COURT OF APPEAL FOR BRITISH COLUMBIA

Citation: *Cliffs Over Maple Bay (Re),* 2011 BCCA 180

Date: 20110414
Docket: CA038042

In the Matter of the
***Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36**

And

In the Matter of the
***Business Corporations Act*, R.S.B.C. 2002, c. 57**

And

In the Matter of The Cliffs Over Maple Bay Investments Ltd.

Between:

Fisgard Capital Corporation and Liberty Holdings Excell Corp.

Appellants
(Respondents on Cross-Appeal)

And

Century Services Inc., Lawson Lundell LLP

Respondents
(Appellants on Cross-Appeal)

Before: The Honourable Madam Justice Prowse
The Honourable Madam Justice Newbury
The Honourable Mr. Justice Chiasson

On Appeal from the Supreme Court of British Columbia, March 25, 2010
(*Cliffs Over Maple Bay (Re)*, 2010 BCSC 389,
Vancouver Registry, Docket No. S083716)

Counsel for the Appellant:	G.J. Tucker Z.J. Ansley
Counsel for the Respondent Century Services Inc.:	M.I.A. Buttery L. Williams
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Place and Dates of Hearing: Vancouver, British Columbia
January 14, 2011

Place and Date of Judgment: Vancouver, British Columbia
April 14, 2011

Written Reasons by:
The Honourable Madam Justice Newbury

Concurred in by:
The Honourable Madam Justice Prowse
The Honourable Mr. Justice Chiasson

Reasons for Judgment of the Honourable Madam Justice Newbury:

[1] This appeal involves a three-way dispute among creditors of The Cliffs Over Maple Bay Investments Ltd. ("Cliffs" or the "Company"), which was the developer of an ill-fated real estate project near Maple Bay on Vancouver Island. Unfortunately, the Company was unable to secure a reliable water supply for its proposed golf course and residential units, and the project failed. The ensuing proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*") were, as it turns out, similarly misconceived: this court ultimately ruled that a Supreme Court order made under the *CCAA* staying creditors' proceedings against the Company and authorizing debtor-in-possession ("DIP") financing, should not have been granted, no arrangement or compromise with creditors having been intended.

[2] In this last phase of the litigation, the court below had to determine the parties' respective entitlements to what remains of one *tranche* of DIP financing that the DIP lender, "Century", purported to advance in violation of a term in its letter of commitment. The letter had been incorporated by reference in the court order. The chambers judge who was seized of this matter below decided the priority issue as between Century and the existing first-ranking creditor, "Fisgard Liberty", with respect to the funds so advanced. He found that "Century's priority for advances made pursuant to the order is lost because ... those advances were not in compliance with the terms of the order." He granted a declaration that Fisgard Liberty was "entitled to priority" in respect of the funds, subject to the claim of a third creditor, "Lawson", to a solicitor's lien over all or part of the funds – a matter to be decided at a separate hearing following the issuance of his reasons. No appeal was taken from the order.

[3] However, Century then brought another motion before the chambers judge, questioning whether the funds had in law and in fact been advanced. On this occasion, the judge stated that

his previous order had not determined "entitlement" to the funds. He declined to apply *res judicata*. He found that the advance had never taken place, that the funds remaining in Lawson's trust account had been subject to a *Quistclose* trust in Century's favour, and that Cliffs had never obtained an interest in the funds to which Fisgard Liberty's security interest could attach. Lawson was ordered to [re]pay what remained in its trust account to Century, and its motion for a declaration of solicitor's lien over the funds was dismissed.

[4] In this court, Fisgard Liberty (with Lawson joining in) argues among other things that the question of priority was *res judicata* and that issue estoppel or cause of action estoppel should have barred the chambers judge from making the second order. These creditors also assert that the "new" issues concerning advance, trust and attachment raised in the second hearing below were wrongly decided. Fisgard Liberty seeks a declaration that its security interest attached to the funds upon their release to Lawson as Cliffs' agent.

[5] Following the issuance of these reasons, this court will consider Lawson's claim both to part of the "Administrative Charge" contemplated by the original DIP order and to a solicitor's lien over all the funds it holds in trust. Until that matter has also been disposed of by this court, Lawson holds the funds in trust.

Chronology

[6] The following chronology will, I hope, be sufficient to provide an overview of the facts of this case. I will provide additional facts as necessary when analyzing the issues on appeal.

- April 18, 2006 – Cliffs granted to the appellants Fisgard Capital Corp. and Liberty Holdings Excell Corp. (collectively, "Fisgard Liberty") a mortgage of its real property and a General Security Agreement ("GSA"), registered pursuant to the *Personal Property Security Act* ("*PPSA*"), charging all the Company's present and after-acquired property. (The Fisgard Liberty mortgage was a third mortgage, but it appears that the first and second mortgages, which secured fairly small amounts, were assigned at some point to Fisgard Liberty.)

- January 9, 2007 – The Company granted a fourth mortgage to Liberty Holdings Excell Corp. and Canada Trust Company in the amount of $7,650,000.

- June 15, 2008 – By this time, the Company found itself unable to move forward with the project or to draw down funds required for that purpose because of the water supply problem. Approximately $21,160,000 was outstanding under the third mortgage and $8,800,000 under the fourth, and the sum of approximately $7,340,000 was owed to various trade creditors, lessors and others.

- April-May, 2008 – Fisgard Liberty served the Company with notices of intention to enforce its security and on May 23 appointed a receiver.

- May 26, 2008 – Cliffs proceeded *ex parte* to obtain a stay of proceedings under the *CCAA* and the Court appointed The Bowra Group Inc. as Monitor. The order provided detailed terms for an "Administrative Charge", not to exceed $200,000, in favour of the Monitor and Cliffs' counsel, Lawson Lundell LLP ("Lawson") as security for the payment of their respective fees and disbursements. The Charge was to rank in priority over all other interests and charges.

- June 27, 2008 – The stay was extended in a 'comeback order' under which the Court authorized DIP financing not to exceed $2,350,000 and to be advanced in *tranches* not to exceed $500,000 each. The DIP lender was Century Services Inc. ("Century"), one of the respondents herein. The order, referred to by counsel as the "DIP Order", stated:

> THIS COURT ORDERS that, advances under the DIP Facility shall be made only at the request of the Monitor to the DIP Lender, such advances to be paid to Lawson Lundell LLP "in trust" and to be paid out only on the written request of the Monitor in consultation with the Petitioner, subject to further Order of the Court. [Emphasis added.]

The DIP financing itself was to be on the terms in Century's commitment letter dated June 13, which contained an "appeal provision" as follows:

> The liability and obligation herein and any future obligations of any nature and kind of the Borrower shall be evidenced, governed and secured, as the case may be, by the following documents (collectively, the "Security") completed in a form and manner satisfactory to Century's counsel:
>
> a. Loan Agreement;
>
> b. Promissory note;
>
> c. A court[-]approved first and unencumbered charge on the real and personal property of the Borrower and no appeal

> therefrom being taken within 21 days after the pronouncement of that Order ... [Emphasis added.]

- July 7, 2008 – Cliffs and the Monitor signed an "Order to Pay" authorizing Century to advance the first *tranche* of DIP financing to Lawson as solicitors for the Company.

- July 18, 2008 – Fisgard Liberty obtained leave to appeal the June 27 order under the *CCAA*. (This occurred within the specified 21-day appeal period.)

- Early August 2008 – The following events took place as described by the chambers judge:

> [16] In early August, prior to the hearing of the appeal, Century purported to waive the appeal provision, and provided the $500,000 in DIP financing authorized by the order to pay to Lawson Lundell. Century sought, and was provided, further security from the Cliffs' principals for this payment. When commitment fees, interest charges, and other chargebacks were taken into account, Lawson Lundell held the net amount of $350,500 in trust on account of this payment.
>
> [17] Lawson Lundell was placed on an undertaking not to release any portion of this $350,500 until Century's solicitors provided them with written authority to do so. A further condition imposed was the payment of a $25,000 due diligence fee to Century.
>
> [18] On August 8, 2008, this undertaking and condition were satisfied.
>
> [19] In accordance with paragraph 8 of the DIP Order, the Cliffs and the Monitor requested and proceeded to use some of the DIP funds held in trust by Lawson Lundell. On July 15, 2008, a real estate appraisal was prepared by the Altus Group in respect of the Cliffs' property located at North Cowichan on Vancouver Island at the direction of the Monitor (the "Altus Report"). The parties agree that approximately $98,000 of the DIP monies were used to pay for the Altus Report. Additionally, the parties agree that the amount of $12,958.52 was directed to be paid by the Monitor out of the DIP facility to consultants who provided advice on golf course specific issues. Payments were also made to the principals of the Cliffs on account of wages.
>
> [20] None of the parties dispute the propriety of these expenses, and none advance a claim of entitlement for these amounts. After these expenditures are taken into account, the $162,276.33 which constitutes the subject of this dispute remains in Lawson Lundell's trust account. [Emphasis added.]

- August 15, 2008 – This court allowed Fisgard Liberty's appeal and set aside the June 27 order for reasons indexed as 2008 BCCA 327. Tysoe J.A. for the Court stated at para. 41:

> I would allow the appeal and set aside the order dated June 27, 2008. I would declare that the powers and duties of the Monitor contained in the

> orders dated May 26, 2008, and June 27, 2008, continued until today's date and that the Administration Charge created by the May 26 order shall continue in effect until all of the Monitor's fees and disbursements, including the fees and disbursements of its counsel, have been paid. I would remit to the Supreme Court any issues relating to the DIP financing that has been advanced.

