Court File No. C12-9731-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

B E T W E E N:

PINNACLE CAPITAL RESOURCES LIMITED in its capacity as general partner of RED ASH CAPITAL PARTNERS II LIMITED PARTNERSHIP

Applicant

- and -

KRAUS INC., KRAUS CANADA INC., STRUDEX FIBRES LIMITED, and 538686 B.C. LTD.

Respondents

APPLICATION UNDER SUBSECTION 46(1) and Section 243 OF THE *BANKRUPTCY AND INSOLVENCY ACT,* R.S.C. 1985, c. B-3, as amended

BOOK OF AUTHORITIES OF THE APPLICANT

May 25th, 2012

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TAB 1.

Case Name:

Konopny (Re)

RE: IN THE MATTER OF the Bankruptcy of Motek Konopny

[2009] O.J. No. 3548

57 C.B.R. (5th) 87

2009 CarswellOnt 5013

179 A.C.W.S. (3d) 1103

Court File No. 31-OR-207567-T

Ontario Superior Court of Justice

G.R. Strathy J.

Heard: August 25, 2009.
Judgment: August 26, 2009.

(30 paras.)

Bankruptcy and insolvency law -- Administration of estate -- Administrative officials and appointees -- Receivers -- Appointment -- When required or justified -- Interim appointment -- Motion by creditor to appoint interim receiver of property of debtor allowed -- Creditor filed application for bankruptcy order against debtor based on alleged guarantee -- Creditor made out prima facie case that debtor signed guarantee -- Debtor's conduct indicated there was real risk of dissipation of estate -- Although prejudice to debtor could be assumed, debtor had been subject to interim receivership order and no evidence of disruption of his affairs, proposed receivership would continue until application had been dealt with and debtor swore assets not being dissipated and did not identify any prejudice he would suffer.

Motion by creditor to appoint an interim receiver of the property of the debtor. The debtor was the president of a company which went out of business in August 2008. The creditor filed an application for a bankruptcy order against the debtor in August 2008 based on an alleged guarantee given by the debtor of the indebtedness of his company to the predecessor of the creditor. The creditor was unable to produce an original of the application form containing the alleged guarantee, was not aware of the guarantee form until after the debtor's company went out of business and the debtor did

not remember signing the guarantee. Approximately two months after the application for a bankruptcy order was made, the debtor gave a mortgage on his residence, securing a payment of $200,000, to a non-arm's length company owned by his parents. He was then ordered not to have any further dealings with his property pending the return of the creditor's motion or further court order. Notwithstanding that order, the debtor received three payments, totalling $20,315, under the mortgage. An interim receiver was appointed to monitor the debtor's expenses following an application by another creditor. The debtor was also ordered not to further encumber, transfer or convey his home or other assets prior to hearing the bankruptcy application. After reaching an agreement with the second creditor, the application for a bankruptcy order was dismissed and the receiver was discharged. Although counsel for the creditor requested at that time that the receivership provisions of the earlier order be continued, such an order was not made.

HELD: Motion allowed. The creditor made out a prima facie case that the debtor signed the guarantee. The debtor's conduct indicated that there was a real risk of dissipation of the estate if the order was not granted as he had demonstrated an intention to defeat his creditors by disposing of his assets in the face of pending proceedings. Although prejudice to the debtor could be assumed, the debtor had been subject to an interim receivership order for nine months and there was no evidence of a disruption of his affairs, the proposed interim receivership would continue until the application for bankruptcy had been dealt with and the debtor swore his assets were not being dissipated and did not identify any prejudice he would suffer.

Statutes, Regulations and Rules Cited:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B.3, s. 46(1)

Counsel:

Katherine I. Henshell, for the Applicant.

Douglas Bourassa, for the Respondent.

ENDORSEMENT

1 **G.R. STRATHY J.**:-- The applicant creditor, S.P. Richards Co. Canada Inc., ("Richards") moves to appoint an interim receiver of the property of the debtor.

2 Richards' claim is based on an alleged guarantee given the respondent, Motek Konopny, of the indebtedness of "Office Supercentre" to Norwestra Sales (1992) Inc., the predecessor of Richards. Mr. Konopny was the President of Office Supercentre, which went out of business in August, 2008. I will discuss the alleged guarantee in more detail below. What follows is a brief history of these proceedings.

Background

3 On August 27, 2008, Richards filed an Application for Bankruptcy Order against Mr. Konopny. The application claimed a debt of $848,136.61.

