeed, it is difficult to set the limits upon the powers of the court in the exercise of its inherent jurisdiction to control and regulate its process, for these limits are coincident with the needs of the court to fulfil its judicial functions in the administration of justice.
>
> p. 32-33

  

28 The *CCAA* gives no specific guidance to the court on how to determine the existence, nature, validity or extent of a claim against a debtor company. As noted earlier, the only reference is in s. 12 of the *Act* that if there is a dispute as to the amount of a claim, then the amount shall be determined by the court "on summary application". In *Freeman, Re*, [1922] N.S.J. No. 15, [1923] 1 D.L.R. 378 (N.S. C.A.) (en banc) the court considered the words "on summary application" as they appeared in the *Probate Act* R.S.N.S. 1900 c.158. Harris C.J. wrote:

> [17] The words "summary application" do not mean without notice, but simply imply that the proceedings before the Court are not to be conducted in the ordinary way, but in a concise way.
>
> [18] The Oxford Dictionary p. 140 gives as one of the meanings of "summary" dispensing with needless details or formalities — done with despatch.
>
> [19] In the case of the Western &c R. *Co. v. Atlanta* (1901), 113 Ga. 537, the meaning of the words "summary proceeding" is discussed at some length and the Court held at pp. 543-544: —
>
> > "In a summary manner does not at all mean that they may be abated without notice or hearing, but simply that it may be done without a trial in the ordinary forms prescribed by law for a regular judicial procedure."
>
> [20] I cite this not because it is a binding authority, but because its reasoning commends itself to my judgment and I adopt it.

29 In my opinion, whatever process may be appropriate and necessary to adjudicate disputed claims that ultimately end up before a judge of the superior court, the determination by the court that claims must initially be identified and assessed by the Monitor, and heard first by a Claims Officer, is a valid exercise of the court's inherent jurisdiction.

30 The *CCAA* gives to the court the express and implied jurisdiction to do a variety of things. They need not all be enumerated. The court is required to appoint a monitor (s.11.7). Once appointed, the monitor is required to monitor the company's business and financial affairs. The *Act* mandates that the monitor have access to and examine the company's property including all records. The monitor must file a report with the court on the state of the company's business and financial affairs and contain prescribed information. In addition, the monitor shall carry out such other functions in relation to the company as the court may direct (s.11.7(3)(d)).

31 In these circumstances, it is not only logical, but eminently practical that the monitor, as an officer of the court, be directed by court order to fulfil the analogous role to that of the trustee under the *BIA*. The Claims Procedure Order of February 18, 2009 accomplishes this.

**Power of the Monitor**

32 The Monitor was required by the Order to publish a notice to claimants in the newspaper regarding the claims procedure. It was also required to send a claims package to known potential claimants identified by the Monitor through its review of the books and records of ScoZinc. The claims bar date was set as March 16, 2009, or such later date as may be ordered by the court.

33 The duties of the Monitor, once a claim was received by it, were set out in paragraphs 9 and 10 of the Claims Procedure Order. They provide as follows:

> 9. Upon receipt of a Proof of Claim:
>
> > a. The Monitor is hereby authorized and directed to use reasonable discretion as to the adequacy of compliance as to the manner in which Proofs of Claim are completed and executed and may, where it is satisfied that a Claim has been adequately proven, waive strict compliance with the requirements of this Order as to the completion and the execution of a Proof of Claim. A Claim which is accepted by the Monitor shall constitute a Proven Claim;

  

> b. the Monitor and ScoZinc may attempt to consensually resolve the classification and amount of any Claim with the claimant prior to accepting, revising or disallowing such Claim; and
>
> ...
>
> 10. The Monitor shall review all Proofs of Claim filed on or before the Claims Bar Date. The Monitor shall accept, revise or disallow such Proofs of Claim as contemplated herein. The Monitor shall send a Notice of Revision or Disallowance and the form of Notice of Dispute to the Claimant as soon as the Claim has been revised or disallowed but in any event no later than 11:59 p.m. (Halifax time) on March 27, 2009 or such later date as the Court may order. Where the Monitor does not send a Notice of Revision or Disallowance by the aforementioned date to a Claimant who has submitted a Proof of Claim, the Monitor shall be deemed to have accepted such Claim.

34 Any person who wished to dispute a Notice of Revision or Disallowance was required to file a notice to the monitor and to the Claims Officer no later than April 6, 2009. The Claims Officer was designated to be Richard Cregan, Q.C., serving in his personal capacity and not as Registrar in Bankruptcy. Subject to the direction of the court, the Claims Officer was given the power to determine how evidence would be brought before him and any other procedural matters that may arise with respect to the claim. A claimant or the Monitor may appeal the Claims Officer's decision to the court.

35 The Monitor suggests that the power given to it under paragraph 9(a) and 10 is sufficient to permit it to accept the revised Proofs of Claim filed after the claim's bar date of March 16, 2009, but before its assessment date of March 27, 2009.

36 Reliance is also placed on the decision of the Alberta Court of Appeal in *Blue Range Resource Corp., Re*, 2000 ABCA 285 (Alta. C.A.). As noted by the Monitor, the decision in *Blue Range* did not directly deal with the issue on which the Monitor here seeks directions. In *Blue Range*, the claims procedure established by the court set the claims bar date of June 15, 1999. Claims of creditors not proven in accordance with the procedures set out were deemed to be forever barred. Some creditors filed their Notice of Claim after the claims bar date. The monitor disallowed their claims. There were a second group of creditors who filed their Notice of Claim prior to the applicable claims bar date, but then sought to amend their claims after the claims bar date had passed. The monitor also disallowed these claims as late. What is not clear from the reported decisions is whether this second group of creditors requested amendments of their claims during the time period granted to the Monitor to carry out its assessment.

37 The chambers judge allowed the late and amended claims to be filed. Enron Capital Corp. and the creditor's committee sought leave to appeal that decision. Leave to appeal was granted on January 14, 2000 with respect to the following question:

> What criteria in the circumstances of these cases should the Court use to exercise its discretion in deciding whether to allow late claimants to file claims which, if proven, may be recognized, notwithstanding a previous claims bar order containing a claims bar date which would otherwise bar the claim of the late claimants, and applying the criteria to each case, what is the result?
>
> *Blue Range Resource Corp., Re*, 2000 ABCA 16 (Alta. C.A. [In Chambers])

38 Wittmann J.A. delivered the judgment of the court. He noted that all counsel conceded that the court had the authority to allow the late filing of claims and that the appeal was really a matter of what criteria the court should use in exercising that power. Accordingly, a Claims Procedure Order that contains a claims bar date should not purport to forever bar a claim without a saving provision. Wittmann J.A. set out the test for determining when a late claim may be included to be as follows:

> [26] Therefore, the appropriate criteria to apply to the late claimants is as follows:
>
> 1. Was the delay caused by inadvertence and if so, did the claimant act in good faith?
>
> 2. What is the effect of permitting the claim in terms of the existence and impact of any relevant prejudice caused by the delay?

  

> 3. If relevant prejudice is found can it be alleviated by attaching appropriate conditions to an order permitting late filing?
>
> 4. If relevant prejudice is found which cannot be alleviated, are there any other considerations which may nonetheless warrant an order permitting late filing?
>
> [27] In the context of the criteria, "inadvertent" includes carelessness, negligence, accident, and is unintentional. I will deal with the conduct of each of the respondents in turn below and then turn to a discussion of potential prejudice suffered by the appellants.

2000 ABCA 285 (Alta. C.A.)

39 The appellants claimed that they would be prejudiced if the late claims were allowed because if they had known the late claims would be allowed they would have voted differently. This assertion was rejected by the chambers judge. With respect to what is meant by prejudiced, Wittmann J.A. wrote:

> 40 In a CCAA context, as in a BIA context, the fact that Enron and the other Creditors will receive less money if late and late amended claims are allowed is not prejudice relevant to this criterion. Re-organization under the CCAA involves compromise. Allowing all legitimate creditors to share in the available proceeds is an integral part of the process. A reduction in that share can not be characterized as prejudice: Re Cohen (1956), 36 C.B.R. 21 (Alta. C.A.) at 30-31. Further, I am in agreement with the test for prejudice used by the British Columbia Court of Appeal in 312630 British Columbia Ltd. It is: did the creditor(s) by reason of the late filings lose a realistic opportunity to do anything that they otherwise might have done? Enron and the other creditors were fully informed about the potential for late claims being permitted, and were specifically aware of the existence of the late claimants as creditors. I find, therefore, that Enron and the Creditors will not suffer any relevant prejudice should the late claims be permitted.

40 In considering how the Monitor should carry out its duties and responsibilities under the Claims Procedure Order it is important to note that the Monitor is an officer of the court and is obliged to ensure that the interests of the stakeholders are considered including all creditors, the company and its shareholders ( See *Laidlaw Inc., Re* (2002), 34 C.B.R. (4th) 72 (Ont. S.C.J. [Commercial List]).

41 In a different context Turnball J.A. in *Siscoe & Savoie v. Royal Bank* (1994), 29 C.B.R. (3d) 1 (N.B. C.A.) commented that the monitor is an agent of the court and as a result is responsible and accountable to the court, owing a fiduciary duty to all of the parties (para. 28).

42 In my opinion, para. 9(a) is not of assistance in determining the authority of the Monitor to revise upward a claim filed after the claim's bar date but before the assessment date. Paragraph 9(a) authorizes the Monitor to use reasonable discretion as to the adequacy of compliance as to *the manner* to which Proofs of Claim are completed and executed. If it satisfied that the claim has been adequately proven it may waive strict compliance with the requirements of the order as to *completion* and the *execution* of a Proof of Claim.

43 Paragraph 10 of the Claims Procedure Order mandates the Monitor shall review all Proofs of Claim filed on or before the claims bar date. It shall "accept, revise or disallow such Proofs of Claim as contemplated herein". While normally a monitor's revision would be to reduce a Proof of Claim, there is in fact nothing in the Claims Procedure Order that so restricts the Monitor's authority. It is obviously contemplated by para. 10 that the monitor is to carry out some assessment of the claims that are submitted.

44 In my view, the Proofs of Claim that are filed act both as a form of pleading and an opportunity for the claimant to provide supporting documents to evidence its claim. In the case before me, the creditors discovered that the claims they had submitted were inaccurate and further evidence was tendered to the Monitor to demonstrate. The Monitor, after reviewing the evidence, accepted the validity of the claims.