As mentioned earlier, the resulting order had not been settled or entered at the time of the initial hearing of the present appeal, but has now been entered. It states in material part:

> THIS COURT ORDERS that the appeal is allowed, and the order dated June 27, 2008 is set aside;
>
> AND THIS COURT FURTHER DECLARES that the powers and duties of the Monitor contained in the May 26, 2008 and June 27, 2008 orders herein continued until today's date and that the Administration Charge created by the May 26, 2008 order shall continue in effect so as to ensure payment of all of the Monitor's fees and disbursements, including the fees and disbursements of its counsel;
>
> AND THIS COURT FURTHER ORDERS that any issues relating to DIP financing are remitted to the Supreme Court;

- September 24, 2008 – Rice J. confirmed the appointment of a receiver of the Company's assets pursuant to Fisgard Liberty's GSA and granted Century a charge on the Company's property in the amount of $98,000, ranking in priority to all other security interests, to secure the cost of the "Altus report".
- February 17, 2009 – The chambers judge below approved fees and disbursements of the Monitor and counsel. The order did not state the amount so approved, but referred to invoices attached to the Monitor's report. We are told these amounted to $118,577.28.
- March 31, 2009 – Pitfield J. approved the sale of the Company's real property holdings to another company, subject to the prior changes in favour of Fisgard Liberty, various encumbrances in favour of the District of North Cowichan, and the security interest created by the Administrative Charge "as it may have been affected" by the order of June 27, 2008.
- May 4, 2009 – Century filed a motion in Supreme Court seeking *inter alia*:

> 1. A declaration that the monies advanced by Century to The Cliffs Over Maple Bay Investments Ltd. ("Cliffs") on August 7, 2008 was made pursuant to and in accordance with the terms of a valid and enforceable court order dated June 17 [*sic*], 2009 (the "DIP Order");

2. A declaration that an appeal setting aside the DIP Order does not affect the priority of the security held by Century for funds advanced prior to the appeal under the terms of the DIP Order. [Emphasis added.]

- May 5, 2009 – Fisgard Liberty filed a motion seeking an order that its mortgage and GSA charged the Company's property in priority to any claims or interests of Century or Lawson, an inquiry as to the amount Century had advanced to Cliffs, and an order for the delivery up to Fisgard Liberty of all amounts of such advance in the possession of Century or Lawson.

- June 30, 2009 – After hearing both motions on May 12, the chambers judge issued reasons, indexed as 2009 BCSC 869, in which he formulated the issues before him as follows:

1. Was Century's advance of funds to Cliffs made in accordance with the terms of the DIP Order?
2. Does the successful appeal of the DIP Order deprive Century of priority for advances already made pursuant to the order? [Emphasis added.]

He concluded that the "appeal term" in Century's commitment letter had been intended to be a condition of the financing, that Century had not been entitled to waive it unilaterally or indeed without further order, and that:

> ... the August 7, 2008 advance of $500,000 was not authorized under the terms of the DIP order. Thus Century is not entitled to priority on the funds claimed. As Fisgard/Liberty are the first and second mortgagees of Cliffs, they are entitled to priority of the funds in question, with the exception of the amount of $98,000 spent on the Altus appraisal report, which is not in dispute by agreement between the parties. [At para. 51; emphasis added.]

Having answered the first issue in the affirmative, the judge found it unnecessary to go on to consider the second question. In his words, "Century's priority for advances made pursuant to the order is lost because I have concluded that those advances are not in compliance with the terms of the order." [Emphasis mine.] The judge's order of June 30, 2009 stated in material part:

> THIS COURT ORDERS that
>
> 1. The advance of $500,000 by Century, on or about August 7, 2008, to Cliffs Over Maple Bay Investments Ltd. ("Cliffs") (the "Funds"), was not authorized under the terms of the Order of this Court dated June 27, 2008.

2. Century is not entitled to priority over the Funds except with respect to the amount of $98,000 incurred in connection with the Altus appraisal report.

3. Fisgard and Liberty are entitled to priority over the Funds, except with respect to the amount of $98,000 incurred in connection with the Altus appraisal report.

4. Nothing in this Order affects the entitlement, if any, of Lawson Lundell LLP, to a solicitor's lien over all or part of the Funds in its trust account, which shall be determined on a separate motion.

5. Fisgard/Liberty are entitled to their costs of this application. [Emphasis added.]

- In November 2009, Lawson and Fisgard Liberty filed motions which the chambers judge heard on November 24 and 26. Lawson sought a declaration that it was entitled to "payment of its outstanding accounts from the funds secured by the Administrative Charge granted herein by order of the Court on May 26, 2008", and to a solicitor's lien "over funds held in its trust account to the credit of the Petitioner [Cliffs] in an amount to be determined", and costs. For its part, Fisgard Liberty sought an order that:

1. Century Services Inc. ("Century") pay to Fisgard and Liberty the sum of $239,860.31, together with interest on that sum from the date of making of the Advance by Century to The Cliffs Over Maple Bay Investments Ltd. ("COMB") in or about August 2008.

2. Alternatively, an accounting to determine that portion of the $500,000 Advance which was actually paid into the hands of COMB in or about August 2008, and an order that Century pay to Fisgard and Liberty an amount calculated by deducting from the $500,000 Advance;

   a) the sum of $162,139.69 held in trust by [Lawson];

   b) the sum of $98,000 incurred in connection with the Altus appraisal report; and

   c) that amount determined on an accounting to have been actually paid into the hands of COMB from the Advance.

3. Lawson pay to Fisgard and Liberty the sum of $162,139.69, together with interest on that sum from the date of payment of those funds into Lawson's trust account in or about August 2008.

4. An accounting as to funds received into and/or paid out of Lawson's trust account in connection with the Advance and the *CCAA* proceeding.

5. An order that Lawson pay to Fisgard and Liberty any sum held by Lawson for the benefit of or in connection with COMB other than the sum referred to in paragraph 3. ...

The Chambers Judge's Reasons

[7] The chambers judge issued reasons dated March 25, 2010 that are indexed as 2010 BCSC 389. After describing the events I have summarized, he reviewed the amounts relevant to Lawson's claim:

> In addition to its claim of solicitor's lien, Lawson Lundell seeks a declaration that it is entitled to payment of its outstanding accounts from the administrative charge created in the Initial Order.
>
> To date, Lawson Lundell has been paid $15,700.70 by the Cliffs for legal fees and disbursements incurred in this matter. On June 26, 2008, Lawson Lundell rendered a bill in the amount of $7,291.34 for which it was paid in full. On August 18, 2008, Lawsons rendered a bill in the amount of $144,822.94 to the Cliffs for legal services and disbursements incurred up to that date in this matter, of which $8,409.36 has been paid. Thus, Lawson Lundell is owed $136,413.58 on account of that bill. Interest continues to accrue on this sum at 12% per annum.
>
> Since August 18, 2008, Lawsons has continued to perform work for the Cliffs, and as of January 5, 2009, had recorded unbilled work in progress in the amount of $50,516.29 inclusive of disbursements, but not any applicable taxes. [At paras. 30-2.]

[8] He described the issues before him as follows:

> 1. Does *res judicata* bar Century from claiming entitlement to the Funds?
> 2. Were the Funds "advanced" by Century to the Cliffs? Did the Cliffs ever own or possess the Funds?
> 3. Alternatively, are the Funds impressed in equity with a trust in Century's favour? If the Funds are subject to a trust, does this defeat Fisgard's claim?
> 4. Is Lawson Lundell entitled to a solicitor's lien over the Funds?
> 5. Is Lawson Lundell entitled to access the residue of the administrative charge on account of its fees and disbursements? [At para. 33.]

Items 4 and 5 will be the subject of our second hearing in this proceeding.

Res Judicata

[9] The chambers judge's analysis of *res judicata* began at para. 34 of his reasons. Fisgard Liberty contended that any claim by Century to the funds in trust was barred by both issue estoppel and cause of action estoppel in light of the chambers judge's earlier finding that Century's "advance of funds to Cliffs" on August 7, 2008, had violated the DIP Order. That the advance had indeed occurred was also reflected on the face of the order, which stated that "The advance of $500,000 by Century ... to [Cliffs] was not authorized" under the June 30 (DIP) Order, and that "Fisgard and Liberty are entitled to priority over the Funds." No appeal had been taken from that order. As a result, the lenders submitted, it was not open to Century to

assert arguments that could and should have been raised at the hearing on May 12, 2009, nor to attack collaterally what was said to be a final order, i.e., the order of June 30, 2009 declaring Fisgard Liberty's priority over the funds.

