Court File No. CV-23-00696017-CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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 LOYALTYONE, CO.

Applicant

BOOK OF AUTHORITIES OF THE MONITOR

(Motion Returnable June 13 and 14, 2024)

May 28, 2024

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AND TO: **THE SERVICE LIST**

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1

1976 CarswellBC 63
British Columbia Supreme Court, In Bankruptcy

Challmie, Re

1976 CarswellBC 63, 22 C.B.R. (N.S.) 78

Re Challmie

Meredith J. [in Chambers]

Judgment: January 30, 1976
Docket: Vancouver No. B.C. 87138-S 497-74

Counsel: *D. A. Race*, for applicants Primex Investments Ltd. and B. J. Wood Roofmart Ltd.
P. A. Spencer, for respondent.

Subject: Corporate and Commercial; Insolvency

***Meredith J.*:**

1 The applicants, now standing in place of the trustee in bankruptcy, move to set aside a mortgage of the interest of the bankrupt in a home standing in the joint names of the bankrupt and his wife. The mortgage, dated 29th August 1974, was made in favour of Dori Blinder, the wife's brother. The applicants say that the mortgage is to be deemed preferential and thus fraudulent and void under s. 73 of the Bankruptcy Act, R.S.C. 1970, c. B-3.

2 The bankrupt, on the other hand, launches a concurrent motion for his discharge pursuant to s. 139 of the Bankruptcy Act. The applicants, invoking s. 143(1) of the Act, oppose the discharge. They say first that the assets of the bankrupt are not of a value equal to 50 cents in the dollar on the amount of his unsecured liabilities and second that the bankrupt, within three months preceding the date of his bankruptcy, when unable to pay his debts when they became due, gave an undue preference to one of his creditors.

3 Section 73 of the Bankruptcy Act, upon which the applicants rely, reads:

> 73. (1) Every conveyance or transfer of property or charge thereon made, every payment made, every obligation incurred, and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving such creditor a preference over the other creditors shall, if the person making, incurring, taking, paying or suffering the same becomes bankrupt within three months after the date of making, incurring, taking, paying or suffering the same, be deemed fraudulent and void as against the trustee in the bankruptcy.
>
> (2) Where any such conveyance, transfer, payment, obligation or judicial proceeding has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed *prima facie* to have been made, incurred, taken, paid or suffered with a view to giving such creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be receivable or avail to support such transaction.
>
> (3) For the purposes of this section, the expression 'creditor' includes a surety or guarantor for the debt due to such creditor.

4 It will be seen that to invoke the presumption of preference decreed by subs. (2) the applicants must show that the bankrupt was insolvent at the date of the mortgage, that the effect of the mortgage was to confer a preference over other credi tors, and that the bankruptcy took place within three months of the creation of the mortgage. The only question raised as to these requirements is whether the bankrupt was insolvent when the mortgage was given. The bankrupt strongly contends in addition that the presumption that he gave the mortgage with a view to preferring his brother-in-law is, on the evidence, rebutted.

5 An "insolvent person" is defined under s. 2 of the Bankruptcy Act as follows:

> 'insolvent person' means a person who is not bankrupt and who resides or carries on business in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and
>
> (*a*) who is for any reason unable to meet his obligations as they generally become due, or
>
> (*b*) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (*c*) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due.

6 The bankrupt deposes that several years before the bankruptcy he became active in the building and construction industry through a company called Image Developments and Enterprises Ltd. He put a good deal of his own money, and that of others, into the company and went so far as to mortgage his home to provide the company funds. The company operations were not a success, partly, it is suggested, because of the improvidence of his associates. The bankrupt says that he was importuned to sign a personal guarantee of repayment of $20,000 by way of loan to the company from the applicant Primex, and to guarantee the payment to the applicant B. J. Wood Roofmart for materials supplied by it to the company. At the date of the bankruptcy the obligation to B. J. Wood amounted to about $14,000.