  

45 Courts in a general way are engaged in dispensing justice. They do so by setting up and applying procedural rules to ensure that litigants are afforded a fair hearing. The resolution of disputes through the litigation process, including the ultimate hearing, is fundamentally a truth-seeking process to determine the facts and to apply the law to those facts. Can it be any different where the process is not in the court but under its supervision pursuant to a claims process under the *CCAA.?*

46 To suggest that the monitor does not have the authority to receive evidence and submissions and to consider them is to say that it does not have any real authority to carry out its court appointed role to assess the claims that have been submitted. The notion that the monitor cannot look at documentary evidence on its own initiative or at the instance of a claimant, and even consider submissions, is to deny it any real power to consider and make a preliminary determination of the merits of a claim.

47 The Claims Procedure Order contains a number of provisions that anticipate the exchange of information between the Monitor, the company and a creditor. Paragraph 9(b) authorizes the Monitor and ScoZinc to attempt to consensually resolve the classification and the amount of any claim with a claimant prior to accepting, revising or disallowing such claim. Paragraph 17 of the Claims Procedure Order directs that the Monitor shall at all times be authorized to enter into negotiations with claimants and settle any claim on such terms as the Monitor may consider appropriate.

48 In my opinion, it does not matter that revised claims were submitted after the claims bar date. In essence, the Monitor simply acted to revise the Proofs of Claim already submitted to conform with the evidence elicited by the Monitor, or submitted to it. The Monitor had the necessary authority to revise the claims, either as to classification or amount.

49 If a claimant seeks to revise or amend its claim after the assessment date set out in the Claims Procedure Order, different considerations may come into play. The appropriate procedure will depend on the provisions of the Claims Procedure Order. In addition, the court, as the ultimate arbiter of disputed claims under s. 12 of the *CCAA*, should always be viewed as having the jurisdiction to permit appropriate revision of claims.

*Order accordingly.*

**End of Document**

**Most Negative Treatment:** Not followed
**Most Recent Not followed:** M. (L.D.) v. M. (D.R.) | 2008 BCSC 1752, 2008 CarswellBC 2740, [2009] B.C.W.L.D. 1125, [2009] B.C.W.L.D. 1132, [2009] B.C.W.L.D. 1134, [2009] B.C.W.L.D. 1135, 173 A.C.W.S. (3d) 545, [2009] W.D.F.L. 689, [2009] W.D.F.L. 706, [2009] W.D.F.L. 708, [2009] W.D.F.L. 709 | (B.C. S.C., Dec 18, 2008)

1997 CarswellOnt 1489
Supreme Court of Canada

Soulos v. Korkontzilas

1997 CarswellOnt 1489, 1997 CarswellOnt 1490, [1997] 2 S.C.R. 217, [1997] S.C.J. No. 52, 100 O.A.C. 241, 146 D.L.R. (4th) 214, 17 E.T.R. (2d) 89, 212 N.R. 1, 32 O.R. (3d) 716 (note), 46 C.B.R. (3d) 1, 71 A.C.W.S. (3d) 194, 9 R.P.R. (3d) 1, J.E. 97-1111

# Fotios Korkontzilas, Panagiota Korkontzilas and Olympia Town Real Estate Limited, Appellants v. Nick Soulos, Respondent

La Forest, Sopinka, Gonthier, Cory, McLachlin, Iacobucci and Major JJ.

Heard: February 8, 1997
Judgment: May 22, 1997
Docket: 24949

Proceedings: affirming (1995), 84 O.A.C 390 (Ont. C.A..); reversing (1991), 4 O.R. (3d) 51 (Ont. Gen. Div.); additional reasons at (1991), 4 O.R. (3d) 51 at 71 (Ont. Gen. Div.)

Counsel: *Thomas G. Heintzman, Q.C.* , and *Darryl A. Cruz* , for the appellants.
*David T. Stockwood, Q.C.* , and *Susan E. Caskey* , for the respondent.

Subject: Torts; Contracts; Estates and Trusts; Insolvency; Property
**Related Abridgment Classifications**
Commercial law
I Agency
I.6 Relationship between principal and agent
I.6.b Agent's duties to principal
I.6.b.ii Fiduciary duty
I.6.b.ii.C Duty to disclose
Estates and trusts
II Trusts
II.3 Constructive trust
II.3.b Gains by fiduciaries
Real property
IV Real estate agents
IV.10 Agent's duties to principal
IV.10.b Duty to make full disclosure to principal
IV.10.b.v Miscellaneous
**Headnote**
Trusts and Trustees --- Constructive trust — Gains by fiduciaries
Appeal dismissed.
Agency --- Relationship between principal and agent — Agent's duties to principal — Fiduciary duty — Duty to disclose

  

Appeal dismissed.
Fiducies et fiduciaires --- Fiducie par interprétation — Avantages tirés par le fiduciaire
Pourvoi a été rejeté.
Mandat --- Relation entre le mandant et le mandataire — Obligations du mandataire envers le mandant — Obligation fiduciaire — Obligation d'informer — Courtier en immeuble n'a pas informé son client que le vendeur avait accepté son offre pour une propriété
Pourvoi a été rejeté.
A real estate broker failed to advise his client that the seller of a commercial property had accepted the client's counter-offer and arranged for his wife to purchase the property. Title was then transferred to the broker and his wife as joint tenants. When the client discovered what had happened, he commenced an action against the broker for breach of fiduciary duty and sought to have the property conveyed to him on the basis of constructive trust. The client had not suffered any monetary loss as a result of the broker's conduct because of a subsequent decrease in the market value of the property. However, the client still wanted the property because of the prestige associated with the ownership of it.
At trial, the broker was found to have been in breach of fiduciary duty, but the judge refused to grant the constructive trust remedy because the broker had not been enriched by his purchase of the property, in that its value had decreased. The decision was reversed on appeal, with the Court of Appeal holding the the moral quality of the broker's conduct allowed the court to grant the constructive trust remedy. It stated that the remedy was necessary in order to act as deterrent to activity in the real estate business that would undermine bonds of trust that enabled that industry to function. The broker appealed to the Supreme Court of Canada
**Held:** The appeal was dismissed
Per McLachlin J. (La Forest, Gonthier, Cory and Major JJ. concurring): Constructive trusts are not limited exclusively to cases involving unjust enrichment. Wrongful conduct by itself can give rise to the remedy if the following criteria are met: the defendant must have been under an equitable obligation, the defendant must have derived the assets from agency activities in breach of his equitable obligation to the plaintiff, the plaintiff must show a legitimate reason for seeking the remedy, either persona or related to the need to ensure that others like the defendant remain faithful to their duties, and there must be no factors (such as the rights of third parties) which would render imposition of a constructive trust unjust in all the circumstances of the case. In this case, the broker obtained the property as a result of a breach of his obligation to the client and as a direct result of his agency activities with respect to the client. As well, the client still had a desire to own the property and the remedy was necessary to ensure that real estate agents and others in positions of trust remain faithful to their duty of loyalty to their clients. To allow the broker to keep the property in these circumstances would have undermined the trust and confidence which underpins the institution of real estate brokerage. Finally, there were no factors which would make the imposition of a constructive trust unjust.
Per Sopinka J. (dissenting) (Iacobucci J. concurring): The granting of a constructive trust is a discretionary remedy and, as such, a decision of a trial judge on this issue can be overturned only if it can be shown that the judge made an error in principle. In this case, the trial judge did not commit any error in principle in rendering his decision
Recent case law had made it very clear that a constructive trust can be granted only in cases of unjust enrichment, which must be pecuniary in nature. In this case, there was no such enrichment.
. . . . .
Un courtier en immeuble a volontairement omis d'informer son client que le vendeur d'un immeuble commercial avait accepté sa contre-offre et s'est arrangé pour que son épouse en fasse l'acquisition. Le titre a ensuite été transféré au courtier et à son épouse en tant que cotitulaires. Lorsque le client a eu vent de la manoeuvre, il a entrepris une action contre le courtier pour manquement à son obligation de fiduciaire, avec des conclusions translatives de propriété en vertu de la doctrine de la fiducie par interprétation. Le client n'avait pas subi de dommages pécuniaires par suite des agissements du courtier, car l'immeuble avait subséquemment subi une dévaluation. Cependant, le client désirait toujours acquérir l'immeuble à cause du prestige lié à cette propriété.
Au procès, le juge du procès a estimé que le courtier avait manqué à son obligation de fiduciaire, mais a refusé d'accorder le redressement en vertu de la fiducie par interprétation puisque le courtier ne s'était pas enrichi par suite de l'acquisition de l'immeuble, celui-ci s'étant dévalué. Le jugement a été annulé par la Cour d'appel, qui a statué que la turpitude du courtier l'autorisait à accueillir le recours fondé sur la fiducie par interprétation. La Cour a conclu que ce redressement s'avérait nécessaire

  

afin de dissuader les agissements dans le domaine du courtage immobilier qui nuiraient au lien de confiance, élément essentiel dans ce secteur d'activité. Le courtier a formé un pourvoi à la Cour suprême du Canada.

**Arrêt:** Le pourvoi a été rejeté.

McLachlin, J. (La Forest, Gonthier, Cory et Major, JJ., souscrivant) : Les fiducies par interprétation ne se limitent pas seulement aux cas d'enrichissement sans cause. En soi, l'inconduite peut donner ouverture à ce recours si les critères suivants sont rencontrés : le défendeur doit assumer une obligation équitable, le défendeur doit avoir distrait les biens objets de son mandat en violation de son obligation équitable envers le demandeur, le demandeur doit avoir une raison légitime d'entreprendre un tel recours, soit personnelle ou liée au besoin de s'assurer que d'autres dans la position du défendeur respectent leurs obligations et il ne doit pas exister d'autres facteurs (tels les droits des tiers) qui, dans les circonstances du litige, rendraient injuste l'imposition d'une fiducie par interprétation. En l'espèce, le courtier a obtenu l'immeuble à la suite d'une violation de son obligation envers son client et à la suitede ses activités en tant que mandataire pour le compte du client. En outre, le client désirait toujours acquérir l'immeuble et le recours s'avérait nécessaire pour s'assurer que les courtiers en immeuble, de même que d'autres personnes en situation de confiance, respectent leur obligation de loyauté envers leurs clients. En l'occurrence, permettre au courtier de conserver l'immeuble compromettrait le lien de confiance qui sous-tend l'institution du courtage immobilier. En terminant, il n'y avait aucun facteur qui rendait injuste l'imposition d'une fiducie par interprétation.

Sopinka, J. (dissident) (Iacobucci, J., souscrivant) : Accorder une fiducie par interprétation est un redressement discrétionnaire et, comme telle, la décision du juge du procès ne peut être annulée que s'il est démontré une erreur de principe de sa part. En l'espèce, le juge du procès n'a pas commis d'erreur de principe.

La jurisprudence récente a établi très clairement qu'une fiducie par interprétation ne peut être accordée que dans des cas d'enrichissement sans cause, de nature pécuniaire. Il n'existait pas de tel enrichissement dans ce dossier.

