

Litigating with a Bankrupt – Navigating the Stay
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(a) the Bankruptcy and Insolvency Act

(i) Insolvency

1. The Supreme Court of Canada in *R v. Fitzgibbon*, 1990 Canlii 102 commented as follows on the purpose of the stay of proceedings:

[. . .] The aim of the section is to provide a means of maintaining control over the distribution of the assets and property of the bankrupt. In doing so, it reflects one of the primary purposes of the Bankruptcy Act, namely to **provide for the orderly and fair distribution of the bankrupt's property** among his or her creditors on a pari passu basis. See Duncan and Honsberger, *Bankruptcy in Canada* (3rd ed. 1961), at p. 4. **The object of the section is to avoid a multiplicity of proceedings and to prevent any single unsecured creditor from obtaining a priority over any other unsecured creditors by bringing an action and executing a judgment against the debtor.** This is accomplished by providing that no remedy or action may be taken against a bankrupt without leave of the court in bankruptcy, and then only upon such terms as that court may impose.

[emphasis added]

2. Justice Dawson in *Condominium Plan No. 78R15349 v. Fayad*, 2001 SKQB 104 commented as follows in relation to the stay provisions contained in section 69 of the *BIA*:

[12] Section 69 does not give the court power to order a stay; rather it creates a stay ipso facto upon the filing of a notice of intention or upon bankruptcy, by prohibiting a creditor from instituting or continuing the proceedings mentioned without leave of the Bankruptcy Court. Where a creditor with a claim provable in bankruptcy sees a remedy against the debtor or his property, leave of the court must be obtained. When proceedings are taken against the person or property of the debtor for a "claim provable in bankruptcy" leave of the court must also be obtained. In order for leave to be granted, an applicant must demonstrate to the court that there exists compelling reasons to permit an action either to commence or to proceed (*Wychreschuk v. Sellors (Trustee of)* (1988), 71

C.B.R. (N.S.) 37; 55 Man. R. (2d) 89, affm. 73 C.B.R. (N.S.) 267 (Man. C.A.)).

3. Section 69.1 Stay of proceedings — notice of intention:

- (a) Upon an insolvent person filing a notice of intention to make a proposal (see section 50.4), no creditor has remedy against the insolvent person or the insolvent person's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy;
- (b) A secured creditor cannot seize the debtor's assets covered by a security agreement unless the use of or dealing with the assets would significantly prejudice the secured creditor.

4. Section 69.2(1) Stay of proceedings – consumer proposals:

- (a) Upon the filing of a consumer proposal, no creditor has any remedy against the debtor or the debtor's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy until the proposal has been amended, withdrawn, refused, annulled or deemed annulled, or the administrator discharged.
- (b) A consumer proposal does not prevent a secured creditor from realizing his or her security.

5. Section 69.3 Stay of proceedings – bankruptcy:

- (a) On bankruptcy, no creditor has any remedy against the debtor or the debtor's property, or shall commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy.
- (b) Does not prevent a secured creditor from realizing or otherwise dealing with his or her security.
 - (i) The policy of the BIA is that bankruptcy should not interfere with secured creditors except in so far as it may be necessary in order to protect the

estate as to any surplus on the assets covered by the security. Any equity in the security must pass to the Estate.

(ii) Receiverships

6. The template receivership order (and explanatory notes) has recently been updated. Copies of the materials can be found on the Sasklaw Courts Website (<https://sasklawcourts.ca/>). Follow these links to access the materials: (1) Court of Queen's Bench Tab / Administrative Notices / Template Receivership and CCAA Initial Orders. There will be a Table of Contents containing links to the various documents after the Administrative Notice of Chief Justice Popescul.
7. The following sections prevent the commencement, continuation, or exercise of any rights or remedies against the receiver, the debtor, or the property of the debtor that is subject to the receivership order.

NO PROCEEDINGS AGAINST THE RECEIVER

9. No proceeding or enforcement process in any court or tribunal (each, a "**Proceeding**") shall be commenced or continued against the Receiver except with the written consent of the Receiver or with leave of this Court.