7 The circumstances under which the Blinder mortgage was executed, and events immediately preceding the bankruptcy, are described thus in the affidavit of the bankrupt:

> (12) THAT my brother-in-law, one Dori Blinder visited me in approximately July of 1974, having previously loaned me over $9,000.00, and advised that because he had not been receiving the payments owing for interest on such money, he would require a third mortgage to be registered against my home. Initially, I protested as I was concerned it would reduce my ability to continue to obtain financing and stay in business, however, near the later part of August the said Dori Blinder threatened legal action, including a suit, unless I provided such a mortgage as was finally registered against the property on the 27th of August, 1974.
>
> (13) THAT subsequent to, and in return for the registration of that mortgage, I received further loans from the said Dori Blinder as follows:

August 27, 1974	$ 2,199.00
August 30, 1974	2,000.00
September 4, 1974	2,100.00
September 7, 1974	2,100.00
September 11, 1974	2,000.00

	$ 10,339.00

> At the same time, because of a little revenue being received by Image, I agreed to and did work part-time outside the Company's operations for Musgrove Ford as a car salesman.
>
> 14. THAT on or about the 11th of September, 1974 I was advised by Braun that Tax Auditors wished to inspect books of the Company and were considering putting the Company into Receivership. On the 12th of September, 1974, Primex exercised its right under the Debenture held by it to terminate the Company's operations and it was placed under the Trusteeship of one Martin Linsley, a Chartered Accountant and licensed Trustee in the City of Vancouver. I honestly had not known or believed that the state of affairs of the Company were as bad as this at this time.

8 The bankrupt made his assignment in bankruptcy on 6th October 1974, within three months of the granting of the mortgage. The applicants assert that the insolvency of the bankrupt at the time the mortgage was given, as I have said an essential to the presumption created by s. 73(2), is established by reference to the statement of affairs, sworn by the bankrupt, and as well to the statement of the bankrupt himself as set forth in his affidavit that Blinder had not been receiving the payments owing to him. If the amounts which were due to the applicants on the guarantees at the date of the bankruptcy could be said to be "due and accruing due" when the mortgage was granted, there is no doubt that the bankrupt was insolvent since his obligations exceeded the value of his assets by a substantial margin. I believe that having regard to the condition of Image Developments and Enterprises Ltd. at the end of August and the beginning of September, as the bankrupt describes it, the guarantees could be said to be "accruing due", and thus the bankrupt was insolvent at that time. The evidence contained in para. 12 of the affidavit, as above, that the bankrupt was not meeting his payments to Blinder fortifies that conclusion. It suggests as well that the bankrupt was not able to meet his obligations as they became due. The bankrupt has adduced no evidence to meet the strong evidence of his insolvency. And I do not think that his statement that he did not know of the true plight of his company can be taken too seriously, especially since he had been ill with anxiety over the condition of the company in months previous.

9 In commenting on s. 73 (then R.S.C. 1952, c. 14, s. 64) of the Act, Houlden & Morawetz, Bankruptcy Law of Canada, 1960, have this to say at p. 148:

> On an application under Sec. 64 of the Act to set aside as a fraudulent preference a transaction made within three months of bankruptcy the Court must be satisfied by more than a mere statement that the trustee believes the debtor is insolvent, or was insolvent at a certain time, but there is no duty cast upon the trustee requiring proof of a condition of insolvency beyond all reasonable doubt. If the trustee submits evidence which justifies a belief in insolvency, there is *prima facie* satisfaction of the terms of the definition in Sec. 64. It is then open to the debtor to show that by various arrangements he had made with his creditors he was not in fact being required to meet his obligations or to meet his outstanding cheques.

10 I find therefore that the conditions necessary to give rise to the presumption of fraudulent preference, including that the bankrupt be insolvent at the time the mortgage was given, existed and the presumption is to be drawn unless rebutted by the bankrupt.

11 I gather from the authorities cited that the presumption may be successfully rebutted by evidence that the insolvent person gave the preference with a view, not to preferring a creditor, but to the improvement of his own financial condition and thus, I suppose, the condition of his creditors: see for instance *Burns v. Royal Bank; Burns v. Graham* (1922), 2 C.B.R. 241, 482, 51 O.L.R. 564, 69 D.L.R. 608, affirmed 4 C.B.R. 190, 53 O.L.R. 226, [1923] 4 D.L.R. 1111 (C.A.); and *Re A. R. Colquhoun & Son Ltd.; Can. Credit Men's Trust Assn. v. Campbell, Wilson & Strathdee Ltd.*, 18 C.B.R. 124, [1937] 1 W.W.R. 222 (Sask.). Here the bankrupt gives no reason for the mort gage other than to relieve the pressures of a theatened law suit — a factor I am, by the section, expressly precluded from considering. The brother-in-law has not appeared on the application and gives no explanation. Under the circumstances it seems to me that the presumption of preference in respect of the previous advances must clearly apply and it seems that, at least in the absence of an acceptable explanation as to their disposition, the presumption will equally apply to the additional advances. Where the new money went, and whether it added to the assets of the bankrupt, is not known.