**Table of Authorities**

**Cases considered by *McLachlin J.* (*La Forest, Gonthier, Cory* and *Major JJ.* concurring):**

*Beatty v. Guggenheim Exploration Co.*, 122 N.E. 378 (U.S. 1919) — considered

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

*Binions v. Evans*, [1972] 2 All E.R. 70, [1972] Ch. 359 (Eng. C.A.) — considered

*Carl-Zeiss-Stiftung v. Herbert Smith & Co. (No. 2)*, [1968] 2 All E.R. 367, [1968] 2 Ch. 276 (Eng. C.A.) — considered

*Elders Pastoral Ltd. v. Bank of New Zealand* (1989), 2 N.Z.L.R. 180 — considered

*Goldcorp Exchange Ltd., Re*, [1994] 2 All E.R. 806 (New Zealand P.C.) — considered

*Hodgkinson v. Simms*, [1994] 9 W.W.R. 609, 49 B.C.A.C. 1, 80 W.A.C. 1, 22 C.C.L.T. (2d) 1, 16 B.L.R. (2d) 1, 6 C.C.L.S. 1, 57 C.P.R. (3d) 1, 5 E.T.R. (2d) 1, [1994] 3 S.C.R. 377, 95 D.T.C. 5135, 97 B.C.L.R. (2d) 1, 117 D.L.R. (4th) 161, 171 N.R. 245 (S.C.C.) — considered

*Hussey v. Palmer*, [1972] 1 W.L.R. 1286, [1972] 3 All E.R. 744 (Eng. C.A.) — considered

*MacMillan Bloedel Ltd. v. Binstead* (1983), 22 B.L.R. 255, 14 E.T.R. 269 (B.C. S.C.) — considered

*Meinhard v. Salmon*, 164 N.E. 545 (U.S. 1928) — considered

*Neale v. Willis* (1968), 112 Sol. Jo. 521, 19 P. & C.R. 836 (Eng. C.A.) — referred to

*Neste Oy v. Lloyd's Bank Ltd.*, [1983] 2 Lloyd's Rep. 658 (Eng. C.A.) — considered

*Ontario (Wheat Producers' Marketing Board) v. Royal Bank* (1984), 46 O.R. (2d) 362, 9 D.L.R. (4th) 729 (Ont. C.A.) — considered

*White v. Central Trust Co.* (1984), 7 D.L.R. (4th) 236, 54 N.B.R. (2d) 293, 17 E.T.R. 78 (N.B. C.A.) — considered

**Cases considered by *Sopinka J.* (dissenting) (*Iacobucci J.* concurring):**

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

*Brissette v. Westbury Life Insurance Co.*, [1992] I.L.R. 1-2888, 47 E.T.R. 109, 13 C.C.L.I. (2d) 1, 142 N.R. 104, 58 O.A.C. 10, *(*sub nom. *Brissette Estate v. Westbury Life Insurance Co.)* [1992] 3 S.C.R. 87 (S.C.C.) — considered

*Canadian Aero Service Ltd. v. O'Malley* (1973), [1974] S.C.R. 592, 40 D.L.R. (3d) 371, 11 C.P.R. (2d) 206 (S.C.C.) — considered

*Canson Enterprises Ltd. v. Boughton & Co.*, [1992] 1 W.W.R. 245, 9 C.C.L.T. (2d) 1, 39 C.P.R. (3d) 449, 131 N.R. 321, 85 D.L.R. (4th) 129, 61 B.C.L.R. (2d) 1, 6 B.C.A.C. 1, 13 W.A.C. 1, [1991] 3 S.C.R. 534, 43 E.T.R. 201 (S.C.C.) — considered

  

*Donkin v. Bugoy*, [1985] 2 S.C.R. 85, [1985] 6 W.W.R. 97, 21 D.L.R. (4th) 327, 61 N.R. 172, 44 Sask. R. 178, 20 E.T.R. 225, 47 R.F.L. (2d) 113 (S.C.C.) — considered
*Hodgkinson v. Simms*, [1994] 9 W.W.R. 609, 49 B.C.A.C. 1, 80 W.A.C. 1, 22 C.C.L.T. (2d) 1, 16 B.L.R. (2d) 1, 6 C.C.L.S. 1, 57 C.P.R. (3d) 1, 5 E.T.R. (2d) 1, [1994] 3 S.C.R. 377, 95 D.T.C. 5135, 97 B.C.L.R. (2d) 1, 117 D.L.R. (4th) 161, 171 N.R. 245 (S.C.C.) — referred to
*International Corona Resources Ltd. v. LAC Minerals Ltd.*, 6 R.P.R. (2d) 1, 44 B.L.R. 1, 35 E.T.R. 1, 69 O.R. (2d) 287, 26 C.P.R. (3d) 97, 61 D.L.R. (4th) 14, 101 N.R. 239, 36 O.A.C. 57, *(*sub nom. *LAC Minerals Ltd. v. International Corona Resources Ltd.)* [1989] 2 S.C.R. 574 (S.C.C.) — considered
*Lee v. Chow* (1990), 12 R.P.R. (2d) 217 (Ont. H.C.) — considered
*MacMillan Bloedel Ltd. v. Binstead* (1983), 22 B.L.R. 255, 14 E.T.R. 269 (B.C. S.C.) — considered
*Ontario (Wheat Producers' Marketing Board) v. Royal Bank* (1984), 46 O.R. (2d) 362, 9 D.L.R. (4th) 729 (Ont. C.A.) — considered
*Phipps v. Boardman*, [1965] Ch. 992, [1965] 1 All E.R. 849 (Eng. C.A.) — considered
*Phipps v. Boardman*, [1967] 2 A.C. 46, [1966] 3 All E.R. 721 (Eng. H.L.) — considered
*Reading v. R.*, [1948] 2 K.B. 268, [1948] 2 All E.R. 27 (Eng. K.B.) — considered
*Reading v. R.*, [1949] 2 K.B. 232, [1949] 2 All E.R. 68 (Eng. C.A.) — considered
*Reading v. R.*, [1951] A.C. 507, [1951] 1 All E.R. 617 (Eng. H.L.) — considered
*Syncrude Canada Ltd. v. Hunter Engineering Co.*, *(*sub nom. *Hunter Engineering Co. v. Syncrude Can. Ltd.)* [1989] 3 W.W.R. 385, *(*sub nom. *Hunter Engineering Co. v. Syncrude Can. Ltd.)* 57 D.L.R. (4th) 321, *(*sub nom. *Hunter Engineering Co. v. Syncrude Can. Ltd.)* 35 B.C.L.R. (2d) 145, *(*sub nom. *Hunter Engineering Co. v. Syncrude Can. Ltd.)* 92 N.R. 1, *(*sub nom. *Hunter Engineering Co. v. Syncrude Can. Ltd.)* [1989] 1 S.C.R. 426 (S.C.C.) — considered

APPEAL from judgment reported at [1995] 84 O.A.C. 390 , allowing appeal from (1991), 4 O.R. (3d) 51 (Gen. Div.) , additional reasons at (1991), 4 O.R. (3d) 51 at 71 (Gen. Div.) which refused to grant remedy of constructive trust for breach of fiduciary duty when no resulting unjust enrichment.

POURVOI à l'encontre d'un arrêt publié à [1995] 84 O.A.C. 390 , accueillant le pourvoi à l'encontre de (1991), 4 O.R. (3d) 51 (Gen. Div.) , motifs additionnels publié à (1991), 4 O.R. (3d) 51 à 71 (Div. Gén.), refusant le redressement en vertu de la fiducie par interprétation résultant de la violation de l'obligation fiduciaire lorsque aucun enrichissement sans cause n'en résulte.

***McLachlin J.*** **(La Forest, Gonthier, Cory and Major JJ. concurring):**

**I**

1 This appeal requires this Court to determine whether a real estate agent who buys for himself property for which he has been negotiating on behalf of a client, may be required to return the property to his client despite the fact that the client can show no loss. This raises the legal issue of whether a constructive trust over property may be imposed in the absence of enrichment of the defendant and corresponding deprivation of the plaintiff. In my view, this question should be answered in the affirmative.

**II**

2 The appellant Mr. Korkontzilas is a real estate broker. The respondent, Mr. Soulos, was his client. In 1984, Mr. Korkontzilas found a commercial building which he thought might interest Mr. Soulos. Mr. Soulos was interested in purchasing the building. Mr. Korkontzilas entered into negotiations on behalf of Mr. Soulos. He offered $250,000. The vendor, Dominion Life, rejected the offer and tendered a counter-offer of $275,000. Mr. Soulos rejected the counter-offer but "signed it back" at $260,000 or $265,000. Dominion Life advised Mr. Korkontzilas that it would accept $265,000. Instead of conveying this information to Mr. Soulos as he should have, Mr. Korkontzilas arranged for his wife, Panagiota Goutsoulas, to purchase the property using the name Panagiot Goutsoulas. Panagiot Goutsoulas then transferred the property to Panagiota and Fotios Korkontzilas as joint tenants. Mr. Soulos asked what had happened to the property. Mr. Korkontzilas told him to "forget about it"; the vendor no longer wanted to sell it and he would find him a better property. Mr. Soulos asked Mr. Korkontzilas whether he had had anything to do with the vendor's change of heart. Mr. Korkontzilas said he had not.

  

3 In 1987 Mr. Soulos learned that Mr. Korkontzilas had purchased the property for himself. He brought an action against Mr. Korkontzilas to have the property conveyed to him, alleging breach of fiduciary duty giving rise to a constructive trust. He asserted that the property held special value to him because its tenant was his banker, and being one's banker's landlord was a source of prestige in the Greek community of which he was a member. However, Mr. Soulos abandoned his claim for damages because the market value of the property had, in fact, decreased from the time of the Korkontzilas purchase.

4 The trial judge found that Mr. Korkontzilas had breached a duty of loyalty to Mr. Soulos, but held that a constructive trust was not an appropriate remedy because Mr. Korkontzilas had purchased the property at market value and hence had not been "enriched": (1991), 4 O.R. (3d) 51, 19 R.P.R. (2d) 205 (Ont. Gen. Div.) (hereinafter cited to O.R.). The decision was reversed on appeal, Labrosse J.A. dissenting: (1995), 25 O.R. (3d) 257, 126 D.L.R. (4th) 637, 84 O.A.C. 390, 47 R.P.R. (2d) 221 (Ont. C.A.) (hereinafter cited to O.R.).

5 For the reasons that follow, I would dismiss the appeal. In my view, the doctrine of constructive trust applies and requires that Mr. Korkontzilas convey the property he wrongly acquired to Mr. Soulos.