[10] The chambers judge reviewed the law relating to issue estoppel, which he noted (citing *Danyluk v. Ainsworth Technologies Inc.* 2001 SCC 44, [2001] 2 S.C.R. 460) applies only where the question said to be previously decided was "distinctly put in issue and directly determined by the court" at the previous hearing. (See also *R. v. Van Rassel* [1990] 1 S.C.R. 225 at 238.) After reviewing the motion material filed prior to the hearing on May 12, 2009, his earlier reasons for judgment and the resulting order of June 30, 2009, the judge concluded that what he had considered and decided on the previous occasion was limited to the "construction of a clause in the commitment letter, whether the loan was made in compliance with the required terms and conditions, and the relative priorities Century and Fisgard held in relation to those funds as a result of the advance having been made in a manner contrary to these terms and conditions." He continued:

> It is clear that issue estoppel does not bar what Fisgard itself characterized as Century's "new arguments", based on unjust enrichment and the law of trusts. The beneficial ownership of the funds was not a question decided at the May 12, 2009 hearing, nor was it raised in the parties' arguments or the reasons of this Court. Thus, it cannot be said that this question was "distinctly put in issue and directly determined" at that time. Neither party raised, nor did the Court address, any party's equitable interest in or entitlement to the funds at the previous hearing.
>
> Further, I find that Century is not barred by issue estoppel from arguing that the Funds were never advanced to the Cliffs. The previous hearing only addressed priorities within the context of the DIP charge, not at large.
>
> Finding that Fisgard was entitled to "priority" over the Funds insofar as the terms of the DIP Order were concerned was not a finding on the issue of ownership. A "priority" is distinct from an *in rem* interest in property: *Dinning v. Workmen's Compensation Board*, [1932] 1 D.L.R. 373 at 378 (B.C.C.A.). A priority is not a property right; rather, it is a relative or comparative term, a concept which is legally distinct from that of ownership or title: *Attorney General of Newfoundland v. Churchill Falls (Labrador) Corporation Ltd.* (1983), 49 Nfld. & P.E.I.R. 181 at 226, *aff'd*. on other grounds (1985), 56 Nfld. & P.E.I.R. 91 (Nfld. C.A.), *aff'd*. [1988] 1 S.C.R. 1085. [At paras. 45-7; emphasis added.]

[11] The chambers judge also rejected Fisgard Liberty's submission that his order of June 30 had conclusively established that Century had not retained "title" to the funds. In his analysis, issues of "ownership" and the "impact of legal and equitable principles beyond the narrow scope of the priority granted in the DIP order itself" had not been argued and were simply "not in the contemplation of the Court" at the time of the previous hearing.

[12] Alternatively, if he was wrong and issue estoppel was applicable in the circumstances, the chambers judge said he would exercise his discretion to refuse to apply the doctrine where it would work an injustice. Again in his words:

> These proceedings are not the "one shot" trial of an action, and of necessity have required multiple hearings. Great care must be taken in applying *res judicata* to proceedings in the same action, as distinct from separate actions between the same parties: *Talbot v. Pan Ocean Oil Corp*. (1977), 3 Alta. L.R. (2d) 354 at 360 (C.A.).
>
> Further, the key finality rationale which was held in *Danyluk* to underpin *res judicata* is of limited weight in the present circumstances, given that Fisgard knew that issues surrounding Lawson Lundell's entitlement to a solicitor's lien would require a subsequent application relating to the Funds, and that no conclusive finding as to their ultimate disposition had been made in my June 30 reasons.
>
> I do not accept that Century is precluded from advancing its claim. The public interest in ensuring that justice is done on the facts of this case requires entertaining the parties' submissions on the merits. [At paras. 52-4; emphasis added.]

[13] The chambers judge then turned to cause of action estoppel. Unlike issue estoppel, he noted, this principle does not require that the issue have been directly raised and decided by the court previously. The classic statement to this effect is found in *Henderson v. Henderson* (1843) 3 Hare 100, [1843-60] All E.R. 378, where Wigram, V.C. stated:

> In trying this question, I believe I state the rule of the court correctly when I say, that where a given matter becomes the subject of litigation in, and of adjudication by, a court of competent jurisdiction, the Court requires the parties to that litigation to bring forward their whole case, and will not (except under special circumstances) permit the same parties to open the same subject of litigation in respect of matter which might have been brought forward as part of the subject in contest, but which was not brought forward only because they have, from negligence, inadvertence, or even accident, omitted part of their case. The plea of *res judicata* applies, except in special cases, not only to points upon which the Court was actually required by the parties to form an opinion and pronounce a judgment, but to every point which properly belonged to the subject of litigation, and which the parties, exercising reasonable diligence, might have brought forward at that time. [At 381-82; emphasis added.]

[14] The chambers judge noted that "some flexibility" had been introduced to cause of action estoppel recently in *Hoque v. Montreal Trust Co. of Canada* (1997) 162 N.S.R. (2d) 321 (C.A.), where it was suggested that the language in *Henderson* was "somewhat too wide" and that the better principle was that "those issues which the parties had the opportunity to raise and, in all the circumstances, should have raised, will be barred." (At para. 37.) He also referred to *Buschau et al. v. Rogers Communications Inc.* 2003 BCSC 1718 (*rev'd on other grounds*, 2004 BCCA 142), where the Court observed that the rule in *Henderson* is of limited application to interlocutory applications and that judicial efficiency will often "be well served by allowing interlocutory applications to deal with only small parts of a larger picture." (Para. 36.)

[15] The chambers judge was not satisfied that cause of action estoppel had any application in the circumstances before him. This was not an instance, he said, in which Century was seeking any relief against Fisgard Liberty – indeed there was "no cause of action or claim asserted by Century against Fisgard". Instead, the dispute involved three competing creditors in a dispute over a pool of money. Further, the question litigated at the prior hearing had not decided the ultimate disposition of the funds. (Para. 65.) In the circumstances, the chambers judge found that cause of action estoppel had not been established and that in any event, he would again have exercised his residual discretion to refuse to apply the doctrine:

> I reiterate my earlier conclusion that it would be against the interests of justice if Century were precluded from arguing its legal and equitable entitlement to the funds, given that the issue was not considered, and that the fundamental "finality" consideration which underpins *res judicata* is of limited force in the circumstances. [At para. 68.]

Were the Funds Advanced to Cliffs?

[16] Being satisfied that neither issue estoppel nor cause of action estoppel applied to bar Century's motion, the chambers judge turned next to consider whether Century had in fact "advanced" the $500,000 *tranche* of DIP financing to the Company or its agents, thus (in Fisgard Liberty's submission) losing any rights to those funds. Even though Century had purported to advance the funds in breach of the appeal provision in the commitment letter, the chambers judge found that they had remained subject to the conditions specified in the DIP Order – that the Monitor authorize or request the release of funds and that the Monitor in consultation with the Company request Lawson to pay the funds out. The chambers judge said there was "no evidence" the Monitor had authorized or requested the funds and that accordingly, they had remained subject to a trust condition that would now never be satisfied. In his analysis:

> Where funds have been released by a lender to a borrower's solicitor with trust conditions governing their use, they do not become the property of the borrower until the trust conditions are satisfied. If the trust conditions are not satisfied, unspent funds must be returned to the lender. [At para. 78.]

This conclusion, the Court said, defeated the claims of both Fisgard Liberty and of Lawson. (Para. 89.)

Alternative Conclusions: Trust and Attachment

[17] Century argued in the alternative that Fisgard Liberty and Lawson would be unjustly enriched if they obtained the funds, but the chambers judge found a "clear juristic reason" – the

existence of the financing agreement between Cliffs and Century, the foreclosure proceedings taken against Cliffs, and Lawson's "purported statutory entitlement" to a solicitor's lien pursuant to the *Legal Profession Act* – for any deprivation Century might have suffered if the funds had been advanced and Fisgard Liberty or Lawson were to receive them. (Para. 93.)

[18] In the further alternative, Century submitted that regardless of whether the funds had been advanced to Cliffs, they had been subject to a *Quistclose* trust in Century's favour: see *Barclay's Bank Ltd. v. Quistclose Investments Ltd.* [1970] A.C. 567 (H.L.). It was clear that such trusts are subject to the requirement of the three certainties (see *Twinsectra Ltd. v. Yardley* [2002] 2 A.C. 164, [2002] 2 All E.R. 377 (H.L.) at paras. 70-1, 101; *Re Westar Mining Ltd.* 2003 BCCA 11 at para. 12; *Giles v. Westminster Savings Credit Union* 2007 BCCA 411 at para. 31.) With respect to certainty of intention, the Court reviewed Century's commitment letter, which stated that the purpose of the DIP loan was to further the "construction of a golf course and development of the home lots and source an irrigation source for the golf course." This purpose had the effect of restricting the Company's freedom to use the funds. (Para. 105.) The surrounding circumstances and the terms of the DIP order shed additional light on the parties' intention that the funds were not to be used to extinguish the Company's general liabilities or wind up the project. The chambers judge found as a fact that the terms of the commitment letter disclosed a mutual intention on the part of Century and Cliffs to create a *Quistclose* trust. (Para. 110.)

[19] Being satisfied that the second certainty – certainty of subject matter – was shown, the chambers judge found that the commitment letter provided adequate clarity for the Court to determine that if the funds had been provided either to Fisgard Liberty or Lawson following the demise of Cliffs' development project, the funds would have been misapplied, i.e., the trust would have been breached. Thus, he said, certainty of objects was also made out.