4 On October 14, 2008, Mr. Konopny gave a mortgage on his residence, securing payment of $200,000, to a non-arm's length company owned by his parents.

5 On November 3, 2008, there was a hearing before the registrar at which time the registrar noted that a dispute had been filed and the matter would be added to the hearing list for November 6, 2008. In the interim, Mr. Konopny was ordered "not to have any further dealings with [his] property, real or person, pending return of that motion or further court order."

6 Notwithstanding the registrar's order, on that very day, November 3, three payments in the total amount of $20,315 were advanced to Mr. Konopny under the mortgage. It is not clear whether these advances were made before or after the registrar's order.

7 On November 7, 2008, on the application of another creditor, the registrar ordered that an interim receiver be appointed to monitor Mr. Konopny's expenses and ordered that he not further encumber, transfer or convey the matrimonial home or any other asset whatsoever prior to the hearing of the bankruptcy application or other order of the court. The order made provision for Mr. Konopny to borrow against the equity on the matrimonial home, to a prescribed monthly maximum, and to borrow funds on an unsecured basis for ordinary living and legal expenses.

8 That order appears to have remained in effect until August 12, 2009, the date on which the application was scheduled to be heard.

9 On August 11, 2009, at 5:00 p.m., an agreement was reached between the petitioning creditor and Mr. Konopny, whereby it was agreed that its application for bankruptcy order be dismissed, without costs.

10 On August 12, 2009, as a result of that settlement, Mesbur J. ordered that the interim receivership order of November 7, 2008 order be terminated and the receiver be discharged. She noted that Richards' application for bankruptcy would be heard on September 17, 2009. She noted that a request had been made by counsel for Richards that the receivership provisions of the registrar's order be continued until the hearing of the application, but as the file was not before her she declined to make that order. She noted that Richards was at liberty to move for the appointment of a receiver pending the bankruptcy proceeding.

11 That brings me to the motion before me.

Submissions

12 Ms. Henshell on behalf of Richards relies on s. 46(1) of the *Bankruptcy and Insolvency Act,* R.S.C. 1985, c. B.3 which provides:

> The court may, if it is shown to be necessary for the protection of the estate of a debtor, at any time after the filing of an application for a bankruptcy order and before a bankruptcy order is made, appoint a licensed trustee as interim receiver of the property or any part of the property of the debtor and direct the interim receiver to take immediate possession of the property or any part of it on an undertaking being given by the applicant that the court may impose with respect to interference with the debtor's legal rights and with respect to damages in the event of the application being dismissed.

13 She submits that there is clear evidence Mr. Konopny has engaged in dissipation subsequent to being served with the application for bankruptcy order and that his conduct demonstrates a need

for supervision. She relies on *Atsana Semiconductor Corp. (Re.)* (2005), 14 C.B.R. (5th) 1, [2005] O.J. No. 3242 (S.C.J.) and *Maxium Financial Services Inc. v. Corporate Cars Limited Partnership* (2006), 29 C.B.R. (5th) 110, [2006] O.J. No. 4878 (S.C.J.), In the former case, it was suggested that the danger of dissipation of assets must be actual and immediate and not based on mere suspicion: *Royal Bank of Canada v. Zutphen Brothers Constructions Ltd.* (1993), 17 C.B.R. (3d) 314 (N.S.S.C.). In the *Maxium Financial* case, however, C.L. Campbell J. suggested that the *Royal Bank of Canada v. Zutphen Brothers* test is not the law in Ontario. He stated at paras. 14 and 15:

> Ground J. in *Bank of Nova Scotia v. D.G. Jewelry Inc.*, [2002] O.J. No. 4000 rejected the above test on the basis that it was not the law of Ontario. In *Atsana Semi-conductors Corp. (Re)*, [2005] O.J. No. 3242, Aitkin J. accepted the Nova Scotia test but does not appear to have been referred to the statement of Ground J. in *D.G. Jewelry*.
>
> I accept that there must be more than a suspicion or speculation concerning the assets of a company before an interim receiver is warranted. Where, as here, the major secured creditors who have the most at risk have with legitimate reason lost confidence, I do not think that there has to be an actual immediate risk to assets.

14 Ms. Henshell submits that an appointment of an interim receiver is necessary for the preservation and protection of Mr. Konopny's estate for the interests of his creditors.

