Court of Queen's Bench of Alberta

Citation: Servus Credit Union v Sulyok, 2018 ABQB 860

Date:
Docket: 1703 09026
Registry: Edmonton

Between:

Servus Credit Union Ltd

Plaintiff/Appellant

- and -

Daniel Ernest Sulyok and Chelsey Rae Tomlinson

Defendants/Respondents

Reasons for Judgment
of the
Honourable Madam Justice J.E. Topolniski

Table of Contents

Introduction 3

Facts 3

Master's Decision 4

Grounds of Appeal 4

Standard of Review 5

Analysis 5

1. The Legislative Framework 5
   a. Purpose and Interpretation of the BIA 5
   b. Section 84.2 5
   c. Section 178 6
   d. Provable claims 6
2. Overview of the parties' positions 7
3. Section 84.2 precludes enforcement when a contract is in good standing 7
   a. Servus bears the onus of establishing that the mortgage was in good standing 7
   b. The mortgage was in default 8
4. Reaffirmation 9
   a. Reaffirmation by continued payment (the *Seaboard* Approach) 9
   b. Cases Requiring Novation and More 11
   c. Reaffirmation does not require fresh consideration 15
   d. The Senate Reports 16

Conclusion on the Correct Approach 17

Costs 18

Introduction

[1] Servus Credit Union Ltd ("Servus") appeals a Master in Chamber's decision refusing a deficiency judgement in a high-ratio mortgage foreclosure.

[2] Arguing that a secured creditor with a provable claim in the mortgagor's bankruptcy can enforce a personal promise to pay after the bankrupt's discharge, Servus' focus is on the interplay of sections 178(2) and 84.2 of the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 (BIA). Section 178(2) concerns the release of certain debts on discharge from bankruptcy (such that the creditor is unable to enforce). Section 84.2 precludes a creditor from terminating or amending a contract with a bankrupt if the contract is in good standing.

[3] For the reasons that follow, I grant Servus' appeal.

[4] I conclude that s 84.2 is not relevant as there was a default, albeit a relatively minor one, in the mortgage during the currency of the bankruptcy. Servus chose (perhaps understandably) not to rely upon the default to ground foreclosure proceedings, but that forbearance enabled Mr. Sulyok to retain the property until after his discharge from bankruptcy, and the only live issue is whether, despite not having enforced earlier, Servus could still enforce on the personal promise to pay any deficiency.

[5] I conclude that the discharge from bankruptcy did not release Servus' claim for the deficiency; rather the parties' conduct indicated that the contract itself was continued, and that it continued to regulate the parties' relationship post- discharge. While there is case law and academic commentary recommending that the notion of implied reaffirmation of a contract be ended, Parliament was aware of this concern when the BIA was last amended and elected not to do so. As a result, the parties effectively reaffirmed the promise to pay any deficiency sustained by Servus in the event of enforcement proceedings, and Mr. Sulyok is liable for it. This approach balances the rehabilitative goals of giving honest, but unfortunate debtors a fresh start and promoting fiscal responsibility. It further balances the interests of all stakeholders.

[6] Amending the BIA to address express reaffirmation is a task for Parliament, which it has chosen not to do. I have recommended that the Superintendent of Bankruptcy consider requiring licensed insolvency trustees to include counselling on the topic of reaffirmation and continuing liability on a personal promise to pay as part of their general counselling responsibilities under the BIA and pursuant to her directives.

[7] Finally, since the Master should have granted the deficiency judgment against Mr. Sulyok, I have found that Servus is entitled to its costs as provided for in the mortgage and promise to pay.

Facts

[8] The essential facts, set out in chronological order below, are few.

[9] In 2007, the respondent, Mr. Sulyok and his then spouse, Ms. Tomlinson, granted a high ratio mortgage to Servus, which provided that the debtors would be liable for any deficiency under the provisions of the *Law of Property Act,* RSA 2000, c L-7 and solicitor-client costs in the event of enforcement.

[10] When Mr. Sulyok and Ms. Tomlinson separated in the spring of 2015, Ms. Tomlinson remained in the property until the late summer of 2015, and then rented it to tenants. She made all of the monthly payments from April 2015 until January 2017.

[11] In February 2016, Mr. Sulyok made an assignment in bankruptcy. Servus filed a proof of claim as a secured creditor only. The circumstances prompting the filing are unknown.

[12] Mr. Sulyok was discharged from bankruptcy on November 30, 2016.

[13] The mortgage was in default in late January 2017. Then, Mr. Sulyok informed Servus that he planned to move into the property, which he did by March 20, 2017. Also by this date, Mr. Sulyok had cured an earlier default arising from non-payment of condominium arrears, and made a part payment on outstanding mortgage arrears.

[14] Servus commenced foreclosure proceedings in May, 2017 after Mr. Sulyok advised it that he would make no further payments to cure outstanding defaults and was abandoning the property.

[15] Servus obtained an Order for Sale to Plaintiff, also commonly called a Rice Order, with a $73,199.92 deficiency (the Deficiency), and later sought judgement against both Mr. Sulyok and Ms. Tomlinson for the Deficiency.

[16] The Master refused to grant judgement against Mr. Sulyok for the Deficiency and ordered costs against Servus: ***Servus Credit Union Ltd. v Sulyok,*** 2017 ABQB 611.

Master's Decision

[17] The Master framed the issue as whether Servus could enforce the discharged bankrupt's personal promise to pay. She considered the facts, the language of s 178, the "fresh start" principle, and academic commentary on reaffirmation. She also reviewed the conflicting lines of authority on implied reaffirmation; the first of which directs that a promise to pay is not released by bankruptcy if payments were made during the bankruptcy or after discharge. The second line requires evidence of the debtor directing his or her mind to continuing the personal covenant which, in some cases, is coupled with the need for fresh consideration.