[20] The next question was whether, again assuming the funds had been advanced to Cliffs, a *Quistclose* trust alone could defeat Fisgard Liberty's registered security interest. The chambers judge accepted that a *Quistclose* trust is a form of resulting trust, which comes into existence when money is advanced rather than at the time the trust is judicially declared to exist: see *Twinsectra*, *supra*, at paras. 100-102. Existing case law suggested that a constructive trust is not defeated by a prior security interest registered under the *PPSA* (see *Ellingsen (Trustee of) v. Hallmark Ford Sales Ltd.* 2000 BCCA 458 and *Kimwood Enterprises Ltd. v. Roynat Inc.*

(1985) 15 D.L.R. (4th) 751 (Man. C.A.)), but it was unclear whether the same was true of resulting trusts.

[21] The chambers judge found it unnecessary to decide this point, since in his analysis, the *PPSA* security interest of Fisgard Liberty had never "attached" to the funds and could therefore not defeat or rank ahead of Century's "equitable ownership". (Para. 121.) He cited various authorities for the proposition that before an interest may attach, the debtor must have something more than mere possession of the collateral or an interest that is "trifling" or "completely contingent" in nature. (See paras. 122-29.) Since the advances to be made under the DIP loan facility had been conditional upon the Monitor's making a written request, he concluded that the Company had not had sufficient rights in the collateral for Fisgard Liberty's security interest to have attached, regardless of whether the funds had been "advanced" or not. In his analysis:

> ... The will of a third party (the Monitor) is an external condition upon which the Cliffs' entitlement to the money is entirely dependent, and is therefore a barrier to the Cliffs obtaining "rights in the collateral" beyond a mere expectation or contingent right to future enjoyment.
>
> The Cliffs certainly had a right to receive the collateral; but this right was contingent upon the Monitor making a request in writing which has not and never will be made. Century held the entirety of the beneficial interest in the Funds through the *Quistclose* trust; the Cliffs never had actual possession of the Funds, had no control over their disposition, and could not compel Lawson Lundell to disburse them. The agency of the Monitor was required. In these circumstances, I find that the Cliffs did not have sufficient "rights in the collateral" for Fisgard's security interest to attach. [At paras. 131-32; emphasis added.]

[22] In the result, the chambers judge's order, dated March 25, 2010, stated in material part:

> 1. The Fisgard and Liberty Motion is dismissed;
> 2. Lawson pay the sum of $162,276.33 held in Lawson's trust account to the credit of The Cliffs Over Maple Bay Investments Ltd. (the "Funds") to Century;
> 3. Lawson is entitled to payment of $81,422.72 on account of its fees and disbursements from the funds secured by the Administrative Charge granted herein by Order of the Court on May 26, 2008, unless an application for further relief in this regard is brought within 30 days of March 25, 2010;
> 4. Lawson's application for a declaration that it is entitled to a solicitor's lien over the Funds is dismissed; and
> 5. the parties each bear their own costs of the Lawson Motion and the Fisgard and Liberty Motion.

On Appeal

[23] Fisgard Liberty advanced the following grounds of appeal in its factum:

1. The learned Chambers Judge erred in law in determining *res judicata* did not bar Century from claiming entitlement to the Advance at the November 2009 hearing.
2. The learned Chambers Judge committed an error of law in determining the Fisgard/Liberty's security interest did not attach to funds in Lawson's trust account and with Century.
3. The learned Chambers Judge erred in law in holding that the funds in Lawson's trust account were subject to a *Quistclose* trust.
4. The learned Chambers Judge erred in law in finding that the funds in Lawson's trust account were not advanced to Cliffs.
5. The learned Chambers Judge erred in law in determining Lawson was entitled to the administration charge and that the charge had not been used up.

I propose to deal with item 1, and then with items 2, 3 and 4 together. Item 5, together with Lawson's grounds of appeal, will be addressed following the later hearing.

Res Judicata

[24] The appellant Fisgard Liberty acknowledged that whether *res judicata* should have applied to bar Century's motion is a question of law, reviewable on a standard of correctness. The only exception relates to the chambers judge's exercise of discretion not to apply the principle even if the circumstances of this case fell within its ambit. The appellant notes the well-known formulation of the circumstances in which an appellate court may interfere with such a decision – i.e., if the court below proceeded on a wrong principle or failed to give weight, or sufficient weight, to relevant considerations: see *Friends of the Old Man River Society v. Canada (Minister of Transport)* [1992] 1 S.C.R. 3 at 76-7; *Stone v. Ellerman* 2009 BCCA 294, (2009) 92 B.C.L.R. (4th) 203 at para. 94. We were also referred to a more recent formulation, which mandates intervention if the court below has misdirected itself as to the applicable law or made a palpable error in its assessment of the facts: see *British Columbia (Ministry of Forests) v. Okanagan Indian Band* [2003] 3 S.C.R. 371 at para. 43.

[25] The policy objectives underlying *res judicata* generally are well-known and have been discussed at length in the jurisprudence and in the academic context: see for example, Donald J. Lange, *Res Judicata in Canada* (3rd ed., 2010), chapter 1; *Henderson v. Henderson*, *supra*; *Hoystead v. Taxation Commissioner* [1926] A.C. 155 (J.C.P.C.); *Angle v. Minister of National Revenue* [1975] 2 S.C.R. 248; and *Danyluk v. Ainsworth Technologies Ltd.* 2001 SCC 44, [2001] 2 S.C.R. 460. The authors of Spencer Bower and Turner, *The Doctrine of Res Judicata* (4th ed., 2009), state:

> Two policies support the doctrine of *res judicata* estoppel: the interest of the community in the termination of disputes and the finality and conclusiveness of judicial decisions; and the interest of an individual in being protected from repeated suits and prosecutions for the same cause. Maugham L.C. said:
>
> > The doctrine of estoppel is one founded on considerations of justice and good sense. If an issue has been distinctly raised and decided in an action, in which the parties are represented, it is unjust and unreasonable to permit the same issue to be litigated afresh between the same parties or persons claiming under them.

[26] Appellate courts in Canada have emphasized that the importance of finality and the principle that a party should not be 'twice vexed' (*bis vixari*) for the same cause, must be balanced against the other "fundamental principle" (see *Hoque* at para. 21) that courts are reluctant to deprive litigants of the right to have their cases decided on the merits: see *Toronto (City) v. Canadian Union of Public Employees, Local 79*, 2003 SCC 63, [2003] 3 S.C.R. 77, at para. 55; *Revane v. Homersham* 2006 BCCA 8, 53 B.C.L.R. (4th) 76 (C.A.) at paras. 16-7; Lange at 7-8.

[27] *Res judicata* takes two forms in modern practice, cause of action estoppel (still sometimes called *res judicata*) and issue estoppel. Lange summarizes them as follows:

> In their simplest definitions, issue estoppel means that a litigant is estopped because the issue has clearly been decided in the previous proceeding, and cause of action estoppel means that a litigant is estopped because the cause has passed into a matter adjudged in the previous proceeding. [At 1.]

The distinction was described in more elaborate terms by Lord Denning, M.R. in *Fidelitas Shipping Co., Ltd., v. V/O Exportchleb* [1965] 2 All E.R. 4 (C.A.):

> The law, as I understand it, is this: if one party brings an action against another for a particular cause and judgment is given on it, there is a strict rule of law that he cannot bring another action against the same party for the same cause. Transit in *rem judicatam* ... But within one cause of action, there may be several issues raised which are necessary for the determination of the whole case. The rule then is that, once an issue has been raised and distinctly determined between the parties, then, as a general rule, neither party can be allowed to fight that issue all over again. The same issue cannot be raised by either of them again in the same or subsequent proceedings except in special circumstances ... And within one issue, there may be several points available which go to aid one party or the other in his efforts to secure a determination of the issue in his favour. The rule then is that each party must use reasonable diligence to bring forward every point which he thinks would help him. If he omits to raise any particular point, from negligence, inadvertence, or even accident (which would or might have decided the issue in his favour), he may find himself shut out from raising that point again, at any rate in any case where the self-same issue arises in the same or subsequent proceedings. ... But this again is not an inflexible rule. It can be departed from in special circumstances. ... [At 8-9; quoted with apparent approval in *Grandview v. Doering*, *infra*.]

[28] Although grounded in the same basic considerations, each form involves, or has traditionally involved, criteria that have been expressed in slightly different terms. The traditional criteria for cause of action estoppel, confirmed in Canada in *Angle, supra*, were summarized by Chief Justice Hewak in *Bjarnarson v. Manitoba* (1987) 38 D.L.R. (4th) 32 (Man. Q.B.) at 34, *aff'd.* (1987) 45 D.L.R. (4th) 766 (Man. C.A.), as taken from *Grandview v. Doering* [1976] 2 S.C.R. 621:

> 1. There must be a final decision of a court of competent jurisdiction in the prior action [the requirement of "finality"];
> 2. The parties to the subsequent litigation must have been parties to or in privy with the parties to the prior action [the requirement of "mutuality"];
> 3. The cause of action and the prior action must not be separate and distinct; and
> 4. The basis of the cause of action and the subsequent action was argued or could have been argued in the prior action if the parties had exercised reasonable diligence. [At para. 6; emphasis added.]

It is perhaps unnecessary to state that the doctrine contemplates two "causes" – the first having ended in a final judgment that bars a "second claim for the same cause": see *Mohl v. University of British Columbia*, 2006 BCCA 70 at paras. 23-4. In this context, "cause of action" does not refer to the name or classification given to the wrong or remedy, but to a factual situation which entitles one to a remedy: see also Lange at 147; *Comeau v*. *Breau* (1994) 145 N.B.R. (2d) 329 (C.A.) at para. 18; and *Letang v. Cooper* [1965] 1 Q.B. 222 (C.A.) at 242-43.