15 Mr. Bourassa on behalf of Mr. Konopny submits, first, that there is no urgency to the appointment of an interim receiver, relying on *Re. Imperial Broadloom Co.* (1979), 22 O.R. (2d) 129, 29 C.B.R. (N.S.) 113 at paras. 5 and 9 (Sup. Ct.). It is apparent from the reading of those paragraphs that Henry J. was referring to the limitations on the jurisdiction of the *registrar* to make an interim order in the case of urgency. He was not stating a general proposition that the appointment can only be made by a judge in cases of urgency.

16 Mr. Bourassa submits the applicant has not met the test for the appointment of a receiver set out by Saunders J. in *Pure Harmonics Inc. (Re.)* (1983), 50 C.B.R. (N.S.) 170, [1983] O.J. No. 2335 (H.C.J.) at paras 1-4:

> ... The principles on which an order appointing an interim receiver in a bankruptcy petition ought to be granted are not in dispute and for such an appointment the petitioning creditor must show a *strong prima facie case* of bankruptcy and the necessity for immediate protection of the bankrupt estate: see *Re Strain* (1976), 23 C.B.R. (N.S.) 206, a decision of the Manitoba Court of Appeal.
>
> The principles have been set out in the old case of *Re Stuart & Sutterby*, 11 C.B.R. 1, reversed 65 O.L.R. 154, 11 C.B.R. 279, [1930] 2 D.L.R. 689, which was affirmed 66 O.L.R. 427, 12 C.B.R. 267, [1931] 1 D.L.R. 754 (C.A.), in which the registrar made the following statement [at p. 31]:
>
> > In every case, the following essentials are necessary, although the facts may vary in almost every case: (1) it must be shown that a receiving order is *almost certain to be made* eventually, in so far as it can be determined at

> that stage what disposition will be made of the petition; (2) that unless an interim receiver is appointed to take possession to preserve the assets, there is grave danger that the assets existing on the date of the appointment will not all be recovered or be properly accounted for, when a receiving order is made.
>
> While *Stuart & Sutterby* is an old case, it has been subsequently cited with approval in a number of cases and it was not suggested that the principles stated in that case are not applicable to the issue that was before the registrar. [emphasis added]

17 I might note that in the *Imperial Broadloom* case, Henry J. referred to *Re Stuart and Sutterby* and expressed the test as follows:

> The substantive test for the appointment of an interim receiver is that set out in s. 28(1) of the Act, "if it is shown to be necessary for the protection of the estate". The Courts have superimposed on this test other requirements so that the criteria to be met are as follows:
>
> (a) Necessity to protect the estate must be demonstrated by the applicant (s. 28); (b) a strong prima facie case must be shown -- *Re Strain* (1977), 23 C.B.R. (N.S.) 206; *Re Stuart and Sutterby* (1929), 11 C.B.R. 1; (c) as the appointment of a receiver has serious consequences for the debtor in his commercial dealings that may amount to irreparable harm, and as bankruptcy proceedings are quasi-criminal in nature, the Court should exercise extreme caution in appointing an interim receiver: *Re Strain*, supra; *Re Stuart and Sutterby*, supra; *Re Kohen* (1924), 26 O.W.N. 242, [1924] 2 D.L.R. 831 at p. 832, 4 C.B.R. 577 at p. 579 sub nom. *Re Canadian Coal Supply, Ex p. Staples & Bell Inc.*; and *Collver et al. v. Baltzan et al.* (1978), 26 C.B.R. (N.S.) 256.

18 Mr. Bourassa places great emphasis on the failure of the applicant to show that a bankruptcy order is "almost certain" to be made. He submits that the applicant has not met the high onus for a number of reasons, most particularly because:

> * Richards is unable to produce an original of the application form containing the alleged guarantee - there is only a photocopy;
>
> * Richards has no evidence at all concerning the circumstances in which the guarantee was executed;
>
> * The guarantee form is not signed by Richards;
>
> * Richards was not aware of the existence of the guarantee form until after Office Supercentre went out of business;

> * Notwithstanding the alleged execution of the guarantee, Richards repeatedly sought to obtain a personal guarantee from Mr. Konopny - i.e., it did not consider the application form to be a guarantee; and
>
> * Mr. Konopny has no recollection of signing the guarantee.

19 In effect, Mr. Bourassa says that Richards cannot prove the guarantee, it was not aware that a guarantee had been signed and it acted as though it had no personal guarantee from Mr. Konopny.