[18] In the result, the Master adopted the second approach, finding that the right to sue on a provable claim requires proof of mutual consideration and proof that the parties, particularly the debtor, directed their minds to the continuation of personal liability: paras 11, 30-35. Lacking evidence of either, she ruled that deficiency judgment was unavailable and Servus was liable to pay Mr. Sulyok's costs. As against Ms. Tomlinson, she granted the deficiency judgement and found that she, like Servus, should bear her own costs.

[19] Section 84.2 was not argued before the Master, and she was not informed that a 2003 Senate Committee report recommended prohibiting all reaffirmation agreements, a recommendation Parliament chose not to follow when the BIA was last amended in 2009.

Grounds of Appeal

[20] The grounds of appeal are that the Master erred by 1) concluding that the Deficiency was "released" or "extinguished" on Mr. Sulyok's discharge from bankruptcy; 2) awarding party – party costs to Mr. Sulyok; and 3) directing Servus to bear its own costs.

Standard of Review

[21] The standard of review of a Master's decision on appeal is correctness on all issues: ***Bahcheli v Yorkton Securities Inc,*** 2012 ABCA 166 at para 30; ***Axcess Mortgage Fund Ltd v 1177620 Alberta Ltd,*** 2018 ABQB 626 at para 38.

Analysis

1. The Legislative Framework

a. Purpose and Interpretation of the BIA

[22] The BIA is designed to give debtors and creditors certainty in their dealings with one another. It serves two distinct goals – the equitable distribution of a bankrupt's assets among the estate's creditors and the financial rehabilitation of insolvent individuals: ***Husky Oil Operations Ltd v Minister of National Revenue***, [1995] 3 SCR 453 at para 7. It is a commercial statute that is to be broadly interpreted in its entire context and harmoniously with its object and scheme: ***Amateur Youth Soccer Association v. Canada Revenue Agency,*** 2007 SCC 42, [2007] 3 SCR 217 at para. 16; ***Port Alice Specialty Cellulose Inc. Estate (Trustee of) v. ConocoPhillips Co,*** 2005 BCCA 299, 41 BCLR (4th) 259 at para 25.

b. Section 84.2

[23] Contractual provisions permitting termination solely based on insolvency are called *ipso facto* clauses.

[24] Section 84.2, which came into force in 2009, prevents the termination or amendment of an agreement with an individual by reason only of an individual's bankruptcy or insolvency. Put another way, a contracting party cannot rely on an *ipso facto* clause to terminate or amend a contract with a natural person who is either bankrupt or insolvent. It reads:

> No person may terminate or amend — or claim an accelerated payment or forfeiture of the term under — any agreement, including a security agreement, with a bankrupt individual by reason only of the individual's bankruptcy or insolvency.

[25] A creditor can apply to the Court for relief from the restriction if it causes significant financial hardship: s 84.2(6). Moreover, the prohibition does not require the extension of further credit to the bankrupt: s 84.2 (4).

[26] A 2005 Senate committee report on banking, trade, and commerce expresses "disappointment with the [rushed] process" by which Bill C-55 (which led to the 2009 amendments to the BIA) arrived in the Senate, noting that there was an inadequate opportunity to properly review the Bill: *Standing Senate Committee on Banking Trade and Commerce Report on Bill C-55 (an Act to Establish Wage Earner Protection Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and make consequential amendments to other Acts),* dated November 24, 2005 (*2005 Senate Report*).

[27] A *Clause by Clause Briefing Book* describes the general rationale for s 84 as ensuring that agreements in good standing be respected by all parties, and that the

> … individual bankrupt who is attempting to obtain a "fresh start" will not be unreasonably evicted from the family home, denied basic and essential services,

> or denied other benefits to which the bankrupt would otherwise be entitled by reason only of the bankruptcy or insolvency.

(See also: Lloyd W. Houlden, Geoffrey B. Morawetz, and Janis P. Sarra in *The 2017-2018 Annotated Bankruptcy and Insolvency Act,* (Toronto: Thomson Reuters, 2017) (Holden, Morowetz, and Sarra) at p 555.)

[28] The *Clause by Clause Briefing Book* also states that s 84.1 provides protection for the bankrupt's interests, and that

> [T]he co-party retains the right to terminate an agreement with the bankrupt for any reason but for the bankruptcy filing, and that the reform will enhance the estate of the bankrupt while not harming the interests of the co-party to the agreement."

c. Section 178

[29] Section 178(2) provides that, subject to specific types of provable claims deemed by Parliament to warrant the continuation of a creditor's right to enforce claims described in s 178(1), none of which apply in this case, an order of discharge releases the bankrupt from all claims provable in bankruptcy. Put simply, this means that creditors are unable to enforce on any claims unless they fit within s 178(1): ***Schreyer v. Schreyer***, [2011] 2 SCR 605, 2011 SCC 35 at para 21; ***Alberta (Attorney General) v. Moloney,*** [2015] 3 SCR 327, at para 66. Stated another way, while the claim is not "extinguished", it cannot be acted on.