12 In *Re Fulton* (No. 2), 7 C.B.R. 213, 58 O.L.R. 400, [1926] 2 D.L.R. 277 (C.A.), Middleton J.A. had this to say in circumstances not unlike the present [pp. 214-15]:

> The appeal here is limited to the contention that the mortgage should not have been invalidated entirely but that it should have been declared to be valid with respect to the sum of $2,200, said to have been advanced. It is said that the payment of this sum increased the assets of the estate by the amount advanced and that the mortgage ought to be regarded as capable of being severed so that it may be declared invalid in part and valid in part.
>
> Upon the question of fact there is no doubt that the $2,200 did not in fact increase the assets of the estate in any tangible way. What became of it is not shown. It did not reach the trustee in bankruptcy and it did not go to any of his creditors. It was

possibly intended to be paid on account of certain notes upon which the brother was endorser. It was not so applied, for the brother says that he had to pay these notes. The debtor was not called, and no explanation of the fate of the $2,200 is given.

A creditor who makes an advance and takes a security not for that advance alone but also for a pre-existing debt for which he seeks to obtain a preference is not in the happy position, when his scheme to obtain the preference for his old debt fails, of being able to say, the security must stand as good so far as any new advance is concerned, even though it is void under *The Bankruptcy Act* so far as the old debt is concerned. The scheme is a device for obtaining a preference and the new advance is in real peril if the scheme fails.

13 I must conclude that the mortgage by the bankrupt of his interest in the home is void. The discharge of the bankrupt will be suspended at least until the interest in the house is dealt with. Either side will be at liberty to apply, however, either before or after that time.

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Bankruptcy and Insolvency Law of Canada, 4th Edition Scope Information

Summary

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Lloyd W. Houlden, Geoffry B. Morawetz & Dr. Janis P. Sarra, *Bankruptcy and Insolvency Law of Canada, 4th ed* (Toronto: Ontario: Thomson Reuters)

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Bankruptcy and Insolvency Law of Canada, 4th Edition § 5:500

Bankruptcy and Insolvency Law of Canada, 4th Edition
The Honourable Mr. Justice Lloyd W. Houlden, Mr. Justice Geoffrey B. Morawetz, Dr. Janis P. Sarra

Part I. The Bankruptcy and Insolvency Act

Chapter 5. Part IV Property of the Bankrupt

VIII. Sections 95, 96

§ 5:500. Insolvency of Debtor—Assets Insufficient to Pay Obligations

In determining whether a debtor is insolvent under para. (c) of the definition of "insolvent person", the balance sheet of the debtor is the starting point. But the court may conclude from other material, such as the values shown on the statement of affairs and the prices obtained for the assets, that the valuations shown on the balance sheet are inaccurate: Re King Petroleum Ltd. (1978), 29 C.B.R. (N.S.) 76 (Ont. S.C.). If accounts receivable have been shown at full value, but many of the accounts have to be written off, the balance sheet of the debtor will not be a reliable guide to solvency: Re Arthur Lennox Constractors Ltd. (No. 2) (1959), 38 C.B.R. 125 (Ont. S.C.); Touche Ross Ltd. v. Weldwood of Canada Sales Ltd. (1983), 48 C.B.R. (N.S.) 83, additional reasons at 49 C.B.R. (N.S.) 284 (Ont. S.C.).

"Property" in the definition of an "insolvent person" is not limited to non-exempt property. It includes property exempt from execution, even though the trustee may not exercise his or her distribution powers over the exempt property: Re Schroeder (2000), 17 C.B.R. (4th) 135, 144 Man. R. (2d) 101, 2000 CarswellMan 92 (Man. Q.B.).

In Betty Shop Ltd. (Trustee of) v. Hanen Invt. Ltd., 63 C.B.R. (N.S.) 176, 49 Alta. L.R. (2d) 237, [1987] 2 W.W.R. 610, 76 A.R. 129 (Q.B.), two weeks prior to the impugned transfer, an audited balance sheet was prepared. The auditors' report was unqualified. The balance sheet showed that the company was solvent with a substantial shareholders' equity. An explanation was given for the financial collapse of the debtor, which was accepted by the court. In these circumstances, it was found that the debtor was not insolvent at the time of the transfer.

