SUPREME COURT OF NOVA SCOTIA
Citation: Canadian Imperial Bank of Commerce v. Fawson, 2012 NSSC 444

Date: 20121219
Docket: SK 285018
Registry: Kentville

Between:

Canadian Imperial Bank of Commerce

Plaintiff

v.

James Robert Fawson, Lynda Fawson, David Neville and Anna St. Clair

Defendants

Decision

Judge: The Honourable Justice Kevin Coady

Heard: December 3, 2012

Decision: December 19, 2012

Counsel: Keith MacKay, for James & Lynda Fawson
Sean Foreman, for Anna St. Clair

By the Court:

BACKGROUND

[1] In 2001 a group of individuals incorporated River John Oceanfront Resort Limited (R.J.O.R.). The defendant's Fawson, Fawson and St. Clair were part of that group. The defendant Neville was an acquaintance of the group. The business plan of RJOR was to acquire land and to develop a cottage rental business. Michael Dudka was the driving force behind this enterprise. There were several other investors/shareholder in addition to Fawson, Fawson and St. Clair.

[2] RJOR commenced acquiring land and building chalets. In 2003 it became apparent that RJOR required capital to drive the development. RJOR was not in a position to borrow sufficient funds. A plan was hatched that resulted in four lots of RJOR being conveyed to the defendants. The defendants then secured a $200,000 mortgage from the Canadian Imperial Bank of Commerce (CIBC). The proceeds of the mortgage were paid to RJOR.

[3] On November 5, 2003, Mr. Dudka's lawyer drafted a trust agreement that reflected RJOR's arrangement with the defendants. The document was signed by all four defendants. The following represents the terms of that agreement:

> •The defendants would not pay anything to RJOR for the land transferred to them.
>
> •The defendants would not deal with the land in any way other than to mortgage it.
>
> •The defendants would deliver the mortgage proceeds to RJOR to use to develop its business.
>
> •RJOR would make all payments on the mortgage and the defendants were not to be personally liable.
>
> •The defendants were to transfer the four lots to RJOR when the mortgage was repaid.

[4] The following additional term appeared in the trust agreement:

> •This [agreement] is void if River John fails to maintain the CIBC encumbrance in good standing.

The agreement encouraged all four defendants to seek independent legal advice and offered them no opinion as to the viability of the arrangement or the risks attendant thereto.

[5] The arrangement was implemented in all respects. RJOR serviced the mortgage until 2006 and continued with their development. A point in time came when RJOR was financially unable to service the mortgage. CIBC commenced a foreclosure action against the four defendants. On July 30, 2008 a foreclosure order issued with a settled sum of $239,591.88. The court subsequently issued an amended order with a settled sum of $225,210.33

[6] In time the property came to a public auction. Two bidders participated in the auction. Ms. St. Clair bid in order to drive up the price to avoid a deficiency judgment and to protect other obligations owed to her by RJOR. Mr. Dudka's representative bid the property to $335,000 on behalf of a company owned by Mr. Dudka. The latter was the successful bidder and effectively Mr. Dudka became the owner of the subject lots without an encumbrance. CIBC was fully paid and the sale produced a surplus of $88,608.45. Given there was no agreement among the defendants as to distribution, the funds were deposited with the court.

[7] On March 23, 2010, a consent order issued which transferred 3/4 of the surplus ($66,663.56) to RJOR. All four defendants consented to this partial

distribution. These funds were given to Mr. Dudka to apply to a judgment he held against RJOR.

[8] On April 11, 2012 Fawson, Fawson and Neville filed a motion for an order transferring the remaining $22,221.18 to RJOR. The applicants all indicated they had no claim to these funds. They all acknowledged that given RJOR was insolvement, the funds would go to Mr. Dudka to be applied to his RJOR judgment. Ms. St. Clair opposed the motion and claimed she was entitled to these funds.

[9] There are a number of other factors that motivated Ms. St. Clair:

> •Lynda Fawson also held title to lands for RJOR that were mortgaged for the benefit of RJOR. The company ceased making those mortgage payments and in 2006 the bank foreclosed. Ms. Fawson suffered a $54,718.88 deficiency judgment.
>
> •Ms. St. Clair loaned RJOR $27,500 by way of an unsecured promissory note. That obligation is still outstanding.
>
> •Ms. St. Clair loaned RJOR monies from her self-directed RRSP. It was secured by a first charge against other RJOR lands. In 2010 Ms. St. Clair foreclosed and obtained a judgment for $115,957.37.