[30] The purpose of this is explained in ***Moloney*** at para 77:

> ...[T]he language of s. 178(2) makes it clear that the purpose of this provision is to give effect to one of the goals underlying the *BIA* regime — the financial rehabilitation of the debtor — by releasing "the bankrupt from all claims provable in bankruptcy". In other words, s. 178(2) is aimed precisely at providing the bankrupt with a fresh start.

d. Provable claims

[31] Section 121 of the BIA provides:

> All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or **to which the bankrupt may become subject before the bankrupt's discharge** by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act. (Emphasis added)

[32] To be a provable claim, a debt or liability must be due either at law or in equity by the bankrupt to the person seeking to prove a claim: ***Re Excelsior Electric Dairy Machinery Ltd*** (1922), 2 CBR 599, [1923] 3 DLR 1176 at para 8 (Ont SC). Applying ss 121 and 135 of the BIA, the Supreme Court of Canada in ***Schreyer*** (at para 26) held that the claim will be deemed to be provable if: 1) the debt exists and can be liquidated; 2) the underlying obligation exists as of the date of bankruptcy; and 3) no exemption applies: at para 26.

[33] A secured creditor need not file a proof of security unless required to do so under demand of a trustee to prove its security under s 128(1). Here, Servus filed a proof of claim as a secured creditor holding assets of the debtor valued $227,678.26 and attaching a copy of the mortgage. It

did not claim a deficiency as an unsecured creditor. Whether it did so at the behest of the trustee pursuant to s 81(4) or otherwise is unknown.

2. Overview of the parties' positions

[34] Mr. Sulyok urges that s 84.2 is a red herring, and the plain language and intent of s 178(2) to give discharged bankrupts a fresh start is the key. The plain language of s 178 means that Servus' claim is unenforceable.

[35] Although s 84.2 creates a hardship on creditors, this was Parliament's intent. The need for guidance and certainty requires putting an end the notion of implied reaffirmation in all circumstances. The Master was correct in finding that if permissible at all, reaffirmation must be expressed and there must be fresh consideration – facts that the lender, who is best positioned to establish, must prove.

[36] Servus contends that because consumer lending is critical to the economy and guidance is required, this case should not be viewed as a "red herring case". It argues that the judicial lens should not be trained on the fresh start principle alone, but rather, on maintaining the status quo. Since s 84.2(1) of the BIA takes away the right to terminate a contract by reason of bankruptcy alone, creditors have no ability to revive the bankrupt's personal liability by proposing a new contract based on forbearance, and is effectively left with no recourse. Instead, the bankrupt holds all the cards. Servus argues that the cases decided before s 84.2 can no longer be considered good law.

[37] Servus urges that the onus should be on the bankrupt (with the aid of counselling by the trustee) to promptly elect to continue with a contract taking its benefits and burdens, or to renounce it. It considers the notion that a lender bears the onus of establishing express reaffirmation and requiring fresh consideration as preposterous as it fails to balance the parties' interests, and penalizes the lender for failing to act on even the most minor default, which is contrary to the bankrupt's interests. Moreover, it benefits a bankrupt who fails to pay by relieving him of the promise to pay irrespective of the circumstances. Putting the onus on the lender to prove fresh consideration, other than forbearance, is impractical and unrealistic since the only thing a lender could offer to induce a bankrupt would be better terms.

3. Section 84.2 precludes enforcement when a contract is in good standing

[38] Section 84.2 does not preclude a contracting creditor from relying on an *ipso facto* clause if the contract is in default. Accordingly, if there was a default and Servus elected not to enforce, it cannot now complain that s 84.2 negatively affected its rights.

[39] The parties disagree as to whether the mortgage was in default before Mr. Sulyok's discharge.

[40] Servus contends that, at best, the evidence is muddy and cannot support such a finding. Mr. Sulyok urges that evidence of default is discernable from the affidavit of Ms. Tina Sverk, a loans officer with Servus.

a. Servus bears the onus of establishing that the mortgage was in good standing

[41] As Servus relies on s 84.2 as the impediment to terminating, renegotiating, or otherwise reaffirming a mortgage in good standing, it bears the onus of establishing that this mortgage was, in fact, in good standing. While one would expect bankrupts undergoing a rehabilitative process

to be aware of the status of their mortgage obligations; in many, if not most cases, that might amount to wishful thinking. In any event, the lender is best able to readily produce the necessary documentation.

b. The mortgage was in default

[42] The mortgage calls for $1,227.53 installment payments on the first day of each month. It also provides that all overdue interest is treated as principal and bears compound interest.

[43] In her July 25, 2017affidavit, Ms. Sverk deposes that the "mortgage had been in arrears from shortly after the time it was granted in 2007, including the defendants' failure to pay condominium fees, but the arrears were always resolved until the last arrears which lead to the within foreclosure action."

[44] At first blush, it appears that these "last arrears" accrued between December 9, 2016 and late March, 2017(after the discharge on November 30, 2016); however that is not crystal clear as Ms. Sverk also deposes to receiving a January 25, 2017 demand letter from the mortgagee's condominium corporation on February 1, 2017 concerning outstanding condominium and legal fees, the calculation of which suggests outstanding monthly condominium fees (alone) exceeding three months. In any event, shortly thereafter Mr. Sulyok made a part payment on the amount claimed by his condominium and indicated to Servus that he would pay the balance within a few days.

[45] A "Mortgage Statement for Discharge Purposes" exhibited in an affidavit of default made by Ms. Sverk on May 23, 2016 indicates total arrears of $5,962.50 as at May 5, 2017. Another exhibit, a partly produced document entitled "Captivation", contains these entries:

- 07 Nov 2016 "late fee" (interest $48) with a corresponding entry under the heading "Interest" ($48)
- 07 Oct 2016 "late fee (arrears 1491.94)" with a corresponding entry under the heading "Interest" (48.00)
- 26 Sep 2016 "condo arrears recovery" with a corresponding entry under the heading "Interest" 2,295.74
- 06 Sep 2016 "late fees (arrears 2295.74) with a corresponding entry under the heading "Interest" (48.00)

[46] These entries are not explained by the deponent. However, the October 07, 2016 entry specifies that it is a charge relating to arrears. Like the subsequent entry in November, it addresses a nominal late fee charge. The entry concerning recovery of "condo arrears" in September indicates pre-existing arrears, which constitute a default under Clause 30(d) of the mortgage.