NO PROCEEDINGS AGAINST THE DEBTOR OR THE PROPERTY

10. No Proceeding against or in respect of the Debtor or the Property shall be commenced or continued except with the written consent of the Receiver or with leave of this Court and any and all Proceedings currently under way against or in respect of the Debtor or the Property are hereby stayed and suspended pending further Order of this Court, provided, however, that nothing in this Order shall: (i) prevent any Person from commencing a Proceeding regarding a claim that might otherwise become barred by statute or an existing agreement, if such Proceeding is not commenced before the expiration of the stay provided by this paragraph; or (ii) affect a Regulatory Body's investigation in respect of the Debtor or an action, suit or proceeding that is taken in respect of the Debtor by or before the Regulatory Body, other than the enforcement of a payment order by the Regulatory Body or the Court. "**Regulatory Body**" means a person or body that has powers, duties or functions relating to the enforcement or administration of an Act of Parliament or of the legislature of a province.

NO EXERCISE OF RIGHTS OR REMEDIES

11. All rights and remedies (including, without limitation, set-off rights) against the Debtor or the Receiver, or affecting the Property, are hereby stayed and suspended except with the written consent of the Receiver or leave of this Court, provided however that nothing in this paragraph shall: (i) empower the Receiver or the Debtor to carry on any business which the Debtor is not lawfully entitled to carry on; (ii) exempt the Receiver or the Debtor from compliance with statutory or regulatory provisions relating to health, safety or the environment; (iii) prevent the filing of any registration to preserve or perfect a mortgage or security interest; or (iv) prevent the registration or filing of a lien or claim for lien or the commencement of a Proceeding to protect a lien or other rights that might otherwise be barred or extinguished by the effluxion of time, provided that no further steps shall be taken in respect of such lien, claim for lien or Proceeding except for service of the initiating documentation on the Debtor and the Receiver. The stay and suspension shall not apply in respect of any "Eligible Financial Contract" as defined in section 65.1 of the BIA.

NO INTERFERENCE WITH THE RECEIVER

12. No Person shall discontinue, fail to honour, alter, interfere with, repudiate, terminate or cease to perform any right, renewal right, contract, agreement, licence or permit in favour of or held by the Debtor, including, without limitation, insurance coverage, without written consent of the Receiver or leave of this Court. Nothing in this Order shall prohibit any party to an Eligible Financial Contract with the Debtor from terminating such contract or exercising any rights of set-off, in accordance with its terms.

(b) Companies' Creditors Arrangement Act ("CCAA")

8. The language contained in the CCAA Initial Order respecting the stay is similar to that contained in the Receivership Order.

NO PROCEEDING AGAINST THE APPLICANT OR THE PROPERTY

14. Until and including [DATE-MAXIMUM 30 DAYS] 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 Applicant or the Monitor, or affecting the Business or the Property, except with the written consent of the Applicant and the Monitor, or with leave of this Court and any all Proceedings currently underway against or in respect of the Applicant or affecting the Business or the Property are hereby stayed and suspended pending further Order of this Court.

NO EXERCISE OF RIGHTS OR REMEDIES

15. 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 Applicant or the Monitor, or affecting the Business or the Property, are hereby stayed and suspended and shall not be commenced, proceeded with or continued except with the written consent of the Applicant and the Monitor, or leave of this Court, provided that nothing in this Order shall:
- (a) empower the Applicant to carry on any business which the Applicant is not lawfully entitled to carry on;
 - (b) affect such investigations, actions, suits or proceedings by a regulatory body as are permitted by section 11.1 of the CCAA;
 - (c) prevent the filing of any registration to preserve or perfect a security interest;
 - (d) prevent the registration of a claim for lien; or
 - (e) prevent the commencement of a Proceeding to preserve rights that might otherwise be barred or extinguished by the effluxion of time, provided that no further steps shall be taken in respect of such Proceeding except for service of the initiating documentation on the Applicant and that written notice of such action be given to the Monitor at the first available opportunity.

NO INTERFERENCE WITH RIGHTS

16. During the Stay Period, no Person shall accelerate, suspend, discontinue, fail to honour, alter, interfere with, repudiate, terminate or cease to perform any right, renewal right, contract, agreement, licence or permit in favour of or held by the Applicant, except with the written consent of the Applicant and the Monitor, or leave of this Court.

(c) **Does The Stay Apply To My Claim?**

(i) Debts not Discharged by Bankruptcy

9. There are certain debts or claims that are not released by an order of discharge from the bankruptcy, and in these cases a creditor may pursue the claim against the bankrupt individual despite the operation of the stay of proceedings.