- Shortly after the CIBC foreclosure, Mr. Dudka filed a claim against RJOR seeking payment of a loan. In time RJOR signed a consent order in the amount of $171,361.88 in favour of Mr. Dudka.

- On the same date another investor filed a claim against RJOR seeking payment on an outstanding promissory note. Once again RJOR signed a consent order in the amount of $40,533.33 in favour of one James Hannifen.

- The evidence suggests that the RJOR property that Mr. Dudka's company bought at foreclosure is worth $6 - $700,000.

It is Ms. St. Clair's view that given the above, the surplus funds represent her only chance to recover her $17,500 loan plus interest.

CIVIL PROCEDURE RULE 72:14:

[10] A party or a subsequent encumbrancer may apply for a distribution of surplus funds arising out of a foreclosure. Rule 72.14(3) and (4) state:

> (3) A subsequent encumbrancer or other party may make a motion for payment of the surplus funds.
>
> (4) A judge may take accounts, make inquiries, tax costs and order distribution of the surplus.

I am satisfied that Fawson, Fawson and Neville have standing to bring this motion.

APPLICANTS POSITION:

[11] The applicants argue that the trust agreement dictates that the surplus belongs to RJOR. It is their view that the beneficial interest in the subject lands remained with RJOR notwithstanding the transfer of the legal title to the defendants.

[12] The applicants argue that the surplus funds stand in the place of the equity of redemption. They cite *Credit Union Atlantic Ltd. v. Isenor*, 2012 NSSC 183 where Justice Moir stated at paragraph 3:

> Surplus funds after foreclosure and sale stand in the stead of the foreclosed equity of redemption.

The applicants stipulate that these funds are not theirs and belong to RJOR.

ANNA ST.CLAIR'S POSITION:

[13] Ms. St. Clair argues that she is not advancing an equitable claim, rather she has a legal claim to the funds. She suggests that the actual mortgagors own any

equity of redemption. She argues that the only way RJOR could be entitled is if the trust agreement remains in effect and provides for such.

[14] Ms. St. Clair argues that she has always asserted her 1/4 interest in the surplus funds. She states that such is supported by her 2010 agreement to release the other 3/4s of the surplus funds.

THE 2003 TRUST AGREEMENT:

[15] There is no doubt in my mind that the 2003 document was a trust agreement. It clearly states that "this [agreement] is void if River John fails to maintain the CIBC encumbrance in good standing." This document was drafted by RJOR's solicitor. There is nothing in the document that limits the import of the above referenced sentence. There is no dispute that RJOR failed to pay on the CIBC mortgage. I conclude that the trust agreement ended when RJOR defaulted on their obligations to service the CIBC mortgage.

THE 2006 LETTER AND COMPANY MINUTES:

[16] On January 30, 2006, RJOR sent a letter to shareholders as a result of the companies financial difficulties. This letter advanced three options for RJOR. The first two options were bankruptcy and refinancing. The third option was stated as follows:

> Surrender all the lands and buildings to the aforementioned individuals as of March 1, 2006 thus allowing them to protect themselves and their good credit by liquidating the entire assets over a period of time or by continuing to operate the business as they see fit. We have a duty as shareholders and as a company to protect these people. They are willing to put the financial resources in place to pay off all past due real property taxes and liabilities associated with the buildings and land. They will also release us, as shareholders, from everything on March 1, 2006. Any bills up to March 1, 2006 belong to RJOR Ltd. Any bills after March 1, 2006 will belong to the six people aforementioned.

[17] A special shareholders meeting was held on February 16, 2006 at which time the following resolution was passed:

> Option #3. Be it so moved that the shareholders of RJOR Ltd. give authority to the group of shareholders and David Neville, who the company is indebted to by mortgages, loans, or any other form of debt, the following lands and buildings allowing them to have control of generating financial resources, operating the business, liquidating the entire assets, contingent upon the proper approval of any government agencies, securities commission or other laws of the province of Nova Scotia.

Motioned by Mike Dudka
Seconded by Bill Graham

The above letter and resolution supports the position that the 2003 trust agreement was viewed by all the players as terminated when RJOR ceased paying the CIBC mortgage.

CONCLUSION:

[18] I dismiss the motion of Fawson, Fawson and Neville. I order the prothonotary to release the remaining surplus plus interest to Ms. St. Clair. I will hear the parties on costs should they be unable to agree.

J.