**III**

6 The first question is what duties Mr. Korkontzilas owed to Mr. Soulos in relation to the property. This question returns us to the findings of the trial judge. The trial judge rejected the submission of Mr. Soulos that an agreement existed requiring Mr. Korkontzilas to present all properties in the Danforth area to him exclusively before other purchasers. He found, however, that Mr. Korkontzilas became the agent for Mr. Soulos when he prepared the offer which Mr. Soulos signed with respect to the property at issue. He further found that this agency relationship extended to reporting the vendor's response to Mr. Soulos. This relationship of agency was not terminated when the vendor made its counter-offer. The trial judge therefore concluded that Mr. Korkontzilas was acting as Mr. Soulos' agent at all material times.

7 The trial judge went on to state that the relationship of agent and principal is fiduciary in nature. He concluded that as agent to Mr. Soulos, Mr. Korkontzilas owed Mr. Soulos a "duty of loyalty". He found that Mr. Korkontzilas breached this duty of loyalty when he failed to refer the vendor's counter-offer to Mr. Soulos.

8 The Court of Appeal did not take issue with these conclusions. The majority did, however, differ from the trial judge on what consequences flowed from Mr. Korkontzilas' breach of the duty of loyalty.

**IV**

9 This brings us to the main issue on this appeal: what remedy, if any, does the law afford Mr. Soulos for Mr. Korkontzilas' breach of the duty of loyalty in acquiring the property in question for himself rather than passing the vendor's statement of the price it would accept on to his principal, Mr. Soulos?

10 At trial Mr. Soulos' only claim was that the property be transferred to him for the price paid by Mr. Korkontzilas, subject to adjustments for changes in value and losses incurred on the property since purchase. He abandoned his claim for damages at an early stage of the proceedings. This is not surprising, since Mr. Korkontzilas had paid market value for the property and had, in fact, lost money on it during the period he had held it. Still, Mr. Soulos maintained his desire to own the property.

11 Mr. Soulos argued that the property should be returned to him under the equitable doctrine of constructive trust. The trial judge rejected this claim, on the ground that constructive trust arises only where the defendant has been unjustly enriched by his wrongful act. The fact that damages offered Mr. Soulos no compensation was of no moment: "It would be anomalous to declare a constructive trust, in effect, because a remedy in damages is unsatisfactory, the plaintiff having suffered none" (p. 69). Furthermore, "it seems simply disproportionate and inappropriate to utilize the drastic remedy of a constructive trust where the plaintiff has suffered no damage" (p. 69). The trial judge added that nominal damages were inappropriate, damages having been waived, and that Mr. Soulos had mitigated his loss by buying other properties.

  

12 The majority of the Court of Appeal took a different view. Carthy J.A. held that the award of an equitable remedy is discretionary and dependent on all the facts before the court. In his view, however, the trial judge had exercised his discretion on a wrong principle. Carthy J.A. asserted that the moral quality of the defendant's act may dictate the court's intervention. Most real estate transactions involve one person acting gratuitously for the purchaser, while seeking commission from the vendor. The fiduciary duties of the agent would be meaningless if the agent could simply acquire the property at market value, and then deny that he or she is a constructive trustee because no damages are suffered. In such circumstances, equity will "intervene with a proprietary remedy to sustain the integrity of the laws which it supervises" (p. 261). Carthy J.A. conceded that Mr. Soulos' reason for desiring the property may seem "whimsical". But viewed against the broad context of real estate transactions, he found that the remedy of constructive trust in these circumstances serves a "salutary purpose". It enables the court to ensure that immoral conduct is not repeated, undermining the bond of trust that enables the industry to function. The majority accordingly ordered conveyance of the property subject to appropriate adjustments.

13 The difference between the trial judge and the majority in the Court of Appeal may be summarized as follows. The trial judge took the view that in the absence of established loss, Mr. Soulos had no action. To grant the remedy of constructive trust in the absence of loss would be "simply disproportionate and inappropriate", in his view. The majority in the Court of Appeal, by contrast, took a broader view of when a constructive trust could apply. It held that a constructive trust requiring reconveyance of the property could arise in the absence of an established loss in order to condemn the agent's improper act and maintain the bond of trust underlying the real estate industry and hence the "integrity of the laws" which a court of equity supervises.

14 The appeal thus presents two different views of the function and ambit of the constructive trust. One view sees the constructive trust exclusively as a remedy for clearly established loss. On this view, a constructive trust can arise only where there has been "enrichment" of the defendant and corresponding "deprivation" of the plaintiff. The other view, while not denying that the constructive trust may appropriately apply to prevent unjust enrichment, does not confine it to that role. On this view, the constructive trust may apply absent an established loss to condemn a wrongful act and maintain the integrity of the relationships of trust which underlie many of our industries and institutions.

15 It is my view that the second, broader approach to constructive trust should prevail. This approach best accords with the history of the doctrine of constructive trust, the theory underlying the constructive trust, and the purposes which the constructive trust serves in our legal system.

**V**

16 The appellants argue that this Court has adopted a view of constructive trust based exclusively on unjust enrichment in cases such as *Becker v. Pettkus*, [1980] 2 S.C.R. 834 (S.C.C.) . Therefore, they argue, a constructive trust cannot be imposed in cases like this where the plaintiff can demonstrate no deprivation and corresponding enrichment of the defendant.

17 The history of the law of constructive trust does not support this view. Rather, it suggests that the constructive trust is an ancient and eclectic institution imposed by law not only to remedy unjust enrichment, but to hold persons in different situations to high standards of trust and probity and prevent them from retaining property which in "good conscience" they should not be permitted to retain. This served the end, not only of doing justice in the case before the court, but of protecting relationships of trust and the institutions that depend on these relationships. These goals were accomplished by treating the person holding the property as a trustee of it for the wronged person's benefit, even though there was no true trust created by intention. In England, the trust thus created was thought of as a real or "institutional" trust. In the United States and recently in Canada, jurisprudence speaks of the availability of the constructive trust as a remedy; hence the remedial constructive trust.

18 While specific situations attracting a constructive trust have been identified, the older English jurisprudence offers no satisfactory limiting or unifying conceptual theory for the constructive trust. As D. W. M. Waters, *The Constructive Trust* (1964), at p. 39, puts it, the constructive trust "was never any more than a convenient and available language medium through which ... the obligations of parties might be expressed or determined". The constructive trust was used in English law "to link together a number of disparate situations ... on the basis that the obligations imposed by law in these situations might in some way

  

be likened to the obligations which were imposed upon an express trustee": J. L. Dewar, "The Development of the Remedial Constructive Trust" (1981), 6 *Est. & Tr. Q.* 312, at p. 317, citing Waters, *supra* .

19 The situations in which a constructive trust was recognized in England include constructive trusts arising on breach of a fiduciary relationship, as well as trusts imposed to prevent the absence of writing from depriving a person of proprietary rights, to prevent a purchaser with notice from fraudulently retaining trust properties, and to enforce secret trusts and mutual wills. See Dewar, *supra* , at p. 334. The fiduciary relationship underlies much of the English law of constructive trust. As Waters, *supra* , at p. 33, writes: "the fiduciary relationship is clearly wed to the constructive trust over the whole, or little short of the whole, of the trust's operation". At the same time, not all breaches of fiduciary relationships give rise to a constructive trust. As L. S. Sealy, "Fiduciary Relationships", [1962] *Camb. L.J.* 69, at p. 73, states:

> The word "fiduciary," we find, is *not* definitive of a single class of relationships to which a fixed set of rules and principles apply. Each equitable remedy is available only in a limited number of fiduciary situations; and the mere statement that John is in a fiduciary relationship towards me means no more than that in some respects his position is trustee-like; it does not warrant the inference that any particular fiduciary principle or remedy can be applied. [Emphasis in original.]

Nor does the absence of a classic fiduciary relationship necessarily preclude a finding of a constructive trust; the wrongful nature of an act may be sufficient to constitute breach of a trust-like duty: see Dewar, *supra* , at pp. 322-23.

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: *Becker v. Pettkus, supra* .

21 This Court's assertion that a remedial constructive trust lies to prevent unjust enrichment in cases such as *Becker v. Pettkus* should not be taken as expunging from Canadian law the constructive trust in other circumstances where its availability has long been recognized. The language used makes no such claim. A. J. McClean, "Constructive and Resulting Trusts — Unjust Enrichment in a Common Law Relationship — *Pettkus v. Becker* " (1982), 16 *U.B.C.L. Rev.* 156 at p. 170, describes the ratio of *Becker v. Pettkus* as "a modest enough proposition". He goes on: "It would be wrong ... to read it as one would read the language of a statute and limit further development of the law".

22 Other scholars agree that the constructive trust as a remedy for unjust enrichment does not negate a finding of a constructive trust in other situations. D. M. Paciocco, "The Remedial Constructive Trust: A Principled Basis for Priorities over Creditors, (1989), 68 *Can. Bar Rev.* 315, at p. 318, states: "the constructive trust that is used to remedy unjust enrichment must be distinguished from the other types of constructive trusts known to Canadian law prior to 1980". Paciocco asserts that unjust enrichment is not a necessary condition of a constructive trust (at p. 320):

> ... in the largest traditional category, the fiduciary constructive trust, there need be no deprivation experienced by the particular plaintiff. The constructive trust is imposed to raise the morality of the marketplace generally, with the beneficiaries of some of these trusts receiving what can only be described as a windfall.

23 Dewar, *supra* , holds a similar view (at p. 332):

> While it is unlikely that Canadian courts will abandon the learning and the classifications which have grown up in connection with the English constructive trust, it is submitted that the adoption of the American style constructive trust by the Supreme Court of Canada in *Pettkus v. Becker* will profoundly influence the future development of Canadian trust law.

Dewar, *supra* , at pp. 332-33, goes on to state: "In English and Canadian law there is no general agreement as to precisely which situations give rise to a constructive trust, although there are certain general categories of cases in which it is agreed that a constructive trust does arise". One of these is to correct fraudulent or disloyal conduct.

 

24 M. M. Litman, "The Emergence of Unjust Enrichment as a Cause of Action and the Remedy of Constructive Trust", (1988), 26 *Alta. L. Rev.* 407, at p. 414, sees unjust enrichment as a useful tool in rationalizing the traditional categories of constructive trust. Nevertheless he opines that it would be a "significant error" to simply ignore the traditional principles of constructive trust. He cites a number of Canadian cases subsequent to *Becker v. Pettkus, supra* , which impose constructive trusts for wrongful acquisition of property, even in the absence of unjust enrichment and correlative deprivation, and concludes that the constructive trust "cannot always be explained by the unjust enrichment model of constructive trust" (p. 416). In sum, the old English law remains part of contemporary Canadian law and guides its development. As La Forest J.A. (as he then was) states in *White v. Central Trust Co.* (1984), 17 E.T.R. 78 (N.B. C.A.) , at p. 90, cited by Litman, *supra* , the courts "will not venture far onto an uncharted sea when they can administer justice from a safe berth".