[29] Presumably, it is the breadth of the fourth requirement listed above ("could have been argued") that leads Fisgard Liberty to argue that cause of action estoppel can have application in the case at bar. The appellant cites four cases for the proposition that "both issue and cause of action estoppel apply to subsequent motions in the same proceeding on the same questions finally decided in an earlier motion". Three of these authorities – *Air Canada v. British Columbia* (1985) 21 D.L.R. (4th) 685 (B.C.C.A.), *Heather's House of Fashion Inc. (No. 2) (Re)* (1977) 24 C.P.R. (N.S.) 193 (Ont. S.C.J.), and *Las Vegas Strip Ltd. v. Toronto (City)* (1996) 30 O.R. (3d) 286 (Gen. Div.) – do not in my view support this proposition. *Air Canada* was decided on the basis of issue estoppel (see 697), and *Heather's* and *Las Vegas* involved proceedings that resembled separate causes of action (in the substantive, rather than the formal, sense), as opposed to steps taken in the same proceeding. The fourth case, *Re Agil Holdings Ltd.;* (also indexed as *Scherer v. Price Waterhouse* (1985) 32 A.C.W.S. (2d) 259 (Ont. H.C.J.), does take a

broader view than the prevailing one, and illustrates the difficulty in some cases of distinguishing between cause of action and issue estoppel.

[30] While it is arguable that the other conditions associated with cause of action estoppel exist in this case, I am not persuaded the chambers judge erred in concluding that because of the procedural context of the two orders – in particular, the fact this is a "dispute over a pool of money between three competing creditors" in one proceeding – the doctrine does not apply. At the very least, one would have to bend it considerably out of shape to fit the facts with which we are concerned. Given my view that issue estoppel applies, it is not necessary to go to these lengths.

[31] Turning then to issue estoppel, I note the three traditional "tests" adopted by the Supreme Court of Canada in *Angle*, namely:

> (1) that the same question has been decided;
>
> (2) that the judicial decision which is said to create the estoppel was final; and,
>
> (3) that the parties to the judicial decision or their privies were the same persons as the parties to the proceedings in which the estoppel is raised, or their privies. ... [At 254; emphasis added.]

There is also the well-known formulation of issue estoppel given by Middleton J.A. in *McIntosh v. Parent* [1924] 4 D.L.R. 420 (Ont. C.A.):

> When a question is litigated, the judgment of the Court is a final determination as between the parties and their privies. Any right, question, or fact distinctly put in issue and directly determined by a Court of competent jurisdiction as a ground of recovery, or as an answer to a claim set up, cannot be re-tried in a subsequent suit between the same parties or their privies, though for a different cause of action. The right, question, or fact, once determined, must, as between them, be taken to be conclusively established so long as the judgment remains. [At 422; emphasis added.]

[32] The narrow wording ("directly determined") adopted in these and other authorities, however, has not been construed as strictly as one might expect. In *Danyluk,* Binnie J. for the Court stated at para. 54 that issue estoppel applies "to the issues of fact, law, and mixed fact and law that are necessarily bound up [my emphasis] with the determination of that 'issue' in the prior proceeding". This would seem to echo the formulation provided by Lord Shaw in *Hoystead*:

> … Parties are not permitted to begin fresh litigations because of new views they may entertain of the law of the case, or new versions which they present as to what should be a proper apprehension by the Court of the legal result either of the construction of the documents or the weight of certain circumstances. If this were permitted litigation would

> have no end, except when legal ingenuity is exhausted. It is a principle of law that this cannot be permitted, and there is abundant authority reiterating that principle.
>
> Thirdly, the same principle – namely, that of setting to rest rights of litigants, applies to the case where a point, fundamental to the decision, taken or assumed by the plaintiff and traversable by the defendant, has not been traversed. In that case also a defendant is bound by the judgment, although it may be true enough that subsequent light or ingenuity might suggest some traverse which had not been taken. The same principle of setting parties' rights to rest applies and estoppel occurs. [At 165-66; emphasis added.]

The wording used in *Hoystead* (where it was held that issue estoppel applied not only to the admission of a fact fundamental to the first decision, but also to "an erroneous assumption as to the legal quality of that fact") which I have underlined above was approved in *Angle, supra*, at 255, and by this court in *Morgan Power Apparatus v. Flanders Installations Ltd*. (1972) 27 D.L.R. (3d) 249, at 252. (See also *Hill v. Hill* (1966) 57 D.L.R. (2d) 760 (B.C.C.A.) at 764; *Insurance Co. of the State of Pennsylvania v. Global Aerospace Inc*. 2010 SKCA 96 at para. 78; *Foster v. Reaume* [1927] 1 D.L.R. 1024 (Ont. S.C., App. Div.) at 1033; *Prince v. T. Eaton Co*.(1992) 91 D.L.R. (4th) 509 (B.C.C.A.) at 522.)

[33] Lange (see 58-65 and the cases cited therein) suggests that an "extended form" of issue estoppel has been adopted in some provinces such that any question that could have been decided or could have been raised at the first proceeding, will be barred in the second. However, this approach has not received appellate approval in this province, and when it has been used, seems not to have led to a different result than the traditional approach. (See the discussion in *Re Agil Holdings, supra*, and in Lange at 62-3.) Neither party relied on the extended form of issue estoppel in the case at bar.

[34] Century submits that both the requirement of finality and that of the "same question" are not met in the case at bar. Regarding finality, it contends at para. 59 of its factum:

> ... to the extent [the chambers judge's] Order addressed entitlement to the Trust Funds, Century submits that it was not final. Cause of action (and issue estoppel) only apply when the court has no further jurisdiction to hear the issues or to vary or rescind its decision. In this case [the chambers judge] retained jurisdiction to consider entitlement to the Trust Funds. To the extent [his] later decision contradicted his earlier one, the later decision is to be taken as the final one on the basis that it is the most informed expression of the Court's opinion. [Emphasis added.]

With respect, if by this Century is suggesting that having made a final order, a court may subsequently adopt a "more informed opinion" of the matter and proceed to contradict its earlier order, I must disagree. Obviously, this proposition flies in the face of the principle of finality which is the essence of *res judicata.* Nor did the court below "retain jurisdiction" to vary or

rescind its decision: only Lawson's claim, which had the potential of trumping that of Fisgard Liberty, was left for another day. The issue of priority as between Century and Fisgard Liberty was finally determined and the Court did not have jurisdiction to rehear it or to vary or rescind its order.

[35] In connection with the "same question" criterion, Century naturally relies on the chambers judge's observation that the issue of the "ultimate disposition of the funds" was not decided in the first proceeding. It says that since "issues of ownership" were not in the Court's contemplation, Century's position in the second hearing did not amount to a collateral attack on the first order; that the two applications concerned "different facts altogether"; that evidence advanced at the second hearing was not known to Century (although Mr. Roberts on behalf of Lawson suggested it was available) until Lawson's affidavit evidence was filed; and that:

> The two hearings related to separate and distinct causes of action, as the First Hearing sought a declaration in respect of the parties' priorities in respect of Cliffs' estate generally, whereas the Second Hearing concerned the parties' potential entitlement to the Trust Funds in particular.

[36] It is certainly true that the two hearings dealt with different issues. The question is whether the issues of advance, attachment and trust were "necessarily bound up" with or "fundamental to" the determination of priority as between Fisgard Liberty and Century. In my opinion, it is clear that to the extent the earlier order addressed priority, it assumed "entitlement". As a matter of logic, the question of whether the advance had been validly made to Cliffs (through its agent Lawson) should have been raised and determined before or as part of the determination of priority <u>over the advance</u> as between Century and Fisgard Liberty. A finding that Fisgard Liberty was entitled to priority in respect of the funds would seem to be "bound up with" or indeed to rest on the 'foundation' that the funds had indeed been advanced to Cliffs. (Indeed, it was precisely <u>because</u> Century had made an advance in violation of the 21-day period that it had lost its priority in the first hearing.) In the wording used by Lange, entitlement or ownership was part of the "latent structure supporting the express question [of priority] by virtue of an … assumed recognition of that structure." (*Supra*, at 47.) If the funds had not been advanced, the question of priority would have been moot. Priority was not a "threshold issue", as counsel for Century suggests; it was the ultimate issue.

[37] In this respect, the case at bar resembles *Zimbel Estate v. Pascoe* (1992) 80 Man. R. (2d) 142 (Q.B.), where a party who had participated in a proceeding to interpret a will was

barred from challenging the validity of the same will in a subsequent proceeding. The Court noted that "there is an underlying assumption that parties participating in an action for interpretation of the will have inferentially conceded its validity. Courts do not construct invalid wills. If there is some issue as to validity, that issue must first be determined." The Court also quoted the following passage from the 1969 edition of Spencer Bower and Turner, *Res Judicata*:

> Whenever it is shown that the party against whom a judicial decision is ultimately pronounced omitted to raise by pleading, argument, evidence, or otherwise some question, or issue, or point which he could have raised in his favour by way of defence or support to his case without detriment to his position or interests in the pending, or in future, proceedings, and which, therefore, it was his duty (in a sense) to have then raised, the adverse general decision, though it contains no express declaration to that effect, is deemed to carry with it a particular adverse decision on the question, issue, or point so omitted to be raised, just [as] much as if it had been expressly raised by the party, and expressly determined against him. And this is so whether the question or issue is simply passed over through inadvertence, or is made the subject of express or implied assumption or admission. [At 160.]