The words "accruing due" in para. (c) of the definition of "insolvent person" mean "becoming due". Hence it is quite permissible in preparing a balance sheet for the purposes of para. (c) to show a long term debt even though it is not presently due: Re Viteway Natural Foods Ltd. (1986), 63 C.B.R. (N.S.) 157 (B.C. S.C.); Re Consol. Seed Exports Ltd. (1986), 62 C.B.R. (N.S.) 156 (B.C. S.C.). It is also permissible to show obligations under guarantees: Re Challmie (1976), 22 C.B.R. (N.S.) 78 (B.C. S.C.). In Enterprise Capital Management Inc. v. Semi-Tech Corp. (1999), 1999 CarswellOnt 2213, 10 C.B.R. (4th) 133 (Ont. S.C.J. [Commercial List]), Ground J. was of the opinion that obligations due and accruing due should be limited to obligations currently payable or properly chargeable to the accounting period during which the test is being applied.

A futures broker may be insolvent under para. (c) even though he has long positions in the market at the relevant time. If on the day that the impugned payment was made all the broker's assets had been sold at a fair value, and if the proceeds would not have been sufficient to cover all obligations, due and accruing due, the broker is insolvent: Re Consol. Seed Exports Ltd. (1986), 62 C.B.R. (N.S.) 156 (B.C. S.C.).

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3

1978 CarswellOnt 197
Ontario Supreme Court, In Bankruptcy

King Petroleum Ltd., Re

1978 CarswellOnt 197, 29 C.B.R. (N.S.) 76

RE KING PETROLEUM LIMITED; CLARKSON COMPANY LIMITED v. KING

Steele J.

Heard: October 12 and 13, 1978
Judgment: November 7, 1978

Counsel: *T. M. Dolan*, for trustee.
D. G. Bent, for defendant.

Subject: Corporate and Commercial; Insolvency

Application by the trustee to have certain payments made to the president of the company declared fraudulent and void as against the trustee as a preference.

***Steele J.*:**

1 The defendant was the beneficial owner of all of the outstanding shares of the bankrupt, King Petroleum Limited (the "company"), and at all material times was its president and chief executive officer. The petition in bankruptcy against the company was filed on 17th July 1973, and the Clarkson Company Limited (the "trustee") was appointed interim trustee. A receiving order was subsequently made on 4th December 1973, appointing the plaintiff as trustee. There was no invested capital in the company other than $3 in payment of the incorporators' shares. The bulk of the working capital of the company was derived from personal loans made by the defendant to the company. This money was obtained by him from various banks in the United States on a personal loan basis.

2 The company operated the business of purchasing gasoline for resale at wholesale to others and also for selling at retail through gasoline service bars. The predominant business was the wholesale portion. This was also the more profitable part of the business. In May 1973 the company was told by Imperial Oil Limited ("Imperial Oil"), its principal supplier, that its future supply of gasoline would be drastically reduced. I find that this reduction was such that it would effectively prevent the company from operating its wholesale business but would leave the company sufficient gasoline to operate its retail outlets. I find that there was no violation of any agreement by Imperial Oil in making this reduction. At the same time, in May 1973, there were rumours and and announcements of substantial price increases of gasoline to take effect on 1st June 1973. As a result of these rumours the customers of the company, who operated on a credit slip basis, took delivery of substantially increased quantities of gasoline from Imperial Oil. I find that the company was aware of the price increases and the fact that its customers were taking large quantities of gasoline; in fact, the company itself took as much gasoline as it could obtain from Imperial Oil during the month of May.

3 The action before me is to determine whether payments made by the company to the defendant on 23rd May 1973 and 15th June 1973 in the total amount of $374,106 are fraudulent and void as against the trustee as a preference within the provisions

of s. 73 of the Bankruptcy Act, R.S.C. 1970, c. B-3, and whether the trustee is entitled to judgment against the defendant in this amount.

4 I find that at the time the payments were made the principal creditors of the company were Imperial Oil and the defendant. The terms of payment to Imperial Oil were to be 30 days from the date of invoice on all deliveries or within 10 days from the receipt of the statement. I find that all such accounts up to and including those outstanding at the end of April 1973 were paid by the company during the month of May. I find that at 31st May the company owed Imperial Oil Limited $559,413 and that at the end of June it owed a total of $861,816. There is no evidence before me as to the exact dates of deliveries or invoices, although I find that numerous invoices were given to the company during the months of May and June. The statements for the end of May and June respectively were in normal course sent out by Imperial Oil sometime during the first week of the following month. There is no evidence as to the exact date upon which the statements were received. It may be that they were received substantially later than the first week in the month. As a result I find that the plaintiff has failed in its onus to prove that the payments to Imperial Oil were in arrears at the time of the payments in dispute in this action.

5 I find that on 18th May the defendant became aware that Imperial Oil would not continue to supply the company with large quantities of gasoline. I also find that the company and the defendant were aware that without the large supplies of gasoline they would not be able to operate a profitable business.