25 I conclude that the law of constructive trust in the common law provinces of Canada embraces the situations in which English courts of equity traditionally found a constructive trust as well as the situations of unjust enrichment recognized in recent Canadian jurisprudence.

**VI**

26 Various principles have been proposed to unify the situations in which the English law found constructive trust. R. Goff and G. Jones, *The Law of Restitution* (3rd ed. 1986), at p. 61, suggest that unjust enrichment is such a theme. However, unless "enrichment" is interpreted very broadly to extend beyond pecuniary claims, it does not explain all situations in which the constructive trust has been applied. As McClean, *supra* , at p. 168, states: "however satisfactory [the unjust enrichment theory] may be for other aspects of the law of restitution, it may not be wide enough to cover all types of constructive trust." McClean goes on to note the situation raised by this appeal: "In some cases, where such a trust is imposed the trustee may not have obtained any benefit at all; this could be the case, for example, when a person is held to be a trustee *de son tort* . A plaintiff may not always have suffered a loss." McClean concludes (at pp. 168-69): "Unjust enrichment may not, therefore, satisfactorily explain all types of restitutionary claims".

27 McClean, among others, regards the most satisfactory underpinning for unjust enrichment to be the concept of "good conscience" which lies at "the very foundation of equitable jurisdiction" (p. 169):

> "Safe conscience" and "natural justice and equity" were two of the criteria referred to by Lord Mansfield in *Moses v. MacFerlan* (1760), 2 Burr. 1005, 97 E.R. 676 (K.B.) in dealing with an action for money had and received, the prototype of a common law restitutionary claim. "Good conscience" has a sound basis in equity, some basis in common law, and is wide enough to encompass constructive trusts where the defendant has not obtained a benefit or where the plaintiff has not suffered a loss. It is, therefore, as good as, or perhaps a better, foundation for the law of restitution than is unjust enrichment.

28 Other scholars agree with McClean that good conscience may provide a useful way of unifying the different forms of constructive trust. Litman, *supra* , adverts to the "natural justice and equity" or "good conscience" trust "which operates as a remedy for wrongs which are broader in concept than unjust enrichment" and goes on to state that this may be viewed as the underpinning of the various institutional trusts as well as the unjust enrichment restitutionary constructive trust (at pp. 415-16).

29 Good conscience as the unifying concept underlying constructive trust has attracted the support of many jurists. Edmund Davies L.J. suggested that the concept of a "want of probity" in the person upon whom the constructive trust is imposed provides "a useful touchstone in considering circumstances said to give rise to constructive trusts": *Carl-Zeiss-Stiftung v. Herbert Smith & Co. (No. 2)*, [1968] 2 Ch. 276 (Eng. C.A.) . Cardozo J. similarly endorsed the unifying theme of good conscience in *Beatty v. Guggenheim Exploration Co.*, 122 N.E. 378 (U.S. 1919), at p. 380:

> A constructive trust is the formula through which the conscience of equity finds expression. *When property has been acquired in such circumstances that the holder of the legal title may not in good conscience retain the beneficial interest, equity converts him into a trustee* . [Emphasis added.]

  

30 Lord Denning M.R. expressed similar views in a series of cases applying the constructive trust as a remedy for wrong-doing: see *Neale v. Willis* (1968), 112 Sol. Jo. 521 (Eng. C.A.) ; *Binions v. Evans*, [1972] Ch. 359 (Eng. C.A.) ; *Hussey v. Palmer*, [1972] 1 W.L.R. 1286 (Eng. C.A.) . In *Binions* , referring to the statement by Cardozo J., *supra* , Denning M.R. stated that the court would impose a constructive trust "for the simple reason that it would be utterly inequitable for the plaintiffs to turn the defendant out contrary to the stipulation subject to which they took the premises" (p. 368). In *Hussey* , he said the following of the constructive trust (at pp. 1289-90): "By whatever name it is described, it is a trust imposed by law whenever justice and good conscience require it".

31 Many English scholars have questioned Lord Denning's expansive statements on constructive trust. Nevertheless, he is not alone: Bingham J. similarly referred to good conscience as the basis for equitable intervention in *Neste Oy v. Lloyd's Bank Ltd.*, [1983] 2 Lloyd's Rep. 658 (Eng. C.A.) .

32 The New Zealand Court of Appeal also appears to have accepted good conscience as the basis for imposing a constructive trust in *Elders Pastoral Ltd. v. Bank of New Zealand* (1989), 2 N.Z.L.R. 180 . Cooke P., at pp. 185-86, cited the following passage from Bingham J.'s reasons in *Neste Oy, supra* , at p. 666:

> Given the situation of [the defendants] when the last payment was received, any reasonable and honest directors of that company (or the actual directors had they known of it) would, I feel sure, have arranged for the repayment of that sum to the plaintiffs without hesitation or delay. It would have seemed little short of sharp practice for [the defendants] to take any benefit from the payment, and it would have seemed contrary to any ordinary notion of fairness that the general body of creditors should profit from the accident of a payment made at a time when there was bound to be a total failure of consideration. Of course it is true that insolvency always causes loss and perfect fairness is unattainable. The bank, and other creditors, have their legitimate claims. *It nonetheless seems to me that at the time of its receipt [the defendants] could not in good conscience retain this payment and that accordingly a constructive trust is to be inferred* . [Emphasis added.]

Cooke P. concluded simply (at p. 186): "I do not think that in conscience the stock agents can retain this money." *Elders* has been taken to stand for the proposition that even in the absence of a fiduciary relationship or unjust enrichment, conduct contrary to good conscience may give rise to a remedial constructive trust: see *Mogal Corp. v. Australasia Investment Co. (In Liquidation)* (1990), 3 N.Z.B.L.C. 101 , 783; J. Dixon, "The Remedial Constructive Trust Based on Unconscionability in the New Zealand Commercial Environment" (1995), 7 *Auck. U. L. Rev.* 147, at pp. 157-58. Although the Judicial Committee of the Privy Council rejected the creation of a constructive trust on grounds of good conscience in *Goldcorp Exchange Ltd., Re*, [1994] 2 All E.R. 806 (New Zealand P.C.) , the fact remains that good conscience is a theme underlying constructive trust from its earliest times.

33 Good conscience addresses not only fairness between the parties before the court, but the larger public concern of the courts to maintain the integrity of institutions like fiduciary relationships which the courts of equity supervised. As La Forest J. states in *Hodgkinson v. Simms*, [1994] 3 S.C.R. 377 (S.C.C.) , at p. 453:

> The law of fiduciary duties has always contained within it an element of deterrence. This can be seen as early as *Keech* in the passage cited *supra* ; see also *Canadian Aero, supra* , at pp. 607 and 610; *Canson, supra* , at p. 547, *per* McLachlin J. In this way the law is able to monitor a given relationship society views as socially useful while avoiding the necessity of formal regulation that may tend to hamper its social utility.

The constructive trust imposed for breach of fiduciary relationship thus serves not only to do the justice between the parties that good conscience requires, but to hold fiduciaries and people in positions of trust to the high standards of trust and probity that commercial and other social institutions require if they are to function effectively.

34 It thus emerges that a constructive trust may be imposed where good conscience so requires. The inquiry into good conscience is informed by the situations where constructive trusts have been recognized in the past. It is also informed by the dual reasons for which constructive trusts have traditionally been imposed: to do justice between the parties and to maintain the integrity of institutions dependent on trust-like relationships. Finally, it is informed by the absence of an indication that a

 

constructive trust would have an unfair or unjust effect on the defendant or third parties, matters which equity has always taken into account. Equitable remedies are flexible; their award is based on what is just in all the circumstances of the case.

35 Good conscience as a common concept unifying the various instances in which a constructive trust may be found has the disadvantage of being very general. But any concept capable of embracing the diverse circumstances in which a constructive trust may be imposed must, of necessity, be general. Particularity is found in the situations in which judges in the past have found constructive trusts. A judge faced with a claim for a constructive trust will have regard not merely to what might seem "fair" in a general sense, but to other situations where courts have found a constructive trust. The goal is but a reasoned, incremental development of the law on a case-by-case basis.

36 The situations which the judge may consider in deciding whether good conscience requires imposition of a constructive trust may be seen as falling into two general categories. The first category concerns property obtained by a wrongful act of the defendant, notably breach of fiduciary obligation or breach of duty of loyalty. The traditional English institutional trusts largely fall under but may not exhaust (at least in Canada) this category. The second category concerns situations where the defendant has not acted wrongfully in obtaining the property, but where he would be unjustly enriched to the plaintiff's detriment by being permitted to keep the property for himself. The two categories are not mutually exclusive. Often wrongful acquisition of property will be associated with unjust enrichment, and vice versa. However, either situation alone may be sufficient to justify imposition of a constructive trust.

37 In England the law has yet to formally recognize the remedial constructive trust for unjust enrichment, although many of Lord Denning's pronouncements pointed in this direction. The courts do, however, find constructive trusts in circumstances similar to those at bar. Equity traditionally recognized the appropriateness of a constructive trust for breach of duty of loyalty simpliciter. The English law is summarized by Goff and Jones, *The Law of Restitution, supra* , at p. 643:

> A fiduciary may abuse his position of trust by diverting a contract, purchase or other opportunity from his beneficiary to himself. If he does so, he is deemed to hold that contract, purchase, or opportunity on trust for the beneficiary.

P. Birks, *An Introduction to the Law of Restitution* (1985) (at pp. 330; 338-43) agrees. He suggests that cases of conflict of interest not infrequently may give rise to constructive trust, absent unjust enrichment. Birks distinguishes between anti-enrichment wrongs and anti-harm wrongs (at p. 340). A fiduciary acting in conflict of interest represents a risk of actual or potential harm, even though his misconduct may not always enrich him. A constructive trust may accordingly be ordered.

38 Both categories of constructive trust are recognized in the United States; although unjust enrichment is sometimes cited as the rationale for the constructive trust in the U.S., in fact its courts recognize the availability of constructive trust to require the return of property acquired by wrongful act absent unjust enrichment of the defendant and reciprocal deprivation of the plaintiff. Thus the authors of *Scott on Trusts* (3rd ed. 1967), vol. V, at p. 3410, state that the constructive trust "is available where property is obtained by mistake or by fraud or by other wrong". Or as Cardozo C.J. put it, "[a] constructive trust is, then, the remedial device through which preference of self is made subordinate to loyalty to others": *Meinhard v. Salmon* (1928), 164 N.E. 545 (U.S. 1928), at p. 548, cited in *Scott on Trusts, supra* , at p. 3412. *Scott on Trusts, supra* , at p. 3418, states that there are cases "in which a constructive trust is enforced against a defendant, although the loss to the plaintiff is less than the gain to the defendant or, indeed, where there is no loss to the plaintiff".