[38] Similarly, in *Ernst & Young Inc. v. Central Guaranty Trust Co.* 2006 ABCA 337, the Alberta Court of Appeal held that the defendant's apparent acceptance of the validity of certain trusts in a receivership proceeding barred it from challenging the validity of the trusts in a subsequent action. (See also *Hill v. Hill* (1966), 57 D.L.R. (4th) 760 (C.A.) at 769; *R. v. Duhamel* (1982) 33 A.R. 271 (C.A.) at 277-8 (*aff'd.* [1984] 2 S.C.R. 555.); Spencer Bower and Turner (2009), *supra*, at § 8.09, 8.10 and 8.12, and cases cited therein.)

[39] Ms. Buttery contends on behalf of Century that at the time of the first hearing in May 2009, her client was not aware of the amount of funds Lawson was holding in trust – a fact she says was important because Century needed to know whether the question of "entitlement" was "worth fighting about". Since it was clear, and the first order contemplated, that Lawson would be asserting entitlement to a solicitor's lien at a later date, she says it would be "incongruous" if other parties (i.e., Century) would not have been able to assert claims at a later date as well. In her submission, there was nothing in the record to suggest that the "super-priority" question (i.e., priority as between Fisgard Liberty and Century as the DIP lender) decided at the first proceeding was intended to be the only issue, or that its determination was to bar any of the parties from raising questions as to whether an advance had taken place and whether Cliffs' interest had attached. Although the parties' notices of motion and the first order itself had all referred to "advances" as though they were an accepted fact, Ms. Buttery emphasized that counsel were dealing with an unusual situation (i.e., the reversal of a stay granted under the

CCAA and the finding that the Supreme Court's authorization of DIP financing was invalid). This situation gave rise to many uncertainties in the course of the 'unwinding' of the restructuring, and counsel found themselves having to adapt to facts as they unfolded. Thus, it is implied, the requirements of due diligence should not be applied too stringently in this instance.

[40] These arguments may bear on the issue of the chambers judge's discretion, but I do not find them persuasive on the prior question of whether issue estoppel is technically applicable to this case. If counsel at the first hearing intended the Court to deal with only one of many issues, they should have made that clear to the other parties and to the Court, which may have had an opinion on the subject. They should have begun with what logically was the first issue – were the funds advanced? – and left the ultimate issue – which creditor has priority? – for later if that course was acceptable to the Court, and if it became necessary. They should have reserved not only the question of Lawson's entitlement in the order but Century's – a course that would have placed the problem of "conflict" front and centre. They should have been much more restrictive in the wording of the first order, ensuring that the Court would not be embarrassed by what appears to be a contradiction of its first order by the second order. If nothing else, this case is a cautionary tale for practitioners in the insolvency area about the importance of clearly informing the Court as to the issues being raised, and properly stating in the Court's order exactly what was determined and what was not.

[41] In my respectful view, the question of Cliffs' "entitlement" to the funds advanced by Century was, to paraphrase the reasoning in *Hoystead*, a "point fundamental to the [first] decision ... assumed by [Fisgard Liberty] and traversable by [Century] which was not traversed." I conclude that the chambers judge erred in permitting Century to re-open the question, and in ruling that its arguments were not barred by issue estoppel.

[42] This brings us to the exercise of the chambers judge's discretion not to apply issue estoppel, a question that is also dependant on case law that is not completely consistent and in which subtleties abound. In *Danyluk*, the Court ruled that it was an error of principle not to address the factors for and against the exercise of the discretion not to apply issue estoppel and that "The list of factors is open ... The objective is to ensure that the operation of issue estoppel promotes the orderly administration of justice but not at the cost of real injustice in the particular case." (Para. 67.) The most important of these, the Court said, was the potential for injustice since, as noted by Jackson J.A. in dissent in *Iron v. Saskatchewan (Minister of the Environment & Public Safety)* [1993] 6 W.W.R. 1 (Sask. C.A.):

> The doctrine of *res judicata*, being a means of doing justice between the parties in the context of the adversarial system, carries within its tenets the seeds of injustice, particularly in relation to issues of allowing parties to be heard. [At 21.]

[43] Binnie J. was referring, however, to the tribunal-to-court context rather than the court-to-court context. He noted the Court's earlier decision in *G.M. (Canada) v. Naken* [1983] 1 S.C.R. 72, where it was said that the discretion not to apply issue estoppel is "very limited in its application'". A broader discretion, Binnie J. stated, was warranted in relation to the decisions of administrative tribunals. This distinction was made in *Furlong v. Avalon Bookkeeping Services Ltd*., 2004 NLCA 46, where the Court emphasized that *Danyluk* had not modified *Naken, supra,* and that potential injustice becomes relevant only where, having exercised due diligence, a party has not received a "full and fair hearing". (At paras. 41-2; my emphasis.)

[44] In *Proctor & Gamble Pharmaceuticals Canada, Inc. v. Canada (Minister of Health)* [2004] 2 F.C.R. 85, Rothstein J., then of the Federal Court of Appeal, suggested for the majority that the discretion is limited to "special circumstances" (citing *Henderson v. Henderson, supra*, at 115), which would include fraud, misconduct or the discovery of decisive fresh evidence that could not have been adduced at the earlier proceeding by the exercise of reasonable diligence, although "fairness considerations could cancel the exercise of discretion." (Para. 29.) In *Saskatoon Credit Union Ltd. v. Central Park Enterprises Ltd*. (1988) 47 D.L.R. (4th) 431 (B.C.S.C.), Chief Justice McEachern described the exception as requiring "some overriding question of fairness" necessitating a rehearing. (At 438.)

[45] Fisgard Liberty contends that Century made no argument and led no evidence at the second hearing as to any "special circumstances" that would justify the chambers judge's decision declining to apply *res judicata* in this case. Whilst acknowledging that considerations of fairness are relevant, the appellant emphasizes that the first hearing occupied an entire day, that the parties filed extensive written submissions, and that both are "sophisticated commercial entities". Not surprisingly, Century responds that if the chambers judge "did not decide the ultimate disposition of the funds" and if the issues raised in the second hearing were "simply not in the contemplation of the court" in the first hearing (as the chambers judge himself suggested), it would be unfair if Century were held to be bound by the earlier order.

[46] It will be recalled that the chambers judge enunciated two reasons for finding that it would be contrary to justice to apply issue estoppel in this case. The first was that these proceedings are not the "one-shot" trial of an action and that "great care" should be taken in applying *res*

judicata to proceedings in the same action. On this point, he cited *Talbot v. Pan Ocean Corp*. (1977) 3 Alta.L.R. (2d) 354 (C.A.) at 360, where the Court was discussing the fact that in many interlocutory applications – e.g., an application for an interim injunction – the court proceeds on assumed or incomplete facts. Obviously, such applications do not give rise to final decisions, and *res judicata* has no place. (For this reason, it seems to me that the comment quoted by the chambers judge from *Buschau v. Rogers* (see para. 14 above) cannot be correct.) The Court in *Talbot* did not suggest that estoppel is to be applied with "great care" in subsequent motions once a final determination has been made on an issue; nor did it make any mention of the residual discretion not to apply issue estoppel.

[47] The second reason given by the chambers judge was that the principle of "finality" underlying *res judicata* was of "limited weight" in this instance, given that Fisgard Liberty knew a subsequent application would be necessary to decide Lawson's claim to the funds, and that no "conclusive finding as to their ultimate disposition" had been made in the order of June 30, 2009. As has been seen, however, Fisgard Liberty's status was squarely raised at the first hearing and Fisgard Liberty had no reason to think that the Court's declaration of priority over Century was anything less than a "conclusive finding" on that question.

[48] We are of course not exercising our discretion as a matter of first instance. The question for us is whether the chambers judge proceeded on a wrong principle or failed to give weight or sufficient weight to valid considerations in exercising his discretion as he did. In my view, he did err in failing to recognize the finality of his earlier order as between Century and Fisgard Liberty and in failing to give consideration to the narrowness of the circumstances in which his discretion could properly be exercised. It cannot be said "special circumstances" existed here: this was a monetary dispute between sophisticated lenders that had been decided in favour of one of them, and it was not open to the Court to change its mind in favour of a party that had thought of additional arguments that it could and should have mounted at the previous hearing. No overriding question of fairness was engaged. Indeed, in my view, it would be unfair to permit Century's arguments to prevail. I would allow the appeal on this ground.

"Advance" and "Attachment" Issues

[49] In the event I am wrong on the applicability of issue estoppel to this case, however, I turn to the alternative grounds of appeal advanced by Fisgard Liberty, namely that the chambers judge erred in determining that the funds in Lawson's trust account had not been advanced to

Cliffs and in finding that the appellant's security interest did not attach to the funds. In my view, these two issues are essentially the same: if the funds were indeed "advanced" to the Company (through its agent Lawson), then, subject to the remaining issue concerning the existence of a *Quistclose* trust, Cliffs would have been entitled to the funds and thus would have had a sufficient interest to which Fisgard Liberty's security could attach.