10. These are the kinds of claims that society, through Parliament, considers to be of a quality that outweighs any possible benefit in the bankrupt being relieved of them: *Simone v. Daley* (1999), 170 D.L.R. (4th) 215 (Ont. C.A.).
11. Section 178 of the *BIA* details the types of claims that are not discharged, some of which include the following:
 - (a) Fine, penalty, or restitution order imposed by a court in respect of a debt arising out of a recognizance or bail;
 - (b) Award of damages imposed by a court in civil proceedings in respect of intentionally inflicted bodily harm, sexual assault, or wrongful death;
 - (c) Debt or liability for support or maintenance for a former spouse of child living apart from the bankrupt. The payee spouse must file a proof of claim for the amounts and will receive a preferred claim for amounts accrued in the year before the date of bankruptcy, together with any lump sum payments. This does not include an equalization payment. There is no stay of proceedings with respect to such payments; however, the payee spouse cannot take action against any property that is vested in the name of the trustee in bankruptcy; and
 - (d) Debt arising out of fraud, embezzlement, misappropriation, or defalcation;
 - (i) Fraudulent means something more than merely wrongful: there must be an element of dishonesty;
 - (ii) The most common type of fraud claim that I have come across are situations where there is a builders' lien claim, the debtor makes an assignment, and the creditor down the pyramid alleges that the debtor breached the trust provisions of *The Builders' Lien Act*, ie. the debtor was in possession of trust funds from the owner or

contractor, did not pass them down the trust, and used the funds for a use inconsistent with the trust while leaving the debt to the lien claimant/sub-contractor unpaid.

- (e) Debts arising from obtaining property or services by false pretences or fraudulent misrepresentation. To establish fraudulent misrepresentation, the following must be proved:
 - (i) The making of a misrepresentation
 - (ii) The representation was false;
 - (iii) The representation was made knowingly without belief in its truth, or recklessly indifferent whether it was true or false;
 - (iv) The creditor relied on the representation and turned over property to the debtor.
 - (f) Student loans provided that the assignment is made while the bankrupt is still a student, or the assignment is made within 7 years of ceasing to be a student. After 5 years of ceasing to be a student, the bankrupt can on application seek an order that the debt not survive bankruptcy for reasons that he or she acted in good faith in connection with the liabilities under the loan and the bankrupt will continue to experience financial difficulties to such an extent that he will be unable to pay the loan.
12. Obtain the consent of the Trustee to pursue claims that are not subject to the stay of proceedings, and which will continue during the insolvency. We did this recently and the Trustee approved our action, but the Trustee will likely not consent to taking enforcement proceedings in relation to a judgment arising from a finding of fraud while the bankrupt is undischarged and the estate is being administered.

13. In the event of non-exempt assets to be realized and/or surplus income payable for the benefit of all creditors, the Trustee's position is that those are assets of the bankruptcy estate and subject to unsecured claims. The creditor obtaining a judgment arising from fraud does not get a priority.
14. The Court can direct a trial of the issue to determine if the matter falls within s. 178 of the *BIA*,
15. If leave of the court is not obtained and it should have been obtained, the proceedings are ineffective to confer any rights on a creditor: *Amanda Designs Boutique Ltd. v. Charisma Fashions Ltd.* (1972) 17 C.B.R. (N.S.) 16 (Ont. CA). Hence the importance of ensuring that you have the consent of the Trustee, or the court, to proceed with a claim against an undischarged bankrupt.
16. The Trustee could also disallow the claim of a security creditor, and if not appealed, the creditor becomes an unsecured creditor subject to the stay.

(d) Lifting the Stay

17. Under section 69.4 of the *BIA*, a creditor may apply to the court to have the stay lifted. The moving party must prove that:
 - (a) It is likely to be materially prejudice by the stay; or
 - (b) That it is equitable on other grounds to do so.
18. The Court in *Re Advocate Mines Ltd.*, (1984), 52 C.B.R. (N.S.) 277 (Ont. Reg.) is the leading case on the topic and summarizes the types of cases where the court will likely remove the stay:

- (a) Actions against the bankrupt for a debt to which a discharge would not be defence;
- (b) Actions in respect of a contingent or unliquidated debt, the proof of which and valuation has that degree of complexity which makes the summary procedure in section 121(2) (contingent¹ or unliquidated claims²) and 135 (Trustee's disallowance of claim) of the BIA inappropriate;
- (c) Actions in which the bankrupt is a necessary party for the complete adjudication of matters at issue involving other parties;
- (d) Actions brought to establish judgment against the bankrupt to enable the plaintiff to recover under a contract of insurance or indemnity or under compensatory legislation; and
- (e) Actions in Ontario which, at the date of bankruptcy, have progressed to a point where logic dictates that the action be permitted to continue to judgment.