39 Canadian courts also recognize the availability of constructive trusts for both wrongful acquisition of property and unjust enrichment. Applying the English law, they have long found constructive trusts as a consequence of wrongful acquisition of property, for example by fraud or breach of fiduciary duty. More recently, Canadian courts have recognized the availability of the American-style remedial constructive trust in cases of unjust enrichment: *Becker v. Pettkus, supra* . However, since *Becker v. Pettkus* Canadian courts have continued to find constructive trusts where property has been wrongfully acquired, even in the absence of unjust enrichment. While such cases appear infrequently since few choose to litigate absent pecuniary loss, they are not rare.

  

40 Litman, *supra* , at p. 416, notes that in "the post-*Pettkus v. Becker* era there are numerous cases where courts have used the institutional constructive trust without adverting to or relying on unjust enrichment". The imposition of a constructive trust in these cases is justified not on grounds of unjust enrichment, but on the ground that the defendant's wrongful act requires him to restore the property thus obtained to the plaintiff.

41 Thus in *Ontario (Wheat Producers' Marketing Board) v. Royal Bank* (1984), 9 D.L.R. (4th) 729 (Ont. C.A.) , a constructive trust was imposed on a bank which received money with actual knowledge that it belonged to someone other than the depositor.

42 Again, in *MacMillan Bloedel Ltd. v. Binstead* (1983), 14 E.T.R. 269 (B.C. S.C.) , a constructive trust was imposed on individuals who knowingly participated in a breach of fiduciary duty despite a finding that unjust enrichment would not warrant the imposition of a trust because the plaintiff company could not be said to have suffered a loss or deprivation since its own policy precluded it from receiving the profits. Dohm J. (as he then was) stated that the constructive trust was required "not to balance the equities but to ensure that trustees and fiduciaries remain faithful and that those who assist them in the breaches of their duty are called to account" (p. 302).

43 I conclude that in Canada, under the broad umbrella of good conscience, constructive trusts are recognized both for wrongful acts like fraud and breach of duty of loyalty, as well as to remedy unjust enrichment and corresponding deprivation. While cases often involve both a wrongful act and unjust enrichment, constructive trusts may be imposed on either ground: where there is a wrongful act but no unjust enrichment and corresponding deprivation; or where there is an unconscionable unjust enrichment in the absence of a wrongful act, as in *Becker v. Pettkus, supra* . Within these two broad categories, there is room for the law of constructive trust to develop and for greater precision to be attained, as time and experience may dictate.

44 The process suggested is aptly summarized by McClean, *supra* , at pp. 167-70:

> The law [of constructive trust] may now be at a stage where it can distill from the specific examples a few general principles, and then, by analogy to the specific examples and within the ambit of the general principle, create new heads of liability. That, it is suggested, is not asking the courts to embark on too dangerous a task, or indeed on a novel task. In large measure it is the way that the common law has always developed.

**VII**

45 In *Becker v. Pettkus, supra* , this Court explored the prerequisites for a constructive trust based on unjust enrichment. This case requires us to explore the prerequisites for a constructive trust based on wrongful conduct. Extrapolating from the cases where courts of equity have imposed constructive trusts for wrongful conduct, and from a discussion of the criteria considered in an essay by Roy Goode, "Property and Unjust Enrichment", in Andrew Burrows ed., *Essays on the Law of Restitution* (1991), I would identify four conditions which generally should be satisfied:

> (1) The defendant must have been under an equitable obligation, that is, an obligation of the type that courts of equity have enforced, in relation to the activities giving rise to the assets in his hands;
>
> (2) The assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant in breach of his equitable obligation to the plaintiff;
>
> (3) The plaintiff must show a legitimate reason for seeking a proprietary remedy, either personal or related to the need to ensure that others like the defendant remain faithful to their duties and;
>
> (4) There must be no factors which would render imposition of a constructive trust unjust in all the circumstances of the case; e.g., the interests of intervening creditors must be protected.

**VIII**

  

46 Applying this test to the case before us, I conclude that Mr. Korkontzilas' breach of his duty of loyalty sufficed to engage the conscience of the court and support a finding of constructive trust for the following reasons.

47 First, Mr. Korkontzilas was under an equitable obligation in relation to the property at issue. His failure to pass on to his client the information he obtained on his client's behalf as to the price the vendor would accept on the property and his use of that information to purchase the property instead for himself constituted breach of his equitable duty of loyalty. He allowed his own interests to conflict with those of his client. He acquired the property wrongfully, in flagrant and inexcusable breach of his duty of loyalty to Mr. Soulos. This is the sort of situation which courts of equity, in Canada and elsewhere, have traditionally treated as involving an equitable duty, breach of which may give rise to a constructive trust, even in the absence of unjust enrichment.

48 Second, the assets in the hands of Mr. Korkontzilas resulted from his agency activities in breach of his equitable obligation to the plaintiff. His acquisition of the property was a direct result of his breach of his duty of loyalty to his client, Mr. Soulos.

49 Third, while Mr. Korkontzilas was not monetarily enriched by his wrongful acquisition of the property, ample reasons exist for equity to impose a constructive trust. Mr. Soulos argues that a constructive trust is required to remedy the deprivation he suffered because of his continuing desire, albeit for non-monetary reasons, to own the particular property in question. No less is required, he asserts, to return the parties to the position they would have been in had the breach not occurred. That alone, in my opinion, would be sufficient to persuade a court of equity that the proper remedy for Mr. Korkontzilas' wrongful acquisition of the property is an order that he is bound as a constructive trustee to convey the property to Mr. Soulos.

50 But there is more. I agree with the Court of Appeal that a constructive trust is required in cases such as this to ensure that agents and others in positions of trust remain faithful to their duty of loyalty: see *Hodgkinson v. Simms, supra, per* La Forest J. If real estate agents are permitted to retain properties which they acquire for themselves in breach of a duty of loyalty to their clients provided they pay market value, the trust and confidence which underpins the institution of real estate brokerage will be undermined. The message will be clear: real estate agents may breach their duties to their clients and the courts will do nothing about it, unless the client can show that the real estate agent made a profit. This will not do. Courts of equity have always been concerned to keep the person who acts on behalf of others to his ethical mark; this Court should continue in the same path.

51 I come finally to the question of whether there are factors which would make imposition of a constructive trust unjust in this case. In my view, there are none. No third parties would suffer from an order requiring Mr. Korkontzilas to convey the property to Mr. Soulos. Nor would Mr. Korkontzilas be treated unfairly. Mr. Soulos is content to make all necessary financial adjustments, including indemnification for the loss Mr. Korkontszilas has sustained during the years he has held the property.

52 I conclude that a constructive trust should be imposed. I would dismiss the appeal and confirm the order of the Court of Appeal that the appellants convey the property to the respondent, subject to appropriate adjustments. The respondent is entitled to costs throughout.

***Sopinka J.*** **(dissenting) (Iacobucci J. concurring):**

53 I have read the reasons of my colleague McLachlin J. While I agree with her conclusion that a breach of a fiduciary duty was made out herein, I disagree with her analysis concerning the appropriate remedy. In my view, she errs in upholding the decision of the majority of the Court of Appeal to overturn the trial judge and impose a constructive trust over the property in question. There are two broad reasons for my conclusion. First, the order of a constructive trust is a discretionary matter and, as such, is entitled to appellate deference. Given that the trial judge did not err in principle in declining to make such an order, appellate courts should not interfere with the exercise of his discretion. Second, even if appellate review were appropriate in the present case, a constructive trust as a remedy is not available where there has been no unjust enrichment. The main source of my disagreement with McLachlin J. arises in consideration of the second point, but in order to address the reasons of the majority in the court below as well, I will consider both of these issues in turn.

**Standard of Review and the Exercise of Discretion**

  

54 It is a matter of settled law that appellate courts should generally not interfere with orders exercised within a trial judge's discretion. Only if the discretion has been exercised on the basis of an erroneous principle should the order be overturned on appeal: see *Donkin v. Bugoy*, [1985] 2 S.C.R. 85 (S.C.C.) . As acknowledged by the majority in the Court of Appeal ((1995), 25 O.R. (3d) 257 (Ont. C.A.) , at p. 259), the decision to order a constructive trust is a matter of discretion. In *International Corona Resources Ltd. v. LAC Minerals Ltd.*, [1989] 2 S.C.R. 574 (S.C.C.) , the majority held that the order of a constructive trust in response to a breach of a fiduciary duty would depend on all the circumstances. La Forest J. stated at p. 674:

> In the case at hand, the restitutionary claim has been made out. The Court can award either a proprietary remedy, namely that Lac hand over the Williams property, or award a personal remedy, namely a monetary award. ... [A constructive trust] is but one remedy, and will only be imposed in appropriate circumstances.

The discretionary approach to constructive trusts is also consistent with the approach to equitable remedies generally: see *Canson Enterprises Ltd. v. Boughton & Co.*, [1991] 3 S.C.R. 534 (S.C.C.) , at p. 585.

55 Given that ordering a constructive trust is a discretionary matter, it is necessary to show an error in principle on the part of the trial judge in order to overturn the judge's decision not to order such a remedy. In my view, the trial judge committed no such error.

56 The majority of the Court of Appeal apparently found that the trial judge erred in failing to consider the moral blameworthiness of the appellants' actions. Similarly, McLachlin J. would hold that a constructive trust was appropriate in the present case simply because of considerations of "good conscience". In my view, the trial judge considered the moral quality of the appellants' actions and thus there is no room for appellate intervention on this ground. He stated ((1991), 4 O.R. (3d) 51 (Ont. Gen. Div.) , at p. 69) that, while "[n]o doubt the maintenance of commercial morality is an element of public policy and a legitimate concern of the court", morality should generally not invite the intervention of the court, except where it is required in aid of enforcing some legal right. Put another way, in my view the trial judge was of the opinion that where there is otherwise no justification for ordering a constructive trust or any other remedy, the morality of the act will not alone justify such an order, which statement of the law is in my view correct.