[50] It will be recalled that the chambers judge's order of June 27, 2008 authorized the Company to borrow an amount not exceeding $2,350,000 from Century, "provided that such advances under the DIP Facility will be made in *tranches* not to exceed $500,000, unless permitted by further Order of this Court". The conditions under which such advances would be made were specified:

> ... advances under the DIP Facility shall be made only at the request of the Monitor to the DIP Lender, such advances to be paid to Lawson Lundell LLP "in trust" and to be paid out only on the written request of the Monitor in consultation with the Petitioner [the Company], subject to further Order of the Court.

[51] The order also stated that the "DIP Facility" would be on the terms and conditions in the commitment letter, which in turn said the purpose of the loan was to "facilitate further construction of the golf course and development of the home lots and source an irrigation solution for the golf course." A commitment fee of 3% was to be deducted from each advance, "representing the Commitment Fee for the entire Facility and six months' interest for each draw."

[52] On or before July 17, 2008, Cliffs and the Monitor signed an "Order to Pay" addressed to Century and its solicitors, Boughton Law Corporation ("Boughton"). The material part of this document stated:

> Please accept this as your <u>irrevocable authority and direction</u> to payout [*sic*] of the first advance under the above referenced mortgage loan all taxes, assessments and utilities charged against the Property given as security; property valuation fee, solicitor's charges, accrued interest to interest adjustment date, and other expenses payable, and to pay all prior encumbrances on the Property as follows:
>
> | | |
> |---|---|
> | Mortgage Advance Amount | $500,000 |
> | <u>Less</u>: | |
> | The Lender's Commitment Fee | 70,500 |
> | The Lender's Six Month Interest Reserve | 54,000 |
> | Boughton Law Corporation | |
> | Holdback for estimated legal fees, disbursements and taxes to complete the transaction** | 25,000 |
> | Net mortgage proceeds under the 1st advance payable to Lawson Lundell LLP "In Trust" | $350,500 |
>
> Dated this 17th day of July, 2008. [Emphasis added.]

[53] On August 7, Boughton remitted its trust cheque to Lawson. Referring to Cliffs as "Borrower" and Century as "Lender", Boughton advised:

> Further to your recent correspondence with ... our office, we enclose our trust cheque payable to Lawson Lundell LLP In Trust in the sum of $350,000.00 representing the advance under the above loan, in accordance with the approved Order to Pay.
>
> The enclosed funds are sent to you on your undertaking not to release any portion of the funds to your client until we have provided you with our written authority that it is in order for you to do so.

The written authority referred to in the second paragraph was given later the same day by an email from Boughton to Lawson, confirming that:

> It is now appropriate pursuant to my instructions to release the monies you have in trust to your client. The only undertaking I impose upon your firm is to pay the due diligence fee of $25000 to Century Services Inc., care of Boughton Law Corporation.
>
> I also confirm that my client has waived the condition requiring no appeals to be filed. [Emphasis added.]

[54] The following day, Lawson forwarded its trust cheque in the amount of $25,000 payable to Century. According to the affidavit of Ms. Ferris of Lawson, her firm also disbursed $100,000 to the Monitor, $4,400 to 648962 B.C. Ltd., and $36,000 to Mr. and Ms. Paulin, the principals of Cliffs. (The $100,000 payable to The Bowra Group Inc. represented the costs of preparing the Altus Report, which had been the subject of a specific priority order mentioned earlier.) On August 15, further funds were disbursed by Lawson, leaving the sum of $162,276.33 in its trust account as at November 1, 2009.

[55] The chambers judge stated at para. 21 of his reasons that there was "no evidence that the Monitor requested the release of the Funds, as required by the DIP Order and they were never used by the Monitor or the Cliffs." With respect, the Company and the Monitor did sign the Order to Pay and surely an "order" goes even farther than a "request". In my view, it simply cannot be said that the conditions for the advance set forth in the order of June 27, 2008 were not met. I conclude, with respect, that the chambers judge fell into clear error at para. 89 of his reasons in finding that the funds remained held by Lawson on a trust condition "that has not and now never will be satisfied" and that therefore Century was entitled to their return.

Quistclose Trust

[56] This leads us to the final alternative argument, acceded to by the chambers judge, that the funds were impressed with a *Quistclose* trust in Century's favour, based on the terms of the

commitment letter which were incorporated by reference into the DIP Order of June 27, 2008. The letter described the purpose of the DIP Facility thus:

> 3. PURPOSE: To facilitate further construction of the golf course and development of the home lots and source an irrigation solution for the golf course.
>
> 8. CONDITIONS: The obligation of Century to make the facility available is subject to and conditional upon each of the following:
>
> a. Court [-] authorized DIP borrowing, with the funds to be used for development purposes as disclosed by the borrower. [Emphasis added.]

[57] A *Quistclose* trust is a purpose trust of a very special kind. Waters, Gillen and Smith in *Waters' Law of Trusts in Canada* (3rd ed., 2005) write that such trusts arise "when moneys are loaned by a lending institution expressly for the purpose for which the borrower intends to use the loan." (At 565.) The authors continue:

> These trusts occur when moneys are loaned by a lending institution expressly for the purpose for which the borrower intends to use the loan. The lender advances the moneys on the condition that they are to be held "on trust" by the borrower until the time for expenditure upon the purpose takes place. At that point in time, having the authority of the loan agreement, the borrower applies the moneys to the purpose and becomes a debtor *vis-à-vis* the lender. If the contemplated expenditure upon the purpose does not occur, the moneys are held in trust by the borrower for the lender – that is, ahead of all the unsecured creditors of the borrower. [At 565.]

[58] A somewhat narrower description was given in a Canadian case, *Niedner Ltd. v. Lloyds Bank of Canada* (1990) 72 D.L.R. (4th) 147 (Ont. H.C.J.):

> A Quistclose trust is created when A lends money to B for the specific purpose of enabling B to pay its creditors or a specific class of them ["C"]. The money is then impressed with a trust and may not be reached by third parties other than the beneficiaries of the trust. Assuming the purpose of the trust should fail, the money reverts back to the settlor of the trust. ... [At 151; emphasis added.]

[59] In fact, *Quistclose* trusts have had a broader application, at least in the U.K. In *The Quistclose Trust in a World of Secured Transactions* (1992) 12 Oxf. U. Leg. Stud. 333, Professor M. Bridge observes that they have arisen in three main situations**:**

> These cases are, for the most part, centred on three fact patterns, though the authorities relied upon in the *Quistclose* decision itself are confined to the first of these categories. First, A puts in funds B, a debtor, for the purpose of paying C, one of B's creditors. The practical issue here is whether the funds may be retained or recovered by B's trustee-in-bankruptcy. Secondly, A consigns goods to C in response to an order placed by B and A draws on B for payment of the price. The question here is whether the cargo has been appropriated to secure the due payment of the bill of exchange. This transaction can also occur in a two-party form, where A consigns goods to B and then, after so advising B, discounts a bill drawn upon B. Thirdly, A transfers to B, a bank, bills of exchange payable

> to A in payment for other bills drawn earlier by A upon B. B becomes insolvent before paying the bills drawn upon it. Is B merely indebted to A in respect of the bills transferred to it? Another bank insolvency problem occasionally presents itself where one bank is put in funds to be remitted to another bank and becomes insolvent before the remittance is made. [At 347.]

The author also notes certain characteristics common to the decided cases:

> A characteristic of these cases is the immediacy of the debtor's need for outside sources of funding. The debtor may already be faced with a bankruptcy petition by one of his creditors, who may be a judgment creditor, or he may be poised to abscond to evade his creditors, or already by lying in a debtors' prison. In one case, the money is paid over to the debtor to obtain the release of the payer's property from a sheriff executing on behalf of a judgment creditor of the debtor. It does no harm to the payer's case if the money advanced is still capable of being returned *in specie*. This was so in one case where it was a surety who was seeking the return of the money to the payer, who unlike the surety was unaware that the money was being advanced conditionally to save a bank from bankruptcy. In all of these cases, the party paying the money does so on an emergency, rescue basis and the debtor is merely a conduit through whom money is channelled to the outside creditor. In the circumstances, the debtor's possession of the money is far removed from misleading anyone entering into further dealings with him and any benefit accruing to the unsecured general creditors would be of a windfall nature. Nor is the payer, it seems, receiving anything in the nature of a premium or reward for the very high degree of risk attendant upon the transaction being a mere loan. It is therefore difficult to see that the payer receives an unfair advantage over the payee's other creditors, in the period leading up to the bankruptcy, making it unfair to allow him to retain or recover the money as the case may be. [At 348.]

[60] Such trusts are the subject of much controversy and academic comment in the United Kingdom, and it appears that they are used mainly there to overcome the vagaries of what Bridge describes as its "antiquated" property security laws (see 345.) Many questions about them remain unanswered, despite the important role played by Lord Millett in explaining them in the academic and judicial contexts: see *The Quistclose Trust: Who can Enforce it?* (1985) 101 LQR 269; *The Quistclose Trust – a Reply* (2011) 17:1 Trusts & Trustees 7. (See also Dennis R. Klinck, *Re-Characterizing the Quistclose Trust: Lord Millett's Obiter Dicta in Twinsectra* (2005) 42 Can. Bus. L.J. 427 at 428-31, and Michael Smolyansky, *Reining In the Quistclose Trust: A Response to Twinsectra v. Yardley* (2010) 16 Trusts & Trustees 558.)