[47] Facially, all of these entries indicate defaults, albeit nominal ones, in addition to the mortgage arrears of an unknown value in May 2016 that appear to have been later cured. In the result, s 84.2 did not preclude Servus from taking action to enforce on the mortgage.

[48] I make two observations. First, Servus could not be faulted for inaction concerning defaults arising from overdue condominium fees accrued in November 2016 as it was unaware of them until after the discharge. Second, while the rationale for s 84.2 is laudable, this case exemplifies a potentially unfortunate (and very likely unintended) consequence of forcing lenders to act on the most minor of deficiencies if, as the Master found, the debt is released under s 178(2) and reaffirmation requires that it be expressed and accompanied by fresh consideration.

[49] I turn next to an overview of the authorities addressing s178.

4. Reaffirmation

a. Reaffirmation by continued payment (the *Seaboard* Approach)

[50] ***Seaboard Acceptance Corporation v Moen*** (1986), CBR (NS) 143, [1986] BCJ No 87 (BC CA) is the first reported case concluding that the test for post-discharge survival of a personal promise to pay is whether the bankrupt continued to make payments on the debt. The bankrupt entered into a long-term lease for a vehicle. She did not inform the lessor that she was in bankruptcy, but kept the payments in good standing throughout the bankruptcy and for a period after her discharge. The lessor successfully sued for a deficiency on her personal promise to pay when she later defaulted. In dismissing the appeal, Lambert JA said this at paras 17-18:

> ... Under what basis was that possession retained and on what basis were those payments made? In my opinion, the proper view is that the contract continued throughout the bankruptcy and continued after the discharge from bankruptcy; it was never terminated in accordance with its provisions for termination, and the fact that there might have been a claim provable in bankruptcy, or that a claim provable in bankruptcy might have been made, does not affect the fact that the contract itself continued and continued to regulate the relationship of the parties after the discharge from bankruptcy.
>
> In my opinion, what occurred in this case was not, strictly speaking, a novation, as that term is properly understood, but was merely a continuation of the contract, and a continued abiding by the terms of the contract that had been made between the parties. In effect, the contract was endorsed by the defendant after the discharge.

[51] A series of mortgage foreclosure cases follow the ***Seaboard*** Approach.

[52] In ***Manulife v Planting*** (1996), 43 CBR (3d) 305, 68 ACWS (3d) 20 (ON SC), Manulife brought two actions against a husband and wife, one on a promissory note and a mortgage granted by the wife, and executed by the husband as spouse (action #71558/96), and a second action on a guarantee and mortgage on the same property (action #71559/96). The mortgagors made mortgage payments throughout their bankruptcy and for some three years after their discharge. The Court found them liable for the deficiency in 71559/96 because of their continued payments, noting that that creditor did not prove its claim in the bankruptcy. In action 71558/96, however, the Court found there was no liability against the husband. There were two subsequent appeals of the decisions. Although confusing, it appears that the appeal in 71558/96 was dismissed without reasons: [1998] OJ No 73 (CA), while the appeal in 71559/96 was granted with a finding that the husband was not liable because he was not a guarantor, but executed only as a spouse: [1998] OJ No 74.

[53] In both ***Seaboard*** and ***Manulife***, payments were continued after discharge. It may be less clear whether payments made only in the pre-discharge phase have the same effect. For example, in ***CIBC Mortgage Corp v Stenerson,*** [1998] ABQB 482, one of the co-mortgagors made an assignment in bankruptcy, made payments on the mortgage for seven months of the bankruptcy period, and was discharged about two months after the last payment. The lender obtained a Rice Order and deficiency judgements against both co-mortgagors. On appeal, Hart J followed ***Seaboard***, finding that the mortgagor had affirmed the contractual relationship by making certain

payments before her discharge. The Court did not address whether it mattered that the payments ended before the discharge.

[54] The mortgagors in ***CIBC Mortgage Corp v Coleski***, 180 NSR (2d) 2; 13 CBR (4th) 17 (NS SC) kept their mortgage in good standing throughout their bankruptcies and for a period thereafter. Following ***Seaboard*** and ***Stenerson***, the Court noted that the mortgagors benefitted from being able to remain in the property during the bankruptcy and reducing the lenders' claim by their payments.

[55] However, I do not find ***Coleski*** to be particularly persuasive because the Court's observation is *obiter dicta*. The Court found that the mortgagors did not have standing to contest the deficiency, but considered the BIA argument because it was "somewhat novel."

[56] In ***Bridgewater Bank v Simms,*** [2011] BCSC 1453, Master Keighley considered ***Seabord***, ***Planting***, ***Stenerson***, ***Coleski***, and the unreported decision in ***Royal Bank of Canada v. Paul Douglas Nolan and Gina Marie Nolan***.

[57] In both ***Simms*** and ***Nolan,*** the debtors had maintained their mortgages in good standing throughout their bankruptcies. In the former, the lender filed a proof of claim. In the latter, it did not. In both, liability ensued on the deficiency on the basis of affirmation. The Court in ***Simms*** specifically addressed benefits and burdens: at paras 19 and 23.

[58] The question of whether payment is made during the bankruptcy is addressed in ***Dament (Re),*** 2015 ONSC 7960, a case involving a motor vehicle lease. There, the bankrupt told the lessee (through his trustee) that he wanted to keep the car and would continue the payments. He kept the car. He did not make any payments, but his estranged wife, who was a guarantor, did.

