CITATION: Royal Bank of Canada v. CFNDRS Inc., 2017 ONSC 7661
COURT FILE NO.: CV-17-587341-00CL
DATE: 20171220

ONTARIO SUPERIOR COURT OF JUSTICE

B E T W E E N:

ROYAL BANK OF CANADA

Applicant

-and-

CFNDRS INC.,
formerly known as DESIGN COFOUNDERS INC.,
formerly known as TAILORED UX INC.

Respondent

BEFORE: F.L. Myers J.

COUNSEL: *James Satin,* counsel for Royal Bank of Canada
Mustafa Redha in person

HEARD: December 20, 2017

ENDORSEMENT

[1] On November 28, 2017, the bank commenced a summary application seeking the appointment of a receiver over the property, assets, and undertaking of the respondent. The relief claimed in the notice of application does not include the appointment of a manager of the business. Neither does it include a claim for judgment on the respondent's indebtedness. The appointment of a receiver alone is the sole substantive relief sought in this application.

[2] The grounds relied upon in the application and the bank's evidence are that: the bank holds security under a general security agreement and a lease; the terms of the security documents provide for the appointment of a receiver on default; the respondent is indebted to the bank; it defaulted; and the bank has made demand.

[3] The bank relies upon s. 101 of the *Courts of Justice Act,* RSO 1990, c. C-43 and s. 243 of the *Bankruptcy and Insolvency Act*, RSC 1985, c. B.3.

[4] Section 101 of the *Courts of Justice Act* does not apply in this application. The section involves only interlocutory orders. Here, the appointment is sought on a final basis. This is allowed under s. 243 of the *BIA* and therefore under Rule 14.05 (2) of the *Rules of Civil Procedure*, RRO 1990, Reg. 194. However, nothing in that statute describes what happens after the receiver is appointed by way of application. An application is made and the court issues a

final order appointing the receiver – presumably defining the goals of the process in that final order.

[5] By contrast, when an action is commenced to enforce a debt and the plaintiff seeks the interim appointment of a receiver and manager under s. 101 of the CJA and Rule 41, the appointment is interlocutory. The receiver preserves and protects the assets pending proof of the debt. If the plaintiff obtains judgment on its debt, the receiver and manager then will enforce the plaintiff's judgment by way of equitable execution akin to an appointment under Rule 60.02 (1)(d). The receiver and manager will liquidate assets or engage in other processes to realize cash to pay to the plaintiff who is then a judgment creditor. Before the receiver and manager can pay a judgment creditor however, the receiver and manager, of necessity, will have to consider whether there are other claims that must, by law, be paid in priority to the claim of the judgment creditor. In that process an orderly liquidation and payment scheme is mandated and carried out.

[6] While there is much similarity between the provincial and federal regimes, it should be borne in mind that s. 243 (7) of the BIA prohibits the court from providing a super-priority charge to the receiver to indemnify it for disbursements it incurs in the operation of a business of the insolvent person. I am unaware of any case law that provides for the appointment of a receiver under s. 243 of the BIA by way of originating application in which the receiver has been ruled to be entitled to a super-priority charge to protect its right to indemnity for business disbursements.

[7] Although the notice of application in this case sought only the appointment of a receiver, the draft order submitted by the bank followed the Commercial List model form of order. It provided for the appointment of a receiver and manager under both s. 101 of the *CJA* and s. 243 of the *BIA*. It provided a super-priority charge for all fees and disbursement of the receiver and manager and its counsel on all disbursements although that is available only under the former statute and not under the latter. Where both statutes apply, that is permissible. But here, since s. 101 is not engaged in an interlocutory appointment process, the receiver would not be entitled to indemnity for business disbursements in a s. 243 receivership.

[8] The test for the appointment of an interlocutory receiver is well understood. In para. 10 of *Bank of Nova Scotia v. Freure Village of Clair Creek*, 1996 CanLII 8258 (ON SC) Blair J. (as he then was) set out several propositions that remain applicable today:

a. The Court has the power to appoint a receiver or receiver and manager where it is "just or convenient" to do so;

b. In deciding whether or not to do so, the court must have regard to all of the circumstances but in particular the nature of the property and the rights and interests of all parties in relation thereto;

c. The fact that the moving party has a right under its security to appoint a receiver is an important factor to be considered but so, in such circumstances, is the question of whether or not an appointment by the Court is necessary to enable the receiver-manager to carry out its work and duties more efficiently;

d. It is not essential that the moving party, a secured creditor, establish that it will suffer irreparable harm if a receiver-manager is not appointed.

[9] Justice Blair also noted that while the appointment of a receiver may be seen to be extraordinary, it is much less extraordinary when the plaintiff has a contractual right to appoint a receiver on its own. The question of whether a court appointment then is just and convenient when there is a contractual power of appointment will turn on an assessment of, "the potential costs, the relationship between the debtor and the creditors, the likelihood of maximizing the return on and preserving the subject property and the best way of facilitating the work and duties of the receiver-manager." *Freure Village* at para. [12].