20 Mr. Bourassa also submits that the application is also flawed on a technical basis because no undertaking as to damages has been given by the applicant and the consent of the proposed receiver has not been filed.

Discussion

21 Section 46(1) of the *BIA* provides that the appointment of a receiver must be "necessary for the protection of the estate of a debtor". I accept the test set out in Houlden and Morawetz, *Bankruptcy and Insolvency Law of Canada,* 4th ed., (Toronto: Carswell, Looseleaf ed., 2009) at p. 2-115:

> The applicant creditor must establish through evidence that: (1) on a *balance of probabilities* the applicant creditor is likely to succeed in obtaining a bankruptcy order; and (2) there is an immediate need for protection of the debtor's estate due to the grave danger that assets will disappear *or the estate is otherwise in jeopardy.* [emphasis added]

22 I also accept that the appointment of a receiver is a serious interference with the affairs of the debtor and the court's discretion must be exercise cautiously.

23 Dealing with the merits of Richards' claim, the document allegedly signed by Mr. Konopny on behalf of his corporation was attached to a "New Account Application" and was entitled "Terms of Credit". Underneath his signature as President, the following appears:

> Form to be completed where company is a limited liability company.
>
> In consideration of Norwestra Sales (1992) Inc. extending credit to the above named business, the undersigned co-covenantor shall be jointly and severally liable as principal debtor and act as guarantor or surety for due payment of all amounts of money payable by the above named customer to Norwestra Sales (1992) Inc.
>
> **Dated** [etc]
>
> **Witness**: [Name] **Signature** of Co-Covenantor: M. Konopny [signature]

24 The signature of the "Co-Covenantor" appears, at first glance, to be similar to the signature of Mr. Konopny. Mr. Konopny does not deny he signed the form. He does not suggest that his signature was forged. He simply says that he has no recollection of signing the form.

25 I am satisfied that the applicant has made out a *prima facie* case that Mr. Konopny signed the guarantee. He may not remember having signed it, but it appears to be his signature. The form

of the guarantee is simple and clear. He guarantees payment of all money due by his company to Norwestra Sales (1992) Inc. Whether the guarantee sat in a drawer in a filing cabinet and whether Richards sought additional security from Mr. Konopny is not relevant to his liability under the guarantee. There may be defences, whether technical or substantive, but those defences will have to be proven and have not been identified to me. Richards has established a meritorious claim, on the balance of probabilities.

26 The second question is whether there is a grave risk that assets will disappear if a receiver is not appointed. Is the estate in jeopardy? Mr. Konopny's previous conduct weighs heavily on my conclusion that there is a real risk of dissipation of the estate if the order sought is not granted. He has demonstrated an intention to defeat his creditors by disposing of his assets in the face of pending proceedings. The last minute settlement with the petitioning creditor has had the effect of pulling the rug out from under Richards and removing the protection that had been put in place for the benefit of all creditors. In my view, there is a real risk that without this protection, Mr. Konopny will continue the engage in the course of conduct that lead to the initial order. In my view, Richards has good reason to feel insecure.

27 While prejudice to Mr. Konopny may be assumed, three things are worth noting: first, he was subject an interim receivership order for some nine months and there is no evidence of undue disruption of his affairs; second, the term of the proposed interim receivership will continue only until the application for bankruptcy has been dealt with, subject to further order of the court; third, Mr. Konopny swears his assets are not being dissipated and identifies no specific prejudice that he will suffer if the order is granted.

28 I should note that, in lieu of the appointment of a receiver, Ms. Henshell was prepared to accept a non-dissipation order. Ms. Bourassa was not prepared to accept such an order. In the circumstances, I am prepared to grant the relief sought.

29 For these reasons, and subject to the conditions that follow, the application for the appointment of an interim receiver over the property of Mr. Konopny is granted. The order shall contain provisions permitting payment of Mr. Konopny's ordinary living expenses and reasonable legal expenses. Until such time as the receivership is in place, Mr. Konopny is restrained from encumbering, transferring or dissipating any of his assets. The order shall issue on the applicant filing (a) an undertaking as to damages, in form acceptable to counsel for the respondent or as approved by the court; (b) the consent of the proposed receiver, M.S.I. Spergel Inc. In the event of any issues in settling the terms of the order, the undertaking or the appointment, submissions may be made to me, care of Judges' Administration.