(e) Suing an Undischarged Bankrupt

- 19. There are situations where a bankrupt does not cooperate with the Trustee or complete the duties imposed on him in an insolvency, and does not obtain his or her discharge. The insolvency drags out and matter goes unresolved. In these situations, the bankrupt may continue to engage in trade or business incurring further claims or liabilities.
- 20. The stay remains in effect until the Trustee is discharged. Pursuant to section 69.3(1.1) the stay of proceedings ceases to apply in respect of a creditor on the day the Trustee is discharged. The discharge of a trustee permits creditors, whose entitlement has not otherwise been dealt with as part of the bankruptcy, to pursue remedies against an undischarged bankrupt without leave.

¹ Contingent claim is a claim that may or ever ripen into a debt, according to some future event

² A claim is in the nature of a debt, i.e. a specific sum of money due and payable under or by virtue of a contract. Its amount must either be already ascertained or capable of being ascertained.

21. If a bankrupt continues to engage in trade and business while prior to his discharge and the discharge of the Trustee, the creditor may oppose the discharge under section 173 and seek a conditional discharge.

(f) Proceedings By Creditor When Trustee Refuses to Act

22. If a creditor identifies some conduct, or a claim, against the bankrupt and the Trustee refuses to take action, the creditor may apply for an order that the creditor be permitted to proceed with the action – see section 38.
23. In this instance, any benefit derived from the proceedings belongs to the creditor to the extent of the debt, and any surplus belongs to the Trustee.

(g) Objections to Discharge by the Bankrupt

24. If the claim of your client is ultimately captured by the stay of proceedings, that is not necessarily the end of the matter. A creditor can oppose the discharge of a bankrupt and seek a discharge that is conditional upon something such as the payment of money, or a discharge that is suspended for a period of time.
25. The following are the relevant grounds of misconduct on the part of the bankrupt that may result in a discharge not being granted:

(a) the assets of the bankrupt are not of a value equal to fifty cents on the dollar on the amount of the bankrupt's unsecured liabilities, unless the bankrupt satisfies the court that the fact that the assets are not of a value equal to fifty cents on the dollar on the amount of the bankrupt's unsecured liabilities has arisen from circumstances for which the bankrupt cannot justly be held responsible;

(b) the bankrupt has omitted to keep such books of account as are usual and proper in the business carried on by the bankrupt and as sufficiently disclose the business transactions and financial position of the bankrupt within the

period beginning on the day that is three years before the date of the initial bankruptcy event and ending on the date of the bankruptcy, both dates included;

(c) the bankrupt has continued to trade after becoming aware of being insolvent;

(d) the bankrupt has failed to account satisfactorily for any loss of assets or for any deficiency of assets to meet the bankrupt's liabilities;

(e) the bankrupt has brought on, or contributed to, the bankruptcy by rash and hazardous speculations, by unjustifiable extravagance in living, by gambling or by culpable neglect of the bankrupt's business affairs;

(f) the bankrupt has put any of the bankrupt's creditors to unnecessary expense by a frivolous or vexatious defence to any action properly brought against the bankrupt;

(g) the bankrupt has, within the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy, both dates included, incurred unjustifiable expense by bringing a frivolous or vexatious action;

(h) the bankrupt has, within the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy, both dates included, when unable to pay debts as they became due, given an undue preference to any of the bankrupt's creditors;

(i) the bankrupt has, within the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy, both dates included, incurred liabilities in order to make the bankrupt's assets equal to fifty cents on the dollar on the amount of the bankrupt's unsecured liabilities;

(j) the bankrupt has on any previous occasion been bankrupt or made a proposal to creditors;

(k) the bankrupt has been guilty of any fraud or fraudulent breach of trust;

(l) the bankrupt has committed any offence under this Act or any other statute in connection with the bankrupt's property, the bankruptcy or the proceedings thereunder;

(m) the bankrupt has failed to comply with a requirement to pay imposed under section 68;

(n) the bankrupt, if the bankrupt could have made a viable proposal, chose bankruptcy rather than a proposal to creditors as the means to resolve the indebtedness; and

(o) the bankrupt has failed to perform the duties imposed on the bankrupt under this Act or to comply with any order of the court.