[59] At the bankrupt's discharge hearing, his estranged wife sought some form of relief, the nature of which is not readily discernable from the case report, but could be expected to be some form of compensation, given the Court's statements. While the Court found that it could not give her the relief she sought, it found the bankrupt liable for the entire amount of the loan, saying at para 63:

> This Court finds that there is no difference in principle between a situation where a debtor continues to make payments on a contract through the period of bankruptcy, and a situation where the debtor, making payments at the start of the bankruptcy period, promises during the period of bankruptcy to continue to make such payments until the debt is paid, but then stops. The Court also finds no difference between these situations and a situation where a debtor, though not making payments at the time, promises during the bankruptcy period to make ongoing payments. **In those cases, the parties agree to continue the contract through the period of the bankruptcy, notwithstanding the existence of a claim provable in bankruptcy.** In those cases, the debtor continues to enjoy the benefits of the contract. (Emphasis added)

[60] The Court went on to find consideration in the form of the bankrupt's request to keep the vehicle and make the payments and his continued use of it. He went on to note that it would be socially irresponsible in the circumstances to relieve the bankrupt of the debt: para 67.

[61] In ***E.R.I. Engine Rebuilders Inc. v MacEachern,*** 2011 PECA 2, 73 CBR (5th) 73 the Court considered the ***Seaboard*** line of cases to determine that a personal guarantee was not discharged by the guarantor's bankruptcy. The case concerned a bankrupt who was a guarantor

of a corporate debt. The Court found reaffirmation on the basis that the company (which also bankrupted, but after the guarantor's discharge) and the bankrupt continued to receive and accept credit from the lender. But, relying on ***Ontario New Home Warranty Program v Jiordan Homes Ltd*** (1999), 43 OR (3d) 756 (Ont Gen Div), additional reasons 1999 CarswellOnt 4113 (Ont. SCJ), the Court found that liability under the guarantee was not a provable claim in the guarantor's bankruptcy because the claim did not arise until **after** his discharge: at para 13. As a result, the guarantor continued to be liable for the corporate debt. Parenthetically, I note that there is disagreement about the propriety of burdening a guarantor with such liability since it undermines the fresh start principle and fails to recognize a contingent, provable claim: Roderick J. Wood, *Creeping Statutory Obsolescence in Bankruptcy Law,* I.I.C. Art. Vol. 3-1; ***SemCanada Crude Co., Re***, 2012 ABQB 495, 546 AR 370, at para 55, leave to appeal refused, 2012 ABCA 312.

b. Cases Requiring Novation and More

[62] The cases disagreeing with or distinguishing the ***Seaboard*** Approach include ***Scotia Mortgage Corp v Winchester*** (1997), 205 AR 147, 46 CBR (3d) 314 (QB); in ***Day c Banque Laurentienne du Canada,*** 2014 QCCA 449, and ***Scotia Mortgage Corporation v. Berkers,*** 2016 NSSC 12. These cases hold that mere possession and continued payment is insufficient to warrant liability on a personal promise to pay. Rather, there must be a clear acknowledgment of the continuing obligation. As the Master did in this case, some Courts impose the additional requirement of fresh consideration.

[63] ***Winchester*** concerned a deficiency judgement against an original mortgagor who gave a high-ratio mortgage before selling the property to a third party. The third party later made an assignment into bankruptcy. When the third party defaulted on the loan, the lender sought judgment against the original mortgagor. Otherwise, the reported facts are scant, and it is unclear whether the default occurred before or after the discharge from bankruptcy.

[64] Refusing to grant judgement, Master Funduk found the lender's claim to be a claim provable in the original mortgagor's bankruptcy that, as such, was a discharged by operation of s 178. He distinguished ***Seaboard*** on the basis that it concerned a new post-discharge contract made between the lessor and lessee, saying (in part) this at paras 20-21:

> ***Seaboard Acceptance Corp.*** involved a pre-bankruptcy automobile lease that the bankrupt continued to perform during the bankruptcy and after bankruptcy. The court says this, p. 146-47:
>
>> ...
>>
>> In my opinion, what occurred in this case was not, strictly speaking, a novation, as that term is properly understood, but was merely **a continuation of the contract, and a continued abiding by the terms of the contract that had been made between the parties. In effect, the contract was endorsed by the defendant after the discharge**. In those circumstances no other order is possible in relation to damages than that the contractual provisions apply and they must set the quantum of damages in the amount for which judgment was given by the Honourable Judge Campbell.

> What the Court appears to say is that a new contract was entered into after the bankrupt went into bankruptcy. Post-bankruptcy contracts are not caught by a bankruptcy.
>
> I do not see how that helps the Plaintiff. There is no post-bankruptcy conduct by Winchester to create a new contract. (Emphasis in Original)

[65] In my view, the information gap in ***Winchester*** as to when the default occurred renders the case unhelpful. One might surmise that it was more likely after the discharge, given the lag between the discharge and commencement of the foreclosure action, but that requires guess work.