30 Costs, if not agreed, my be addressed by written submissions.

G.R. STRATHY J.

cp/e/qllxr/qljxr/qlmxl/qlaxw/qlced/qlcal

TAB 2.

2001 CarswellOnt 4122, 29 C.B.R. (4th) 191

C

2001 CarswellOnt 4122, 29 C.B.R. (4th) 191

Battery Plus Inc., Re

In the Matter of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, s. 47, as amended

In the Matter of Battery Plus Inc. and 1271273 Ontario Inc.

Ontario Superior Court of Justice [Commercial List]

O'Driscoll J.

Heard: November 15, 2001
Judgment: November 15, 2001
Docket: Toronto 01-CL-4319

Counsel: *A.E. Kauffman, K. McEachern*, for Laurentian Bank of Canada

G. Tighe, for Domenick Bellisario

S.J. Mann, J. Simpson, for Battery Plus Inc.

Subject: Insolvency

Bankruptcy --- Interim receiver — Appointment

Bank lent money to two corporate borrowers and took security over their assets — Borrowers defaulted on loans — Bank brought application under s. 47(1) of Bankruptcy and Insolvency Act for order appointing interim receiver — Application granted — Bank had sent notice to borrowers as required under s. 244(1) of Act — Borrowers were in default to bank and were no longer able to pay employees or have rent cheques honoured — All attempts by borrowers to raise additional capital to allow them to carry on business had failed — Appointment of interim receiver was required in order to salvage assets of business and security of bank — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 47(1), 47(3), 244(1).

Cases considered by *O'Driscoll J.*:

> *Canada (Minister of Indian Affairs & Northern Development) v. Curragh Inc.* (1994), 27 C.B.R. (3d) 148, 114 D.L.R. (4th) 176 (Ont. Gen. Div. [Commercial List]) — followed

Statutes considered:

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

s. 47 — referred to

s. 47(1) — pursuant to

s. 47(3) — considered

s. 244 — referred to

s. 244(1) — referred to

APPLICATION by bank under s. 47(1) of *Bankruptcy and Insolvency Act* for order appointing interim receiver.

***O'Driscoll J.* (orally):**

1 The Applicant, Laurentian Bank, seeks an order appointing Deloitte & Touche Inc. as Interim Receiver of Battery Plus Inc. (BPI) and 1271273 Ontario Inc. (127). The order is sought under the provisions of s. 47(1) of the *Bankruptcy and Insolvency Act*. With the consent of BPI and 127, Deloitte & Touche Inc. has been their monitor since August 1, 2001. The Bank is a lender to BPI and 127 (Borrowers) and the Bank has security over the assets of the Borrowers. The material filed persuades me that:

a) the required notice under s. 244(1) of the BIA was sent by the Bank to the Borrowers on November 8, 2001,

b) the debts owed by the Borrowers to the Bank are in default;

c) all attempts by the Borrowers to raise additional capital in order to allow BPI to continue to carry on business have failed.

2 Paragraphs 22 and 23 of the affidavit of John Smith, Senior Vice President of the Bank, sworn November 13, 2001, discloses that as of November 7, 2001, the Borrowers owed to the Bank the amount of $5,951,285.81 plus $707,759.05. 127 owns all the shares of BPI. Mr. Badr owns the shares of 127. 127 is guarantor of BPI's loan from the Bank and has itself borrowed money from the Bank.

3 On October 18, 2001, Domenick Bellisario issued a notice under s. 244 of BIA demanding payment of his $1 million loan to BPI. Counsel for Mr. Bellisario is present and supports the Bank's application.

4 In his supplementary affidavit, sworn "on the _____ day of November 2001," Mr. Smith deposes:

[3] I attended the meeting referred to during the afternoon of November 13, 2001. At the meeting no fresh proposal, satisfactory to the Bank, was put forward. The proposal discussed was the same as the proposal previously discussed which would have required the Bank to give up substantial security.

[4] In my affidavit sworn November 13, 2001, I made reference to my concern with respect to the diverted funds (paragraph 63). My concern is now heightened in that there have been no deposits to Laurentian Bank on Friday, November 9, 2001 and Tuesday, November 13, 2001. I estimate that the Friday deposits should have been between $30,000.00 to $40,000.00 and the Tuesday deposits should have been approximately $100,000.00 to

$150,000.00.