6 In order that the payments in question be deemed fraudulent and void, it must be shown that the company was insolvent at the time and that they were made with a view to giving the defendant a preference over other creditors and were made within three months of the date of the petition in bankruptcy. It is clear that the payments were made within the three-month period. Also, I find that the payments were made with a view to giving the defendant a preference over other creditors. The defendant, being the president and chief executive officer of the company, knew as much of the transaction as the company itself did. There is no doubt in my mind but that the company repaid this money to the defendant with a view to repaying his personal bank loans so that he would avoid personal liability. The defendant stated that the money was repaid so that he could retain his bank credit for continuing loans. No such loans were in fact obtained, and therefore I do not accept his evidence. Regardless of what may have been said by any official of Imperial Oil to the company, there is no question but that the payments were made with a view to creating a preference over creditors.

7 The major issue is whether the company was an "insolvent person" when the payments were made. I find that at the time the company knew that it was in financial difficulties and would have difficulty in paying its debts, but this does not in itself mean that the company was insolvent. Section 2 of the Bankruptcy Act defines an insolvent person as follows:

> 'insolvent person' means a person who is not bankrupt and who resides or carries on business in Canada, whose liabilities to creditors provable as claims under this Act amount to one thousand dollars, and
>
> (*a*) who is for any reason unable to meet his obligations as they generally become due, or
>
> (*b*) who has ceased paying his current obligations in the ordinary course of business as they generally become due, or
>
> (*c*) the aggregate of whose property is not, at a fair valuation, sufficient, or, if disposed of at a fairly conducted sale under legal process, would not be sufficient to enable payment of all his obligations, due and accruing due.

8 Clause (*b*) speaks in the past tense, and on the facts of this case I find that the company had not ceased paying its current obligations in the ordinary course of business as they generally became due, and therefore the clause is not applicable.

9 With respect to cl. (*a*), it was argued that at the time the disputed payments were made the company was able to meet its obligations as they generally became due because no major debts were in fact due at that time. This was premised on the fact that the moneys owed to Imperial Oil were not due until ten days after the receipt of the statements and that the statements had not then been received. I am of the opinion that this is not a proper interpretation of cl. (*a*). Clause (*a*) speaks in the present and future tenses and not in the past. I am of the opinion that the company was an "insolvent person" within the meaning of cl. (*a*) because by the very payment-out of the money in question it placed itself in a position that it was unable to meet its

obligations as they would generally become due. In other words, it had placed itself in a position that it would not be able to pay the obligations that it knew it had incurred and which it knew would become due in the immediate future.

10 While there were no specific financial statements of the company on 23rd May or 15th June, it is obvious from the audited financial statements for the year ended 31st July 1972 and the interim period ended 28th February 1973 and the unaudited financial statement for the period ended 30th June 1973 that the company had a serious working capital deficit at all times. Having reviewed the transactions with Imperial Oil of May 1973 and even assuming that the money that would be received would include a profit over the money that would have to be paid out, I am of the opinion that these interim transactions could not have placed the company in a position at any time between 28th February 1973 and 30th June 1973 where it would have been in a position that it could meet its obligations as they generally became due once the money had been paid out to the defendant on 23rd May, and still less after the payment on 15th June.

11 To consider the question of insolvency under cl. (*c*) I must look to the aggregate property of the company and come to a conclusion as to whether or not it would be sufficient to enable payment of all obligations due and accruing due. There are two tests to be applied: first, its fair value and, secondly, its value if disposed of at a fairly conducted sale under legal process. The balance sheet is the starting point, but the evidence relating to the fair value of the assets and what they might realize if disposed of at a fairly conducted sale under legal process must be reviewed in interpreting it. In this case, I find no difficulty in accepting the obligations shown as liabilities because they are known. I have more difficulty with respect to the assets.