[61] The first situation described by Professor Bridge existed in the *Quistclose* case itself, *Barclays Bank Ltd. v. Quistclose Investments Ltd., supra.* It involved a company, Rolls Razor Ltd., that had declared a dividend but was unable to pay it. The company negotiated a loan from Quistclose Investments Ltd. for the purpose of paying it, and the lender paid the money into a specific account at Barclay's Bank for this purpose. Before the dividend could be paid, however, Rolls Razor went into bankruptcy and the bank purported to apply the funds against

the bankrupt's outstanding indebtedness to the bank. The House of Lords held that a (resulting) trust had been created for the purpose of paying the dividend, which trust had "failed", entitling the original settler, the lender, to the return of the funds, and ensuring the bank did not enjoy what would have been a windfall.

[62] The chambers judge in the instant case began his discussion by noting the most recent leading case in this context, the decision of the House of Lords in *Twinsectra, supra.* Its facts were somewhat closer to those in the case at bar: a lender agreed to advance funds to "Y" for the specific purpose of enabling him to purchase certain property. The lender forwarded the loan proceeds in trust to a firm of solicitors on their undertaking to hold the funds until they were applied to the acquisition of the property by Y. The firm instead paid the funds to another solicitor, who simply paid them out on Y's instructions, utilizing some £358,000 for purposes unrelated to the acquisition. The second solicitor then went bankrupt, and the loan was not repaid.

[63] The House of Lords applied *Quistclose*, ruling that the money had been subject to a trust in the firm's hands, that the trust met the three certainties, that the firm was liable for breach of the trust, and that the second solicitor held the remaining funds in trust for the lender, subject to a power to apply it by way of loan to Y in accordance with the undertaking.

[64] The chambers judge quoted by way of overview a passage from the reasons of Lord Millett in *Twinsectra*, part of which I will also reproduce:

> Money advanced by way of loan normally becomes the property of the borrower. He is free to apply the money as he chooses, and save to the extent to which he may have taken security for repayment the lender takes the risk of the borrower's insolvency. But it is well established that a loan to a borrower for a specific purpose where the borrower is not free to apply the money for any other purpose gives rise to fiduciary obligations on the part of the borrower which a court of equity will enforce. In the earlier cases the purpose was to enable the borrower to pay his creditors or some of them, but the principle is not limited to such cases. [At para. 68.]

At the same time, his Lordship observed:

> A *Quistclose* trust does not necessarily arise merely because money is paid for a particular purpose. A lender will often inquire into the purpose for which a loan is sought in order to decide whether he would be justified in making it. He may be said to lend the money for the purpose in question, but this is not enough to create a trust; once lent the money is at the free disposal of the borrower. Similarly payments in advance for goods or services are paid for a particular purpose, but such payments do not ordinarily create a trust. The money is intended to be at the free disposal of the supplier and may be used as part of his cashflow. Commercial life would be impossible if this were not the case.

> The question in every case is whether the parties intended the money to be at the free disposal of the recipient: *In re Goldcorp Exchange Ltd* [1995] 1 AC 74, 100 *per* Lord Mustill. ... [Paras. 73-4.]

[65] As we have seen, in considering whether the three certainties were met in the case at bar, the chambers judge noted the statement of purposes for which the loan was to be used, finding that these were "intended to, and had the effect of, restricting the Cliffs' freedom to utilize the funds for purposes other than those set out in the commitment letter." (Para. 105.) Further, since the commitment letter had been executed after the Company had sought *CCAA* protection, Century was obviously aware that Cliffs' continued existence was "in doubt". He continued:

> ... In light of the danger that Century's funds would simply be used to satisfy other creditors and wind up the project instead of constructing and completing the development, it makes sense that Century set out the permitted purposes for which the Funds could be used in clauses 3 and 8(a) of the commitment letter. The purpose of Century's credit facility was not to pay secured creditors and wind up the project; rather, it was to provide funds which were required for the project's continued existence and completion. [At para. 107.]

[66] It will be recalled that the Order to Pay which was signed by Cliffs and the Monitor and then forwarded to Century and its solicitors, was somewhat more specific than the commitment letter about the purposes for which the first advance was to be used. (See above at para. 52.) It referred to the payment of prior encumbrances, taxes, assessments, utility charges, a property valuation fee, and solicitor's charges. The chambers judge seemed to assume that this "direction" from the Monitor to Century was in conflict with the commitment letter: he said it could not "negate or vary the terms of the purpose trust in the commitment letter." Having said this, he concluded without more that the language of the commitment letter disclosed a mutual intention between Century and the Company to create a *Quistclose* trust.

[67] With respect, I find myself in disagreement with much of the chambers judge's analysis. First, I doubt that a *Quistclose* trust was created. This is not a case in which A put B in funds in order to pay C, a creditor of B. (See *Niedner, supra*.) Rather, A (Century) put B (Lawson, not a debtor) in funds to disburse to B's client, C (Cliffs), on B's undertaking to hold the money until it received A's written authority to release to C. The undertaking was a type of trust, certainly, but did not, as in *Twinsectra,* impose a duty on B to supervise how its client C used the money. The trust was almost completely executed – Lawson disbursed most of the advance, including the $25,000 paid to A – and did not "fail" in the *Quistclose* sense.

[68] Nor is this a case like *Twinsectra*, in which the bankruptcy or insolvency of C made the purposes of the loan impossible, such that a resulting trust was necessary to ensure the monies reverted to A and did not fall into the hands of C's creditors. Indeed, A was fully aware of C's financial condition and believed at the time of the advance that it was entitled to the super-priority given by the DIP Order. Once it had obtained additional covenants from the borrower's principals, Century directed that the funds be disbursed. Upon all the conditions being met, the funds were *ipso facto* "advanced" to C. The Company would have been bound by contract to use the funds for the general purposes it had agreed on in the letter, but the monies were then its own, and but for this litigation, would presumably have been paid into its general bank account. As Lord Wilberforce observed in *Quistclose*, "in the absence of some special arrangement creating a trust ..., payments of this kind are made upon the basis that they are to be included in a company's assets." There was no obligation on Cliffs to hold what it received from the loan proceeds in any separate account; rather, as stated by Lord Millett in *Twinsectra*, "the money [was] intended to be at the free disposal of the [borrower]" and could be used as part of its cash flow.

[69] In short, although it is obvious that Cliffs agreed as a matter of contract that the funds would be used for the general purpose stated, I disagree that this restriction gives rise to any inference of an intention on the part of both parties (Century and Cliffs) to create the specialized vehicle that is a *Quistclose* trust. The only trust in existence here was the usual type created by the undertaking given to the lender by Lawson as Cliffs' solicitors. The terms of that trust were met, as were the terms of the DIP Order.

[70] Nor do I agree that the terms of the Order to Pay, under which the Monitor directed Century to pay the first *tranche* into Lawson's trust account and gave its "irrevocable authority" to pay out taxes, assessments, utilities, solicitor's charges and prior encumbrances, would have constituted a breach or "negation" of any trust or of the June 27 order incorporating the commitment letter. Century chose to make the advance it did in July 2008, fully aware of the circumstances that had led to the receivership and to the *CCAA* order, pronounced on May 26, 2008. We may assume Century had fully discussed the risk of lending to Cliffs and had decided that advancing funds for the specified purposes in the conditions prevailing in August was necessary or conducive to the Company's efforts to revive the project (which efforts were referred to by Tysoe J.A. in his reasons, *supra*, at paras. 14-5). And, by signing the Order to Pay, the Monitor must be taken to have indicated its satisfaction that the expenditures were

appropriate. Both decisions were judgements that in my opinion were not unreasonable, and ones that a court should not second-guess.

[71] In summary, I conclude that:

- the chambers judge did not err in finding that cause of action estoppel did not apply;
- the chambers judge did err in finding that the criteria for issue estoppel were not met. Although different questions were addressed and different evidence was adduced in the two hearings, the issues addressed in the second proceeding were a foundational element of the first order;
- the chambers judge erred in the exercise of his discretion not to apply issue estoppel in that he failed to recognize the finality of his first order, and the requirement for "special circumstances" such as fraud or the discovery of fresh evidence that due diligence could not have brought forward. No such circumstances were present in this case;
- the chambers judge erred in finding that the conditions in the DIP Order for the advances by Century were not met;
- contrary to the finding below, the *tranche* which Century purported to advance on August 7, 2008 was advanced in fact and in law, and Fisgard Liberty's interest thereupon attached to the funds and remains attached to the residue still held by Lawson, subject to the outstanding issue of Lawson's claim;
- the chambers judge erred in finding that a *Quistclose* trust was intended or created; and
- the chambers judge erred in ruling that the use by Cliffs of the funds for the purposes stated in the Order to Pay would have been a violation of the commitment letter or the order that incorporated it.

[72] I would therefore allow Fisgard Liberty's appeal and declare that as between it and Century, its interest in the funds ranks in priority to any interest of Century, but that pending this court's determination of Lawson's claim to the funds (or settlement of that issue by the relevant parties) the funds shall continue to be held by Lawson in trust.

"The Honourable Madam Justice Newbury"

I Agree:

“The Honourable Madam Justice Prowse”

I Agree:

“The Honourable Mr. Justice Chiasson”