[5] In addition, as BPI is now above the limit of its operating facility, the Bank has been, and will be, refusing to honour cheques. BPI will be unable to pay the payroll of its employees (due Thursday and Friday) or have its rent cheques honoured.

5 Indeed, in his affidavit sworn today, Antoine Chahine Badr, the President of BPI and 127 states:

6. As a result of the Bank returning all cheques that have been issued by the Respondents and advising us not to write any further cheques on our bank account, I used funds that were on deposit with other financial institutions for the purpose of preserving the business of the Respondents during my ongoing discussions with the investors and subordinate secured creditors.

6 These actions of Mr. Badr appear to be clearly at odds with the security agreement signed by the Borrowers with the Bank.

7 The material filed and catalogued in the November 13, 2001 affidavit of Mr. John Smith, at paras. 34-47 and para. 53 and in the Factum of the Applicant at para. [25], persuades me that the Borrowers have been unable to re-capitalize. Indeed, there is no "white knight" on the horizon.

8 In my view, although the wording of s. 47(3) of the BIA is disjunctive, the Applicant's material has fulfilled both parts of s. 47(3).

9 Counsel for the Borrowers seeks an adjournment until Monday, November 19, 2001. Why? So that cross-examination may take place of Mr. Smith on his affidavits. I do not wish to be taken as being seen to denigrate the strengths, the products and the by-products of cross-examination, however, in my view, there is no reasonable prospect that anything gleaned on the cross-examination of Mr. Smith will in any way affect the outcome of this application. The cross-examination of Mr. Smith has no hope of turning back the tidal wave that has been demonstrated here. During his submissions, I asked Mr. Mann what would happen in the interim which would keep the business operating on an even keel when we know that BPI's cheques are being turned back at the Bank, that the rent is due, there is a payroll to meet and there are no funds. My recollection is that I did not receive any satisfactory answer.

10 Mr. Mann has brought to my attention a memo from Securitor Canada, a firm employed be Deloitte & Touche. This document is dated November 14, 2001. There are instructions to be put into effect if, as and when the court gave an order appointing an Interim Receiver. Mr. Mann advised me that some of the security staff attended at some of the 88 stores, "jumped the gun" and tried to enter the stores this morning. Mr. Kauffman apologized on behalf of the monitor and advised that Securitor guards were not allowed into the stores and the stores are still open.

11 I agree with Mr. Kauffman that strategic planning is necessary when 88 stores and locksmiths are involved. Sometimes the best-laid plans of men go astray. If it is necessary, I accept the apology and I see no harm done. I do notice that in the November 14, 2001 memo, about a third of the way down the page, it says: "once we have the words to go". As yet, that "word" has not been given but I do not see any contempt on behalf of anyone involved.

12 In referring to s. 47 of the BIA, Mr. Justice Farley said in *Canada (Minister of Indian Affairs & Northern Development) v. Curragh Inc.* (1994), 114 D.L.R. (4th) 176 (Ont. Gen. Div. [Commercial List]), 185:

It would appear to me that Parliament did not take away any inherent jurisdiction from the court but in fact provided, with these general words, that the court could enlist the services of an interim receiver to do not only what "justice dictates" but also what "practicality demands". It should be recognized that where one is dealing with an insolvency situation one is not dealing with matters which are neatly organized and operating under predictable

> discipline. Rather the condition of insolvency usually carries its own internal seeds of chaos, unpredictability and instability. I think it should be emphasized again what I was discussing earlier in my reasons: that an asset of the nature of the Faro mine is not one which can be easily mothballed and insulated from nature affecting its present condition. Rather, it must be constantly attended to so as to avoid adverse environmental deterioration which will not only be very costly to clean up but will create a health and safety hazard.

13 In my view, those words apply mutatis mutandis to the situation before me. The application to adjourn for the purpose of cross-examining Mr. Smith is dismissed.

14 In my view, if nothing else, common sense requires that the order sought under s. 47 of the BIA be granted in order to salvage the assets of the business and the security of the Bank.

15 In my view, the Bank signaled its intentions months ago. The only thing that surprises me on this record is the length of the Bank's forbearance. If there had not been opposition to the motion for the sole purpose of cross-examination, the order sought would have been issued hours ago. I see no reason why the slowing down of the issuance of the order by that argument should prevent the issuance of the order.

16 In the result, order to go as requested in para. 1(a) of the Notice of Motion, dated November 9, 2001, in the terms of a draft order which I have signed.