[66] In ***Day***, the bankrupts continued to make payments throughout their bankruptcy. Foreclosure proceedings were commenced after they abandoned the property post-discharge, and a deficiency judgment was granted. On appeal, the Court of Appeal rejected the ***Seaboard*** approach (which it called the "Moen jurisprudence"), appearing to pay particular heed to the report of a working group established by the Superintendent of Bankruptcy and chaired by Yoine Goldstein, the Personal Insolvency Taskforce Report (*PIT Report*). The Court called the *PIT Report* the "Working Group". [1]

[67] The Court, quoting Goldstein at para 16:

> Le principe fondamental du système d'administration de l'insolvabilité du Canada, défini au paragraphe 178(2) de la LFI, est que les faillis ont droit à un nouveau départ une fois libérés de la faillite. À cette fin, le paragraphe 178(2) libère les faillis de toutes leurs dettes, à l'exception de celles indiquées au paragraphe 178(1).
>
> [...]
>
> Si l'on veut que la loi soit conforme au principe du nouveau départ, les faillis devraient être libérés de ces promesses - également intitulées "des engagements personnels" ou "engagements de payer" - lorsqu'ils sont libérés de la faillite. Dans la jurisprudence Moen, les tribunaux canadiens ont plutôt statué que les faillis libérés doivent s'en tenir à leur engagement de payer établi avant la faillite, une fois qu'ils ont continué à effectuer des paiements après leur libération. Lorsque les faillis ont cessé par la suite d'effectuer les paiements, les tribunaux ont donné raison à la partie adverse. Le groupe de travail considère plutôt que les faillis n'avaient pas l'intention, règle générale, de réaffirmer leur promesse d'avant la faillite; ce qui est probable, c'est qu'ils ont continué d'effectuer les paiements de façon à conserver la possession des biens loués ou hypothéqués sans comprendre qu'ils réaffirmaient ainsi leur engagement de payer.

[68] Translation of the above paragraph:

> The fundamental principle of Canada's insolvency administration system, as defined in subsection 178 (2) of the BIA, is that bankrupts are entitled to a fresh start once they have been released from bankruptcy. To that end, subsection 178 (2) relieves bankrupts of all debts, except those specified in subsection 178 (1).

---

[1] 2012 Personal Insolvency Task Force Final Report: Office of the Superintendent of Bankruptcy, Insolv. Bull. 98811846001

[...]

If the law is to conform to the new start principle, bankrupts should be released from these promises — also called "personal commitments" or "commitments to pay" — when they are released from bankruptcy. In ***Moen*** jurisprudence, Canadian courts have rather ruled that bankrupts released must stick to their pre-bankruptcy commitment to pay, once they have continued to make payments after their release. When the bankrupts subsequently ceased to make the payments, the courts agreed with the opposing party. Rather, the Working Group considers that the bankrupts did not intend, generally, to reaffirm their pre-bankruptcy promise. What is likely is that they continued to make the payments in order to retain possession of the leased or mortgaged property without understanding that they were reaffirming their commitment to pay. (Translation)

[69] The Court concluded that there was no evidence of a recognition of the debt and that the lender bore the onus of establishing the borrowers' intent to recognize the released obligation as enforceable, noting that the revival of a "moral obligation" could be achieved by a written or oral "clear and unequivocal" statement to that effect: paras 12, 17.

12. Voici ce qu'écrit le Pr Deslauriers (notes de bas de page omises) :

2156. Un créancier de la faillite pourrait également exercer un recours contre le failli libéré, si ce dernier, après avoir obtenu sa libération, s'est engagé à payer cette créance : il ne s'agit pas de novation, puisque les recours pour recouvrer la dette originale étaient éteints. Il s'agit d'un nouvel engagement dont la considération est l'obligation naturelle ou morale qui subsiste, malgré l'extinction de l'obligation civile. Toutefois, la simple reconnaissance de l'existence d'une dette ne fait pas revivre celle-ci. Il faut que l'engagement du débiteur de payer cette dette à titre d'obligation morale soit clair et non équivoque. Le débiteur qui, à deux reprises, a reconnu l'existence de sa dette s'oblige juridiquement à l'acquitter.

[70] Translation of the above paragraph:

This is what Dr. Deslauriers writes (footnotes omitted):

2156. A bankruptcy creditor could also bring an action against the discharged bankrupt if the bankrupt, after obtaining his release, undertook to pay the debt: it is not a novation, since the remedies to recover the original debt were extinguished. This is a new commitment, the consideration of which is the natural or moral obligation that subsists, despite the extinction of the civil obligation. However, the mere recognition of the existence of a debt does not revive it. The debtor's obligation to pay this debt as a moral obligation must be clear and unambiguous. The debtor who has twice acknowledged the existence of his debt is legally bound to pay it.

[71] At para 17, the Court goes on :

17. Rien au dossier ici ne donne le moindre indice d'une reconnaissance en bonne et due forme de la dette envers l'intimée. Il n'y a pas eu de pourparlers entre les parties (du moins n'y a-t-il aucune preuve en ce sens au dossier), pas d'engagement ferme de rembourser, pas de billet. Une hypothèse nettement plus

plausible que celle de la reconnaissance est que les paiements à l'intimée avaient lieu d'être, dans l'esprit de l'appelante et du mis en cause, pendant qu'ils continuaient d'avoir la jouissance des lieux. Il revenait à l'intimée de fournir une démonstration prépondérante de l'intention des parties adverses de reconnaître comme valide et exécutoire l'obligation dont ils avaient été libérés par la faillite. Une telle reconnaissance, si elle avait véritablement été de l'intention des emprunteurs, aurait pu se concrétiser dans un écrit ou même par une déclaration suffisamment « claire et non équivoque », selon l'expression du Pr Deslauriers.

[72] Translation of para 17:

Nothing on the file shows any indication or acknowledgment of the debt owed to the respondent. There have been no discussions or negotiations between the parties (at least no evidence of this on record) and no determination and/or commitment of a payment plan. Rather than simply acknowledging the debt owed, a more likely assumption was that the appellant assumed the respondent would continue to utilize/enjoy the property such that it would replace the debt owed by the appellant. It would have been up to the respondent to solidify this intention, if that was in fact agreed upon, and in turn for the opposing parties to acknowledge this agreement as valid and enforceable, thus discharging them from the bankruptcy. Such agreement, had it actually been the intention of the appellant, could have been solidified through a "clear and unambiguous" written statement.