12 No specific appraisal was made of the fixed assets shown on the balance sheet at the time in May or June when the cheques in question were issued. The land, buildings and equipment of the service stations and the leasehold improvements thereto shown on the balance sheet are valued at approximately $555,000 at 30th June 1973. The same general category of asset is valued at approximately $500,000 as at 28th February 1973. No depreciation has specifically been attributed to these assets. Even if all depreciation shown on the two statements were attributable to the service stations, the resulting value is substantially in excess of the value of the service stations on the statement of affairs sworn to by the defendant on 2nd January 1974. I do not accept the evidence of the defendant that he signed the statement of affairs sworn on 2nd January 1974 without proper consideration. I find that it was freely signed by him after he had reviewed it in detail. On the first and many subsequent pages his solicitor's writing shows numerous changes initialled by him. This statement shows the value of the real estate, which in fact was the service stations, at $315,000. Even if all of the machinery, equipment and plant were added to this, the value is considerably less than shown on the two balance sheets above referred to. Also, on 13th August 1973 the defendant, through his solicitor, made a tentative offer to purchase the service stations, or a substantial portion of them, at values close to the valuation set out for the individual stations in the statement of affairs. Some time later, when the trustee sold the stations, the total price was close to the value in the statement of affairs. I find the value shown on the statement of affairs as being more accurate than that shown on the balance sheets.

13 On the balance sheets there are substantial trade accounts receivable and, to a lesser extent, other accounts receivable. No allowance is taken for doubtful accounts. This is not in accordance with normal accounting principles, and no evidence was given by the defendant to explain any special circumstances to warrant this departure.

14 These two items indicate to me that the assets shown on the balance sheets do not show their fair valuation nor the value that they would derive if disposed of at a fairly conducted sale under legal process. I am therefore of the opinion that the company was an "insolvent person" within the provisions of cl. (*c*) in s. 2.

15 Having come to the conclusion that I cannot accept the evidence of the defendant with respect to the signing of the statement of affairs by him and bearing in mind that there was an interim receivership from July 1973 until the date of 2nd January 1974, when he signed the statement of affairs, I do not accept his statement that he was forced to sign the statement. As I have stated, I am of the opinion that he fully considered the statement and freely signed it. This goes to the credibility of the defendant. I find that he was not a credible witness. It is with this view that I consider his evidence with respect to his statement that he was told by one Johns, an employee of Imperial Oil, that he should pay off his own indebtedness and that Imperial Oil would give him an additional line of credit to pay its account later. In itself this is an incredible statement for any creditor to make to a debtor. This is particularly so at a time when that same creditor is arguing with the debtor over future supplies. I accept

the evidence of Mr. LePage of Imperial Oil that he was sent to endeavour to collect the money from the company and that in early July he was told by the defendant that the company could not pay its total debt at that time. I find that this is consistent with the position of Imperial Oil that it was at all times endeavouring to collect its account. The plaintiff gave no explanation for not calling Mr. Johns of Imperial Oil, and I conclude that his evidence would be unfavourable to the plaintiff. Even if it would have confirmed the defendant's statement as to what was supposedly said by Mr. Johns, I find that the defendant could not have seriously believed that Mr. Johns had authority to consent to the payments by the company to the defendant, even if Johns had authority to extend the time of payment to Imperial Oil. However, the more important aspect is that Imperial Oil was only one of the creditors of the company, even if it was the largest. The issue is whether the payments were made with a view to giving the defendant a preference over other creditors, and I have so found.

16 I therefore find that the payments made on 23rd May 1973 and 15th June 1973 to the defendant, Bille Wayne King, are fraudulent and void as against the trustee as a preference within the provisions of s. 73 of the Bankruptcy Act, and judgment will issue in favour of the trustee against the defendant in the amount of $374,106. The plaintiff is entitled to its costs against the defendant.

Application granted; judgment issued in favour of trustee.

4

ESSENTIALS OF
CANADIAN LAW

BANKRUPTCY AND INSOLVENCY LAW

SECOND EDITION

RODERICK J. WOOD
Faculty of Law
University of Alberta

4) The Balance Sheet Test

Under the balance sheet test, a debtor is insolvent if the assets of the debtor are insufficient to satisfy all liabilities of the debtor. In applying this insolvency test, it is necessary to decide what things constitute assets and then appraise their value. It is also necessary to decide what things constitute liabilities and then assess their amount. The assets that can be considered are those that belong to the debtor at the time that the insolvency test is conducted. They do not encompass assets that may be acquired in the future or an anticipated profit or increase in value of the assets that may occur sometime in the future.[61] Exempt assets must be included, even though these assets will not be available to satisfy the claims of creditors in insolvency or other enforcement proceedings.[62]

The balance sheet test contemplates two methods for the valuation of assets — the fair valuation of the assets and the disposal of the assets at a fairly conducted sale under legal process. The valuation of assets set out on the debtor's balance sheet is the starting point, but the liquidation value of the assets must also be considered.[63] The values set out on the balance sheet reflect the historic cost of assets, rather than their current value. The valuation of assets on the balance sheet can be departed from if it is shown that some of the accounts receivable are unlikely to be collected or that certain of the assets have depreciated in value.[64]

There is some disagreement over which liabilities must be taken into account under the balance sheet test. The statutory language refers to "all obligations, due and accruing due." Some cases have held that this does not encompass all future liabilities but only "obligations currently payable or properly chargeable to the accounting period during which the test is being applied."[65] Other cases have held that all future obligations, including contingent liabilities, must be included.[66] In principle, the balance sheet test should include all future liabilities. A failure to include these into the calculation unfairly prejudices long-term creditors.