[10] In my view, the issue that usually tips the balance is whether there is a reason to incur the expense and procedural formality of appointing a third party to exercise neutral, transparent, accountable stewardship of the assets of the debtor while interested parties jostle on the merits of whatever their dispute may be. If the parties' dispute puts the business assets at risk or where realization options may be impaired by leaving the business in the debtor's hands or requiring the secured creditor to bear the risk of indemnifying a privately appointed receiver, the court will usually intervene. Often, simple default on secured debt will be sufficient to attract a receivership where the risk to the business is implicit in the nature of the business or the dispute between the creditor(s) and the debtor(s). However, as with all equitable remedies, context is everything and each case turns on its own facts.

[11] In this case, there is absolutely no evidence before the court as to why a court appointed receiver is just or convenient. All that follows was told to me on an unsworn basis by counsel and Mr. Redha personally.

[12] As best as I can tell, the respondent runs a high tech startup that is in an early development stage. It is creating software that will help lead a business through the steps of a problem solving exercise. Like many startups, the business operates through its principal, Mr. Redha, and a number of independent contractor/consultants. There are no other employees. There is no bricks and mortar. There is Mr. Redha, his computer, and perhaps some IP. I did not ask if the business has an office or if the bank proposed to take possession of Mr. Redha's residence under the order as drafted.

[13] The bank says that it is interested in collecting the respondent's accounts receivable and its entitlement to Scientific Research and Experimental Development Tax Incentive payments. Mr. Redha estimates conservatively that the business has approximately $75,000 in outstanding receivables. It may have entitlement to SR&ED payments for 2016 and 2017 that may be significant. The applications for these payments are complex and require Mr. Redha's involvement with a professional consultant who charges a 7% fee. Mr. Redha is bullish on his prospects to obtain new receivables, i.e. new revenue, in the New Year. I doubt he would have been so bullish had he understood that a receivership would have seen him working for a salary to be negotiated with the receiver while the receiver obtains the receivables generated by his efforts.

[14] Mr. Redha submits that the IP of the business has value that exceeds the amount of his debt. I have no way to assess the correctness of this statement. Moreover, the bank is not

required to keep funding the respondent through a sales process of its own making. However, this much is clear to me (based on experience and common sense absent any evidence one way or the other) – if a receiver is appointed, it has no wherewithal to run the business without Mr. Redha's voluntary and ongoing commitment. Trying to sell partially developed software disembodied from an operating business and without Mr. Redha's ongoing support seems unlikely to be value-maximizing and probably is impossible. In fact, there really is no business for a third party to manage. There is just Mr. Redha and his computer and incomplete software.

[15] Mr. Satin submits that the bank is entitled to a receiver under its loan and security documents. The proposed receiver, he says, is not willing to undertake the appointment without the protection of the court. There is no indication of why that may be so.

[16] The total debt of about $450,000 is very small for a court ordered receivership process. There is no indication as to how a court-based process can be expected to be value-maximizing or why it is more desirable than a private appointment in this case. There is nothing inherent in the relationship between these parties that makes the mere existence of a default on a debt require a neutral third party to assume stewardship of the business such as it may be. The bank has delivered a notice under s. 63 (4) of the PPSA that it intends to realize on collateral of the respondent. Collecting $75,000 in outstanding receivables is not made more convenient by a court appointed receiver. Putting in place a trust or lockbox process for receipt of SR&ED payments may require some negotiation or, perhaps, appointment of a very limited true receiver empowered simply to receive this specific property of the debtor and perhaps to oversee completion of SR&ED applications. With some negotiation, a sale process for the respondent's IP might be agreed upon. It will take evidence however to establish that a professional accountant/trustee can come in and sell the IP in a value-maximizing process without Mr. Redha's voluntary, active engagement.

[17] The respondent should not take from this that it is at all freed from its legal obligations to pay its debt. The bank has many paths open to it to seize and sell the respondent's assets, take its loss, and bring a swift end to the business. That strikes me as a lose-lose proposition, but that is not my decision to make. As usual, if there is to be a win-win, there will need to be a discussion in which each party tries to accommodate the other's interests to some degree at least.

[18] In view of the procedural issues, the complete lack of evidence, and the inapt order sought, I am not prepared to appoint a receiver as sought in this case at this time. If the bank wishes, it may arrange a case conference before me, on notice to the respondent, at which I can assist the parties work towards a consensual outcome or restructured court proceedings. Alternatively, the applicant may file a draft order dismissing this application for signing. Mr. Redha's approval of the form and content of the draft order is not required. Nothing in this outcome precludes the applicant from commencing an action against the respondent to sue on its debt.

F.L. Myers J.

Date: December 20, 2017