[73] It appears that the Court was not directed to the November 2003, *Report of the Standing Senate Committee on Banking, Trade and Commerce, Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (*2003 Senate Report*), which considers the *PIT Report* as well as other stakeholder and academic submissions on reaffirmation agreements. This Report recommends an amendment to the BIA prohibiting all reaffirmation agreements (at pp. 33-36); Parliament chose not to follow that recommendation. Similarly, it appears that s 84.2 was not brought to the Court's attention.

[74] In ***Berkers***, one of the joint mortgagors was assigned into bankruptcy. The mortgage was in good standing throughout the bankruptcy and for some four months thereafter. In rejecting the ***Seaboard*** Approach, the Court reasoned that it failed to disclose a principle of law supporting the conclusion that liability under a continuing contract is treated differently in bankruptcy from other kinds of liability, or give effect to the plain meaning of s.178(2): at para 19.

[75] On the first point, the Court said this at para 21:

The mortgagee, who usually gets notice of the bankruptcy, is usually pleased to take monthly payments. The mortgagor may be content to make the payments in order to stay in a home, at least for the time being. If the mortgagee wants something more, such as a revival of personal liability, **it can propose a new contract based on forbearance**. There is no need for revival by operation of law.

(Emphasis Added)

[76] This suggests that the Court was unaware of s 84.2, a point further evidenced by these observations at paras 5 and 22:

> Clause 3E of the mortgage provides "If you sell, transfer, mortgage or charge your property, we may, at our option, require you to pay all the money that you owe us immediately…" **I emphasize the word "transfer", which would include a transfer by assignment in bankruptcy**...
>
> ...
>
> The unfounded nature of the holding in ***Seaboard*** is underscored by its one-sidedness. **No one suggests that the mortgagee is precluded from exercising its rights to possession or foreclosure for breach of the covenant against transfers**. That would require a new contract or proof of estoppel. That two way street of contract or estoppel is also the place for reviving personal liability.
>
> (Emphasis added)

[77] Concerning s 178(2), the Court found that a "continuing contract" as per the ***Seaboard*** Approach is simply not exempt from release on discharge under s 178(1): at paras 23, 25.

[78] The Court also found that fresh consideration is required to support an express reaffirmation citing at para 18, this statement from Holden, Morowetz & Sarra:

> With respect, it is submitted that, although the security is not affected by a discharge, the debt is extinguished by s.178(2): *Pelyea v. Canada Packers Employees Credit Union Ltd.*, 13 C.B.R. (N.S.) 284, [1970] 2 O.R. 384, 11 D.L.R. (3d) 35 (C.A.); *Burton v. Toronto-Dominion Bank*, 22 C.B.R. (N.S.) 207, [1976] I.L.R. 1-779 (Ont. S.C.). Accordingly, unless there is new consideration advanced by the secured creditor subsequent to the date of bankruptcy, the creditor should not be entitled to judgement against the bankrupt for the debt.

[79] I note that immediately following this passage (at H§67) are citations for several articles: "Post-Bankruptcy Remedies of Secured Creditors: as Good as it Gets" (1999), 31 CBLJ 436 by Tamara M. Buckwold and "Postbankruptcy Remedies of Secured Creditors" (1999) 32 CBLJ 142 by Jacob Zeigel. See also articles "Post-Bankruptcy Remedies of Secured Creditors: A Reply to Professor Ziegel" by Tamara M. Buckwold, 33 Can Bus LJ 128 and "Post-Bankruptcy Remedies of Secured Creditors: A Brief Rejoinder" by Jacob S. Ziegel, 33 Can Bus LJ 144. Coincidentally, the Master in this case considered these same articles, all of which precede the *2003 Senate Report* and the subsequent amendments to the BIA.

[80] Further, as with the Master below, the ***Berkers*** Court appears not to have been advised of the *PIT* and *2003 Senate Reports*, which I will next detail.

c. Reaffirmation does not require fresh consideration

[81] While the Supreme Court has not expressly addressed the issue of whether a personal promise can survive bankruptcy discharge, it made a revealing *obiter* comment in ***Moloney*** at para 81 (citations omitted):

> As a general rule, a creditor cannot cause a debtor to revive an obligation **from which the debtor was released,** unless the creditor offers fresh consideration. Between private

> parties, it is arguable that a debtor may freely agree to revive a discharged debt in exchange for the creditor's provision of goods or services. (Emphasis added)

[82] It remains a question whether this general rule applies when the debtor has continued to make payments during and after the bankruptcy and discharge.

[83] In a recent decision, ***Rosas v Toca,*** 2018 BCCA 191, the British Columbia Court of Appeal ruled that absent duress, unconscionability, or other public policy concerns, there is no need for fresh consideration to vary contractual terms. The Court gave this helpful summary at para 4:

> The time has come to reform the doctrine of consideration as it applies in this context, and modify the pre-existing duty rule, as so many commentators and several courts have suggested. When parties to a contract agree to vary its terms, the variation should be enforceable without fresh consideration, absent duress, unconscionability, or other public policy concerns, which would render an otherwise valid term unenforceable. A variation supported by valid consideration may continue to be enforceable for that reason, but a lack of fresh consideration will no longer be determinative. In this way the legitimate expectations of the parties can be protected. To do otherwise would be to let the doctrine of consideration work an injustice.

[84] I agree with this approach, which in my view is consistent with that taken in ***Seaboard***.

d. The Senate Reports

[85] Given the discussion of the *PIT Report* in ***Day***, I asked counsel to make further submissions regarding the proposed prohibition of reaffirmation agreements. As noted previously, the *2003 Senate Report* considered portions of the *PIT Report* before recommending that the BIA be amended to prohibit all reaffirmation agreements.