57 The majority of the Court of Appeal stated (at pp. 259-60) that the principles set out by the trial judge may be applicable where there are alternative remedies, but are questionable where only one remedy is available, as in the present case. I do not accept this contention. If a constructive trust is held to be inappropriate where there are a variety of remedies available, I cannot understand the principle behind the conclusion that such a remedy may be appropriate where it is the only remedy available. The trial judge has a discretion to order a constructive trust, or not to order one, and this discretion should not be affected by the number of available remedies. In the present case, the plaintiff withdrew his claim for damages. While compensatory damages were unavailable since the plaintiff suffered no pecuniary loss (which I will discuss further below in assessing whether a constructive trust could have been ordered), the plaintiff could have sought exemplary damages — his decision not to do so should not bind the trial judge's discretion with respect to the order of a constructive trust.

58 The trial judge put significant emphasis on the absence of pecuniary gains in concluding that he would not order a constructive trust. For the reasons which I set out in detail below, I am of the opinion that the trial judge was correct in this regard. On the other hand, the majority of the Court of Appeal and McLachlin J. hold that the trial judge erred in improperly appreciating the deterrence role of a constructive trust in the present case. In my view, consideration of deterrence fails to disclose any error in principle on the part of the trial judge. Deterrence, like the morality of the acts in question, may be relevant to the exercise of discretion with respect to the remedy for a breach of a fiduciary duty (see, e.g., *Hodgkinson v. Simms*, [1994] 3 S.C.R. 377 (S.C.C.) , at pp. 421 and 453), but the trial judge in the present case did not fail to consider deterrence in deciding whether to order a constructive trust. As noted above, he stated that while "maintenance of commercial morality is ... a legitimate concern of the court" (p. 69), it would not alone justify ordering a remedy in the present case. In my view, his mention of the "maintenance of commercial morality" indicates that the judge considered deterrence, but held that it alone could not justify a remedy in the present case. Thus, even if failure to consider deterrence could be considered an error in principle, the trial judge in the present case did not so err.

  

59 In my view, the trial judge committed no error in principle which could justify a decision to set aside his judgment and order a constructive trust. Even if the trial judge did commit some error in principle, however, in my view the remedy of a constructive trust was not available on the facts of the present case. That is, even if no deference is owed to the trial judge, the majority below erred in ordering a constructive trust and the appeal should be allowed. The following are my reasons for this conclusion.

**Unjust Enrichment and the Availability of a Constructive Trust**

60 McLachlin J. would hold that there are two general circumstances in which a constructive trust may be ordered: where there has been unjust enrichment and where there has been an absence of "good conscience". While unjust enrichment and the absence of "good conscience" may both be present in a particular case, McLachlin J. is of the view that either element individually is sufficient to order a constructive trust. By failing to consider the "good conscience" ground on its own, McLachlin J. finds that the trial judge erred. I respectfully disagree with this finding. In my view, recent case law in this Court is very clear that a constructive trust may *only* be ordered where there has been an unjust enrichment. For example, passages in *LAC Minerals, supra* , set out the circumstances in which an order of a constructive trust might be appropriate. In my opinion, it is clear from that decision that a constructive trust is not available as a remedy unless there has been an unjust enrichment. La Forest J. stated at pp. 673-74:

> This Court has recently had occasion to address the circumstances in which a constructive trust will be imposed in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426 . There, the Chief Justice discussed the development of the constructive trust over 200 years from its original use in the context of fiduciary relationships, through to *Pettkus v. Becker* , [[1980] 2 S.C.R. 834 ], where the Court moved to the modern approach with the constructive trust as a remedy for unjust enrichment. He identified that *Pettkus v. Becker, supra* , set out a two-step approach. *First, the Court determines whether a claim for unjust enrichment is established, and then, secondly, examines whether in the circumstances a constructive trust is the appropriate remedy to redress that unjust enrichment* . In *Hunter Engineering Co. v. Syncrude Canada Ltd.* , a constructive trust was refused, not on the basis that it would not have been available between the parties (though in my view it may not have been appropriate), but rather on the basis that the claim for unjust enrichment had not been made out, so no remedial question arose.
>
> In the case at hand, the restitutionary claim has been made out. The Court can award either a proprietary remedy, namely that Lac hand over the Williams property, or award a personal remedy, namely a monetary award. While, as the Chief Justice observed, "*The principle of unjust enrichment lies at the heart of the constructive trust* ": see *Pettkus v. Becker* , at p. 847, the converse is not true. The constructive trust does not lie at the heart of the law of restitution. [Emphasis added.]

La Forest J. added at p. 678:

> *Much of the difficulty disappears if it is recognized that in this context the issue of the appropriate remedy only arises once a valid restitutionary claim has been made out* . The constructive trust awards a right in property, but that right can only arise once a right to relief has been established. [Emphasis added.]

61 In *Brissette v. Westbury Life Insurance Co.*, [1992] 3 S.C.R. 87 (S.C.C.) , the majority cited some of the passages above from *Lac* with approval and held at p. 96 that, "[t]he requirement of unjust enrichment is fundamental to the use of a constructive trust."

62 Citing only *Pettkus, supra* , specifically, McLachlin J. states at para. 21 that it and other cases should not be taken to expunge from Canadian law the constructive trust in circumstances where there has not been unjust enrichment. With respect, I do not see how statements such as "The requirement of unjust enrichment is fundamental to the use of a constructive trust" could do anything but expunge from Canadian law the use of constructive trusts where there has been no enrichment. Unjust enrichment has been repeatedly stated to be a *requirement* for a constructive trust; thus to order one where there has been no unjust enrichment would clearly depart from settled law.

  

63 Even aside from the case law, in my view, the unavailability of a constructive trust in the absence of unjust enrichment is consistent with the constructive trust's remedial role. The respondent submitted that if no remedy is available in the present case, there would inappropriately be a right without a remedy. I disagree. Clearly, the beneficiary has a right to have the fiduciary adhere to its duty, and *if damages are suffered* , the beneficiary has a right to a remedy. In my view, this is analogous to remedial principles found elsewhere in the private law. Even if a duty is owed and breached in other legal contexts, there is no remedy unless a loss has been suffered. I may owe a duty to my neighbour to shovel snow off my walk, and I may breach that duty, but if my neighbour does not suffer any loss because of the breached duty, there is no tort and no remedy. Similarly, I may have a contractual duty to supply goods at a specific date for a specific price, but if I do not and the other party is able to purchase the same goods at the contract price at the same time and place, the party has not suffered damage and no remedy is available. It is entirely consistent with these rules to state that even if a fiduciary breaches a duty, if the fiduciary is not unjustly enriched by the breach, there is no remedy.

64 Remedial principles generally thus support the rule against a constructive trust where there has been no unjust enrichment. The rule is also supported, in my view, by specific consideration of the principles governing constructive trusts set out in *LAC Minerals* . In *LAC Minerals* , La Forest J. stated that, even where there has been unjust enrichment, the constructive trust will be an exceptional remedy; the usual approach would be to award damages. He stated at p. 678:

> In the vast majority of cases a constructive trust will not be the appropriate remedy. Thus, in *Hunter Engineering Co. v. Syncrude Canada Ltd., supra* , had the restitutionary claim been made out, there would have been no reason to award a constructive trust, as the plaintiff's claim could have been satisfied simply by a personal monetary award; *a constructive trust should only be awarded if there is reason to grant to the plaintiff the additional rights that flow from recognition of a right of property* . [Emphasis added.]

65 La Forest J. thus held that generally an aggrieved beneficiary will only be entitled to damages, not to the property itself. This implies that the beneficiary does not generally have a right to the property in question, but rather has a right to receive the value of the gains resulting from the acquisition of the property. Following this reasoning, if the value of the gains is zero, that is, there is no unjust enrichment, the beneficiary will not have a right to a remedy. Consequently, where there has been no unjust enrichment, there is no right to a constructive trust or any other remedy.

66 While, in my view, recent decisions of this Court and the principles underlying them settle the matter, McLachlin J. cites other Canadian case law in concluding that constructive trusts may be ordered even where there has not been unjust enrichment. She cites three lower court decisions which she claims involved the award of a constructive trust absent unjust enrichment. With respect, I do not read any one of these cases as supporting her claim. An unjust enrichment exists where there has been an enrichment of the defendant, a corresponding deprivation experienced by the plaintiff and the absence of any juristic reason for the enrichment: *Becker v. Pettkus*, [1980] 2 S.C.R. 834 (S.C.C.) ; *Syncrude Canada Ltd. v. Hunter Engineering Co.*, [1989] 1 S.C.R. 426 (S.C.C.) . McLachlin J. fails to cite a case where a remedial constructive trust was ordered absent such an enrichment.

67 In *Ontario (Wheat Producers' Marketing Board) v. Royal Bank* (1984), 9 D.L.R. (4th) 729 (Ont. C.A.) , a constructive trust was imposed on a bank which received money with actual knowledge that it belonged to someone other than the depositor. The bank was a secured creditor of the depositor, which depositor was in financial difficulty at the time of the deposits. Clearly, this case involved an unjust enrichment: the bank benefitted by gaining rights over the deposited money, as well as by increasing the likelihood of repayment of the depositor's credit; the plaintiff (a corporation whose agent, the depositor, breached his fiduciary obligations) was deprived of its right to its money; and there was no juristic reason for the enrichment. Thus, the order of a constructive trust responded to an unjust enrichment, whether or not the court adverted to such doctrine.

68 *MacMillan Bloedel Ltd. v. Binstead* (1983), 14 E.T.R. 269 (B.C. S.C.) is also, in my view, a case of unjust enrichment. In this case, a fiduciary to a corporation breached his duty by engaging in self-dealing without disclosing his interest. A constructive trust was imposed over the secret profits even though the plaintiff organization, because of its internal policy, could not have realized the profits itself. While the fiduciary was plainly enriched, the trial judge and McLachlin J. conclude that since the plaintiff could not have realized the profits, there was no "corresponding deprivation" and therefore no unjust enrichment.

  

69 I disagree with McLachlin J. that there was no unjust enrichment in *MacMillan Bloedel Ltd.* First of all, courts have consistently treated fiduciaries' profits explicitly as unjust enrichment, whether or not the beneficiary could have earned the profits itself. For example, in *Reading v. R.*, [1948] 2 All E.R. 27 (Eng. K.B.) , aff'd [1949] 2 All E.R. 68 (Eng. C.A.) , aff'd [1951] 1 All E.R. 617 (Eng. H.L.) , Denning J. stated at p. 28:

> It matters not that the master has not lost any profit, nor suffered any damage, nor does it matter that the master could not have done the act himself. If the servant has *unjustly enriched himself* by virtue of his service without his master's sanction, the law says that he ought not to be allowed to keep the money. ... [Emphasis added.]