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61 *Re Consolidated Seed Exports Ltd* (1986), 62 CBR (NS) 156 (BCSC).

62 *Re Schroeder* (2000), 17 CBR (4th) 135 (Man QB); *Re Derksen* (1995), 34 CBR (3d) 252 (Man QB).

63 *King Petroleum*, above note 54.

64 *Touche Ross Ltd v Weldwood of Canada Sales Ltd* (1983), 48 CBR (NS) 83 (Ont HCJ); *633746 Ontario Inc (Trustee of) v Salvati* (1990), 79 CBR (NS) 72 (Ont HCJ).

65 *Enterprise Capital Management Inc v Semi-Tech Corp* (1999), 10 CBR (4th) 133 (Ont SCJ) [*Enterprise*]; *Re Oblats de Marie Immaculée du Manitoba* (2004), 1 CBR (5th) 279 (Man QB); *Industries Cover inc (Syndic des)*, 2015 QCCS 136.

66 *Re Stelco Inc* (2004), 48 CBR (4th) 299 (Ont SCJ) [*Stelco*]; *Viteway*, above note 54; *Optical Recording Laboratories Inc v Digital Recording Corp* (1990), 2 CBR (3d) 64 (Ont CA).

The insolvency test must be met before a payment or transfer of property can be impugned as a preference. A failure to include all liabilities would permit short-term creditors to be paid despite the fact that this will result in insufficient assets to satisfy the claims of long-term creditors. Courts that have refused to include all obligations have expressed a concern that this may result in too many businesses falling within the definition.[67] This concern is misplaced. The excess of liabilities over assets is not an act of bankruptcy, and therefore involuntary bankruptcy proceedings cannot be forced upon a debtor even if the debtor is insolvent under the balance sheet test.

The statutory language associated with the balance sheet test refers to obligations rather than debts. Contingent claims and unliquidated claims are therefore included.[68] The valuation of contingent claims poses a particular difficulty. The contingency may or may not arise, and the probability that it will can range from an almost complete certainty to a very remote possibility. Where the probability is at one of these extremes, the courts will simply include the full value of the high probability claim[69] and reduce to zero the value of the low-probability claim. Matters become less certain when the likelihood of occurrence is somewhere in between these two extremes.

Professor Goode identifies two approaches to valuation of contingent liabilities.[70] One approach is to determine if there is a probability that the claim will occur (i.e., a greater than 50 percent chance). If so, the full value of the claim is included; if not, the obligation is valued at zero. The alternative approach would be to value the claim at the percentage likelihood of its occurrence. Under this approach, a claim for $100 that has a 60 percent chance of occurring would be valued at $60. Courts have adopted the second valuation approach to deal with problems of valuation that arise in connection with the proof of contingent claims by claimants who wish to participate in the proceeds of bankruptcy liquidation. There is no reason why this approach should not also be applied in connection with the balance sheet test.[71]

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67 *Enterprise*, above note 65.

68 *Re Challmie* (1976), 22 CBR (NS) 78 (BCSC).

69 *Ibid*. The contingent liability was a personal guarantee in respect of a company that was in financial difficulties. The court simply added the full value of this claim to the liabilities of the debtor.

70 R Goode, *Principles of Corporate Insolvency Law*, 4th ed (London: Sweet and Maxwell, 2011) at 145–47.

71 *Re Wiebe* (1995), 30 CBR (3d) 109 (Ont Ct Gen Div). And see Chapter 9, Section A(8).

5

Transfers at Undervalue: New Wine in Old Wineskins?