[86] Parliament did not follow the *2003 Senate Report* recommendation.

[87] Counsel for Servus suggests that context of the two reports is important, noting that the *PIT Report* dealt with both *ipso facto* clauses and reaffirmation agreements, recommending that the latter be prohibited for all unsecured transactions, and permitted "under a regulated and principled system" for certain secured transactions. It further recommended that the ***Seaboard*** (aka ***Moen***) line of cases endorsing affirmation by conduct be statutorily overruled. Finally, it recommended extending the prohibition against *ipso facto* clauses in s 66.34 of the BIA for consumer proposals to personal bankruptcies, urging that there was no meaningful distinction between the two. In Servus' view, had Parliament agreed, the two recommendations would have worked harmoniously.

[88] The *2003 Senate Report* did not fully accept the *PIT Report* recommendations. Rather than prohibiting all *ipso facto* clauses in personal bankruptcy, it recommended making them unenforceable in contracts for "basic services". As "basic services" is an undefined term, it is unclear whether the recommendation was intended to apply to mortgages. It also differs from the *PIT Report* by recommending a prohibition of **all** reaffirmation agreements, irrespective of how they arise.

[89] Servus argues that, assuming that mortgages are not "basic services," had both recommendations been accepted by Parliament, the result would be that mortgagees would have to rely on *ipso facto* clauses to call mortgage debts and foreclose unless they were prepared to

lose all recourse to remedies under the mortgage. Accordingly, Parliament's choice to ban *ipso facto* clauses, but not reaffirmation clauses, indicates its approval of implicit reaffirmation by conduct. In light of s 84.2, that is the only practical way reaffirmation could be achieved.

[90] Mr. Sulyok contends that Parliament's failure to implement a ban on reaffirmation should be attributed more to the hasty political process underlying Bill C-55 (noted in the *2005 Senate Report*) than Parliamentary intention. Further, in furtherance of the fresh start principle all reaffirmation agreements must be clear, unequivocal, made in writing, and accompanied by fresh consideration. To support this proposition, he points to ***Moloney*** at para 36.

Conclusion on the Correct Approach

[91] In my view, it is entirely relevant that Parliament had the *2003 Senate Report* recommendations when the BIA was last amended, but chose not to follow them.

[92] Further, of some note is that although the academic writing referenced by the Master preceded the Senate Reports and the 2009 amendments to the BIA, Duggan, Ziegel, and Girgus concluded that ***Seaboard*** was correctly decided on its facts, but not for the reasons given by the Court. Rather, the result could be justified on the basis of estoppel to preclude a debtor from asserting s 178(2) rights: See also, Ronald Cumming, *Interface of Secured Transactions Law and Bankruptcy Law*, *Professor Ziegel's Role*, 2010 Annual Review of Insolvency Law 24.

[93] In my view, requiring something more, be it fresh consideration or an express reaffirmation, fails to adequately balance the rights of all stakeholders – be they creditors, debtors or co-signors. Accepting that the fresh start principle is a sound policy underlying the BIA and that financial haircuts are an expected aspect of bankruptcy, there is also a need to consider and weigh all interests. There are clear examples where simply favouring rehabilitation of the bankrupt could result in significant injustice, i.e. where long periods of time elapse post-discharge, or where the mortgaged property is a revenue property, as was the case for the entirety of the bankruptcy period here.

[94] In this regard, I note that in ***Moloney***, at para 83, the Court noted:

> The rehabilitative purpose of s. 178(2) is not meant to give debtors a fresh start in all aspects of their lives. Bankruptcy does not purport to erase all the consequences of a bankrupt's past conduct.

[95] As evidenced by the provisions of the BIA addressing financial counselling (ss 66.13, 157.1, 168) and the treatment of surplus income (s 68), the rehabilitative purpose of the BIA requires more than just invoking the fresh start principle. Parliament not only expects bankrupts to learn from their financial mistakes, it mandates that they be counselled to learn and take responsibility for their financial affairs.

[96] Appreciative of the benefit of requiring express reaffirmation on bankruptcy, that is a task for Parliament. However, the Superintendent of Bankruptcy can address the issue by requiring trustees to include the topic as part of their counselling responsibilities under the BIA and the Superintendent's Directive No. 1R4, *Counselling in Insolvency Matters*, issued January 29, 2018. I recommend that the Superintendent take whatever actions that she deems appropriate in this regard.

[97] I conclude that when the debtor files an assignment in bankruptcy, but maintains possession of the property and continues to make the payments due under the contract, the debtor has affirmed the contract, including the covenant to pay.

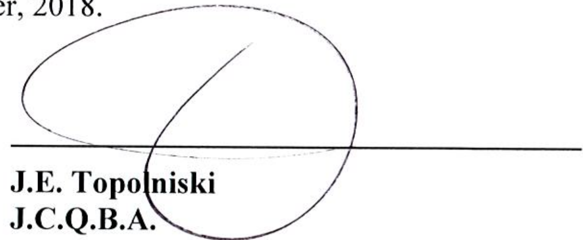
[98] I therefore grant Servus' appeal of the Master's decision.

Costs

[99] As I have found that the promise to pay the Deficiency was not released, it follows that Servus' costs of enforcing was not either.

[100] Mr. Sulyok is liable to pay the costs of the application before the Master and this appeal on a solicitor and own client basis.

Heard on the 24th day of May and the 10th day of August, 2018.
Dated at Edmonton, Alberta this 17th day of October, 2018.



J.E. Topolniski
J.C.Q.B.A.

Appearances:

Kentigern A Rowan, QC and Amber M Poburan
for Servus Credit Union Ltd.

Frank C DeAngelis, QC and Tarryn Klapper
for Daniel Ernest Sulyok