Application granted.

END OF DOCUMENT

TAB 3

2006 CarswellOnt 3780, 23 C.B.R. (5th) 42

C

2006 CarswellOnt 3780, 23 C.B.R. (5th) 42

Royal Bank v. Canadian Print Music Distributors Inc.

Royal Bank of Canada (Applicant) and Canadian Print Music Distributors Inc., Digital Moon Music + Video Inc., Cantur Trans. Inc., Just Service Express Ltd., Pak-Express Inc., ID Merchandising Group Inc., Millwork by Amati Inc., 1569175 Ontario Limited c.o.b. ID Flooring & Finishing and Secure Distribution Services Inc.

Ontario Superior Court of Justice

Cumming J.

Heard: June 14, 15, 2006
Oral reasons: June 15, 2006
Written reasons: June 21, 2006
Docket: 06-CL-6487

Counsel: Steven Graff, Sam Babe for Applicant, Royal Bank of Canada

Robert Tanner for Respondent

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

Bankruptcy and insolvency --- Interim receiver — Appointment

Interim receiver necessary for protection of debtor's estate and creditor's interests — Nine related debtor companies held lines of credit from bank — Most of debtors' accounts with bank were in overdraft positions in excess of their authorized limits — Investigation showed debtors held several accounts receivable which had extended beyond 90 days — Bank also found several transfers of funds between companies — Bank maintained that haphazard corporate structure had developed, not all of whose member companies were customers of bank — Bank noted weak financial reporting of debtors — Bank initiated repayment proceedings — Bank brought application for appointment of interim receiver — Application granted — Order was necessary for preservation of debtor's estate and interests of bank — Proof of misfeasance not required for appointment — No wrongdoing asserted or established, as at time of proceedings reason for dire financial straits of debtors unclear.

Debtors and creditors --- Receivers — Order appointing receiver

Interim receiver necessary for protection of debtor's estate and creditor's interests — Nine related debtor companies held lines of credit from bank — Most of debtors' accounts with bank were in overdraft positions in excess of their authorized limits — Investigation showed debtors held several accounts receivable which had extended beyond 90

days — Bank also found several transfers of funds between companies — Bank maintained that haphazard corporate structure had developed, not all of whose member companies were customers of bank — Bank noted weak financial reporting of debtors — Bank initiated repayment proceedings — Bank brought application for appointment of interim receiver — Application granted — Order was necessary for preservation of debtor's estate and interests of bank — Proof of misfeasance not required for appointment — No wrongdoing asserted or established, as at time of proceedings reason for dire financial straits of debtors unclear.

Statutes considered:

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

s. 47(1) — pursuant to

s. 47(3) — considered

s. 244(1) — referred to

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

s. 101 — referred to

APPLICATION by creditor bank for appointment of receiver in bankruptcy.

***Cumming J.*:**

The Application

1 The Applicant, the Royal bank of Canada (the "Bank"), applies for an Order appointing Grant Thornton Limited ("GTL") as interim receiver, and receiver and manager, under s. 47 (1) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as am. ("*BIA*") and s. 101 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43, as am., to protect the Bank's interests, among others, in the Respondents.

2 The nine related Respondents ("Debtors") are each indebted for significant amounts to the Applicant to a total of some $6.5 million pursuant to Credit Facility Agreements, payable on demand, secured by General Security Agreements ("GSAs"). As well, each of the Debtors has given a guarantee to the Bank in respect of the indebtedness of some of the other Debtors. The indebtedness through such guarantees is also secured by the GSAs.

3 There is common ground that the requisite demands for repayment of the loans and under the guarantees have been made, and that Notices of Intention to Enforce Security, pursuant to s. 244(1) of the *BIA*, were issued to each Respondent, the specified notice periods have expired, and that there has not been repayment of any of the loans.

4 There is also common ground that negotiations took place in May between the Bank with the Respondents' former counsel, and certain parties related to the Respondents, in respect of the Bank's concerns, toward a formal forbearance agreement being executed, but the copy circulated by the Bank's counsel for execution by June 9, 2006, was not executed by the Respondents or their related parties.

5 Mr. Art Goodine, manager in the Special loans and Advisory Services Group of the Bank, has provided a 16 page affidavit in support of the Application.