In *Canadian Aero Service Ltd. v. O'Malley* (1973), [1974] S.C.R. 592 (S.C.C.) , at pp. 621-22, Laskin J., as he then was, stated:

> Liability of O'Malley and Zarzycki for breach of fiduciary duty *does not depend upon proof by Canaero that, but for their intervention, it would have obtained the Guyana contract* ; nor is it a condition of recovery of damages that Canaero establish what its profit would have been or what it has lost by failing to realize the corporate opportunity in question. It is entitled to compel the faithless fiduciaries to answer for their default according to their gain. Whether the damages awarded here be viewed as an accounting of profits or, what amounts to the same thing, *as based on unjust enrichment* , I would not interfere with the quantum. [Emphasis added.]

*Reading* and *Canadian Aero Service Ltd.* are clear: the characterization of the profits earned by a fiduciary in breach of duty is one of unjust enrichment, whether or not the corporation could have earned the profits itself. Thus, *MacMillan Bloedel Ltd.* involved unjust enrichment, contrary to McLachlin J.'s assertion.

70 I wish to add that the treatment of the profits as unjust enrichment in *Reading, O'Malley* , and *MacMillan Bloedel Ltd.* is not inconsistent with the general rules governing unjust enrichment. The plaintiff in each case had a right to have the fiduciary adhere to his duty. When the defendant breached that duty, the profits earned as a result of that breach are essentially treated in equity as belonging to the corporation, whether or not the corporation could have earned those profits in the absence of the breach. As an example of the proprietary analogy, Denning M.R. stated at p. 856 in *Phipps v. Boardman*, [1965] 1 All E.R. 849 (Eng. C.A.) , aff'd [1966] 3 All E.R. 721 (U.K. H.L.) , that:

> [W]ith *information or knowledge* which he has been employed by his principal to collect or discover, *or which he has otherwise acquired* , for the use of his principal, then again if he turns it to his own use, so as to make a profit by means of it for himself, *he is accountable ... for such information or knowledge is the property of his principal, just as much as an invention is* . ... [Italics in original; underlining added.]

71 Thus, in *MacMillan Bloedel Ltd.* , the retention of the profits by the fiduciary would have deprived the corporation of its right to the profits. The deprivation is represented by the monies obtained by the fiduciary as a result of infringing the rights of the plaintiff. In order for there not to have been deprivation and unjust enrichment in circumstances otherwise similar to *MacMillan Bloedel Ltd.* , the self-dealing could not have resulted in any secret profits — if a remedy were awarded in a case without profit, thus no enrichment nor deprivation, McLachlin J. could well point to the case for support. Given that there *was* profit in *MacMillan Bloedel Ltd.* , however, there was unjust enrichment which justified the order of a constructive trust, whether or not the court explicitly relied upon unjust enrichment.

72 In summary, McLachlin J. fails to refer to a single Canadian case where a constructive trust was ordered despite the absence of unjust enrichment. Given this conclusion and given that recent cases of this Court unambiguously foreclose the possibility of ordering a constructive trust in the absence of unjust enrichment, in my view McLachlin J. is in error in concluding that a constructive trust may be ordered in the absence of unjust enrichment.

73 Aside from Canadian case law, McLachlin J. attempts to rely on various scholars and foreign case law as providing support for her conclusion. Because of the clear statement of the law recently set out by this Court, in my view the scholarly writings and foreign cases are only useful insofar as the policy they set out suggests that the law in Canada should be modified. I will therefore simply address the policy upon which McLachlin J. relies, rather than each case and each article she cites.

 

74 Simply put, McLachlin J., reasoning similarly to the majority below, concludes that to fail to permit the order of a constructive trust where there has been a breach of a fiduciary duty, but no unjust enrichment, would inadequately safeguard the integrity of fiduciary relationships. She says at para. 33 that ordering a constructive trust simply on the basis of "good conscience",

> addresses not only fairness between the parties before the court, but the larger public concern of the courts to maintain the integrity of institutions like fiduciary relationships which the courts of equity supervised. ... The constructive trust imposed for breach of fiduciary relationship, thus serves not only to do the justice between the parties that good conscience requires, but to hold fiduciaries and people in positions of trust to the high standards of trust and probity that commercial and other social institutions require if they are to function effectively.

According to McLachlin J., then, deterrence of faithless fiduciaries requires the availability of constructive trust as a remedy even where there has been no unjust enrichment.

75 In my view, deterrence is not a factor which suggests modifying the law of Canada and permitting the order of a constructive trust even where there has been no unjust enrichment. As noted above, despite considerations of deterrence, it is true throughout the private law that remedies are typically unavailable in the absence of a loss. Courts have not, because of concern about protecting the integrity of these duties, held it to be necessary where a tort duty, or a contractual duty, has been breached to order remedies even where no loss resulted. I fail to see what distinguishes the role of fiduciary duties from the very important societal roles played by other legal duties which would justify their exceptional treatment with respect to remedy.

76 In any event, the unavailability of a constructive trust in cases where there is no unjust enrichment does not, in my opinion, have any significant effect on deterring unfaithful fiduciaries and protecting the integrity of fiduciary relationships. First, if deterrence were deemed to be particularly important in a case, the plaintiff may seek and the trial judge may award exemplary damages; a constructive trust is not necessary to preserve the integrity of the relationship, even if this integrity were of particular concern in a given case. The fact that exemplary damages were not sought in the present case should not compel this Court to order a constructive trust in their place. Second, even if a remedy were unavailable in the absence of unjust enrichment, which is not true given exemplary damages, deterrence is not precluded. Taking a case similar to the present appeal, while an unscrupulous fiduciary would know that he or she would not be compelled to give up the surreptitiously obtained property if there were no gains in value to the property, he or she must also reckon with the possibility that if there *were* gains in value, and therefore unjust enrichment, he or she *would* be compelled to pay damages or possibly give up the property. Thus, if the fiduciary were motivated to breach his or her duty because of the prospect of pecuniary gains, which would, I imagine, be the typical, if not the exclusive, motive for such a breach, not ordering a constructive trust where there have been no pecuniary gains does not affect deterrence. I therefore disagree with McLachlin J. that deterrence suggests that a constructive trust should be available even where there is no unjust enrichment.

77 As is clear, I cannot agree with McLachlin J. that a constructive trust could be ordered, and indeed should have been ordered, in the present case even if there was no unjust enrichment. In order to decide whether such a remedy could be ordered, in my view, it must be decided whether there was unjust enrichment in the present case.

**Was There Unjust Enrichment?**

78 In my opinion, there was no enrichment and therefore no unjust enrichment in the present case. It is first of all plain that there were no pecuniary advantages accruing to the appellants from the purchase of the property. The trial judge stated (at p. 68):

> I now consider the facts of the case at bar. The nature of the duty and of the breach have already been discussed. At an interlocutory stage, the plaintiff abandoned any claim for damages. *This step involved no sacrifice because the plaintiff could not have proved any* . [Emphasis added.]

Any enrichment from the purchase of the property was not pecuniary, which would suggest that there has in fact been no enrichment and therefore no unjust enrichment.

  

79 It could, perhaps, be argued that if the property were unique or otherwise difficult to value, the defendant's pecuniary gains may not represent the enrichment of the defendant or the deprivation of the plaintiff. Analogizing to the award of specific performance in contract, where property that is the subject of a contract is unique or otherwise difficult to value, and the contract is breached, it may be held that monetary damages are inadequate and thus a remedy of specific performance must be ordered to compensate the plaintiff adequately. In such cases, pecuniary damages may not represent the loss to the plaintiff or the gain to the defendant from the breach. Thus, perhaps, an enrichment could be found in the absence of a change in market price if the property were unique or otherwise difficult to value.

80 Whether or not such considerations could be relevant to a finding of an enrichment, the property in question was not found to be unique or otherwise difficult to value in a manner relevant to the remedy. The trial judge noted that the respondent had asserted that the property in question had special value to him given its tenant, a bank, and the significance of being a landlord to a bank in the Greek community. The trial judge (at p. 69) held that such a factor should not be taken into account any more than personal attachment in an eminent domain case. In other words, while there may have been personal motivation for the purchase, this was not relevant to an assessment of the value of the property. This indicates, in my view, that the trial judge did not view the property to be unique in a manner meaningful to the remedial analysis. Such a conclusion is plain in the trial judge's analysis of *Lee v. Chow* (1990), 12 R.P.R. (2d) 217 (Ont. H.C.) . In *Lee* , a constructive trust was declared in a property that had been purchased surreptitiously by an agent in a situation similar to the present case. The trial judge in the instant appeal distinguished *Lee* in the following way (at p. 70):

> [The circumstances in *Lee* ] included the following: a degree of dependence by the plaintiff which, in my view, is lacking in the case at bar; that it was a residential property meeting the specific requirements of the plaintiff, *rather than a commercial property having value only as an investment* ; and that it appeared probable that the acquisition price represented a bargain, while the property at issue in the case at bar did not. [Emphasis added.]

In *Lee* there were pecuniary gains, thus an enrichment, and the property had unique qualities which helped justify a constructive trust. In the present case there were no pecuniary gains, and the trial judge did not find any meaningful non-pecuniary advantages associated with the property — the property had value "only as an investment". In my view, given the absence of both pecuniary and non-pecuniary advantages from the property, there was no enrichment and therefore no unjust enrichment.

81 In the absence of unjust enrichment, in my view the trial judge was correct not to order the remedy sought, a constructive trust. The trial judge stated (at p. 69):

> A constructive trust was deemed appropriate in *Lac Minerals, supra* , because damages were deemed to be unsatisfactory. It would be anomalous to declare a constructive trust, in effect, because a remedy in damages is unsatisfactory, the plaintiff having suffered none.

The trial judge, in the absence of pecuniary damages which might have indicated unjust enrichment, declined to order a constructive trust. Neither the majority of the Court of Appeal nor McLachlin J. raise an error in principle in the trial judge's reasons; indeed, in my view they err in concluding that a constructive trust is available in the present case. Even if the trial judge ignored factors such as the moral quality of the defendants' acts and deterrence, which he did not, and even if this could be construed as an error in principle, the factors to be considered in ordering a constructive trust only become relevant at the second stage of the inquiry when it is decided what remedy is appropriate. Unless unjust enrichment is made out at the first stage of the inquiry, there is no need to consider the factors relevant to ordering a constructive trust. The majority of the Court of Appeal erred in interfering with the trial judge's discretion and in deciding that a constructive trust may be ordered in the absence of unjust enrichment.

**Conclusion**

82 Since the trial judge did not err in not ordering a constructive trust, but rather the majority of the Court of Appeal did in ordering one, I would allow the appeal, set aside the judgment of the Court of Appeal and reinstate the judgment of the trial judge. In the circumstances, I would not award costs to the appellants either here or in the Court of Appeal.

 

*Appeal dismissed.*

*Pourvoi rejeté.*

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