Roderick J Wood*

> Neither is new wine put into old wineskins; otherwise, the skins burst, and the wine is spilled, and the skins are destroyed; but new wine is put into fresh wineskins, and so both are preserved.[1]

A. Overview

Section 96 of the *Bankruptcy and Insolvency Act (BIA)*[2] sets out provisions that permit a trustee in bankruptcy to challenge pre-bankruptcy transfers at undervalue entered into by a debtor. These provisions were part of the 2005 and 2007 amendments to the *BIA* that came into force in 2009. The provision replaced the outdated and much maligned[3] settlement provisions and the more recently enacted reviewable transactions provisions[4] of the *BIA*. The obscure settlement provisions are justly consigned to the ash bin of history and are of practically no significance in interpreting the transfer at undervalue provisions. The transfer at undervalue provisions share a number of similarities to the reviewable transactions provisions, and therefore the cases interpreting these provisions are of continuing relevance. In some instances, the transfer at undervalue provisions permit the licensed insolvency trustee to impeach a transfer at undervalue if the debtor intended to defraud, defeat or delay a creditor. In these instances, the case law in relation to fraudulent conveyances law is valuable as it uses a similar formulation.

There can be no doubt that the transfer at undervalue provisions are vastly superior to the provisions that they replaced. A review of the decisions that have interpreted and applied the transfer at undervalue provisions reveals that the tools that are now at hand are much better suited to realizing the underlying objectives of bankruptcy and insolvency law.[5] However, the new provisions recycle several features of prior law. Some of the problematic features of the now repealed reviewable transactions provisions have been retained. Some of the language of centuries old fraudulent conveyance law has also been added. The lingering question is whether

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[1] Matthew 9:17, *New Revised Standard Version Bible.*

[2] RSC 1985, c B-3 [*BIA*].

[3] See RCC Cuming, "Section 91 (Settlements) of the Bankruptcy and Insolvency Act: A Mutated Monster" (1995) 25 *CBLJ* 235.

[4] The reviewable transactions provisions were contained in section 100 of the *BIA* but were repealed and replaced by s 96 of the *BIA* in 2009.

[5] For a discussion of the policies underlying the *BIA* provisions, see A Duggan and T Telfer, "Gifts and Transfers at Undervalue" in Stephanie Ben-Ishai and Anthony Duggan (eds.), *Canadian Bankruptcy and Insolvency Law: Bill C-55, Statute c.47 and Beyond* (Lexis-Nexis, Toronto, 2007) 175.

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1. Disposition of Property or Provision of Services

A "transfer at undervalue" is limited to a disposition of property or provision of services. The precise boundaries established by this language have not yet been fully tested in the courts. There are transactions that confer a benefit on another person, but which do not involve a transfer of property by the debtor to that person. Suppose that A owes $100 to B. If C pays $100 to B in satisfaction of the debt, A obtains a benefit (the release of the debt) even though property was not transferred to A. Is this transaction impeachable in the event that C goes bankrupt?

One suspects that courts will take an expansive view as to the types of transactions that are brought within the scope of the provision. For one thing, the language of the transfer at undervalue provisions is broader in that a "disposition of property" has a wider compass than a "conveyance of property" – the term that is used in fraudulent conveyances law. A disposition would appear to capture a dealing with property even though it might not involve a conveyance of it to the recipient of the benefit.

The Supreme Court of Canada in *Royal Bank of Canada v North American Life Assurance Co*[7] indicated that fraudulent conveyance law should be interpreted liberally in favour of creditors:

> All the provincial fraud provisions are clearly remedial in nature, and their purpose is to ensure that creditors may set aside a broad range of transactions involving a broad range of property interests, where such transactions were effected for the purpose of defeating the legitimate claims of creditors. Therefore, the statutes should be given the fair, large and liberal construction and interpretation that best ensures the attainment of their objects, as required by provincial statutory interpretation legislation…[8]

There is every reason to believe that a similar approach will be taken in respect of the transfer at undervalue provisions as they share a similar objective. The courts have not limited the provision to transactions in which the right in the property is transferred from the debtor to the recipient through a conveyance or assignment. In *City Peel Taxi v Victory Hanna*[9], Justice Wilton-Siegel held that the transfer at undervalue provisions "capture all transactions having the effect of an assignment, whether or not they constitute an actual assignment of rights." Transactions in which licences are cancelled and reissued to another person at the request of the licence holder are therefore within the scope of the term. It remains to be seen whether this expansive view will be extended to other types of cases. The Alberta Court of Appeal in *Sembaliuk v Sembaliuk*[10] held that a disclaimer of a bequest under a will cannot be impeached

[7] [1996] 1 SCR 325 [*North American Life Assurance Co*].
[8] *Ibid* at 365.
[9] 2012 ONSC 2450 [*City Peel Taxi*].
[10] (1984), 15 DLR (4th) 303 (Alta CA).

IN THE MATTER OF THE *COMPANIES CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

Court File No: CV-23-00696017-CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

Proceeding commenced at Toronto

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(Motion Returnable June 13 and 14, 2024)

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