6 Mr. Goodine states that the Bank began to have concerns about the sufficiency of its security about April 25, 2006 when the Bank's Corporate Investigation Services ("CIS") was alerted to a number of irregular banking transactions involving the Respondents. These transactions involved a series of returned cheques issued between the companies and related parties, deposited to accounts of the companies at the Bank and drawn on accounts of related parties at the Bank of Nova Scotia. As a result of these returned items, most of the Respondents' accounts with the Bank were in overdraft positions in excess of their authorized limits.

7 Mr. Goodine says that the resulting examination evidenced that since the middle of April, 2006, the majority of transactions in both quantity and dollar value in most of the Respondents' bank accounts has involved cheques drawn on or payable to related parties. Funds were transferred between companies and related parties operating in different industries, without any obvious business relationship. There were a number of instances of funds being deposited to an account from one company on one day, followed by a payment back to that same company on the following day. Other than payments from related parties, most of the companies did not have a significant external source of funds. Once the Bank placed constraints upon the Respondents' accounts and began to return cheques, the overall combined overdraft position of the Respondents' accounts increased significantly.

8 As a result of the Bank's findings, the Bank retained Price WaterhouseCoopers Inc. ("PWC") to investigate the Respondents' financial positions and prepare a report for the Bank. PWC attended at the Respondents' premises between May 2 and 23, 2006.

9 PWC found that there extensive accounts receivable past due more than 90 days, and considerable accounts payable and accounts receivable were due from related parties. PWC also found that the margin availability calculations provided by management had been considerably overstated.

10 PWC made preliminary conclusions, including: the enterprise has grown in a haphazard fashion into a number of largely unrelated businesses, some of which are not customers of the Bank, there is an unusually high level of intercompany transactions, and the internal financial reporting capacity is "very weak". PWC says it was unable "to obtain sufficient verifiable information to confirm whether" the businesses were profitable at present.

11 PWC also says that its personnel were met outside the Respondents' building on May 23, 2006 and told by Mr. Mahmood Hemani, a principal of the Respondents, that it was felt PWC should no longer continue its investigation.

12 Mr. Goodine says there is some suggestion from the company records that some of the companies are being used to sustain others in meeting payrolls. Mr. Goodine also states that "When the Bank has communicated to the Companies that there are insufficient funds in the Company Bank accounts to cover payroll, the companies have purported to cut down the payroll list".

Disposition

13 Section 47 (3) of the *BIA* provides for the appointment of an interim receiver under s. 47 (1) only if it is shown to the Court to be necessary for the protection of the debtor's estate or the interests of the creditor who sent the notice under s. 244 (1). In my view, the Bank's evidence establishes by a preponderance of evidence that an interim receivership is necessary for both the protection of the debtor's estate and for protection of the interests of the Bank.

14 The Bank has met the onus of establishing a strong *prima facie* case of bankruptcy inasmuch as the respondents cannot meet their liabilities as they fall due. The evidence in support of the Application establishes on a balance of probabilities that the Bank will likely succeed in obtaining an order for a permanent receivership on the return of the Application.

15 The Bank has proven the need for immediate protection of the Debtors' estates. The evidence shows there is a

significant danger that assets may disappear and the estates may be adversely affected in the absence of protection through an interim receiver.

16 Counsel for the Respondents submits that the Bank has not proven that there is actual misfeasance and wrongdoing such that assets are being misappropriated or dissipated. The Respondents assert that proof of such misfeasance is a prerequisite to appointing an interim receiver. I disagree.

17 Because the possible explanations underlying the financial records of the Respondents are unknown, or at least uncertain, at this point in time, it cannot be said with any certainty that wrongdoing on the part of the Respondents has been established. Nor does the Bank so assert.

18 However, in my view, and I so find, the Bank's evidence has established with certainty on a balance of probabilities the need for an immediate interim receivership to assure conservation of the Respondents' assets, and hence, protection of the interests of the Bank through its security.

19 For the reasons given, I granted on June 15, 2006, the Application for an interim receiver to be appointed under s. 47(1) of the *BIA*, with these written reasons to follow. The Application for a permanent receivership is adjourned to July 5, 2006. I shall remain seized of the matter.

Application granted.

END OF DOCUMENT

Red Ash Investments II Limited Partnership	and	KRAUS INC., KRAUS CANADA INC., STRUDEX FIBRES LIMITED and 538686 B.C. LTD
Applicant		Respondents

Court File No. C12-9731-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

PROCEEDING COMMENCED AT
TORONTO

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