Court File No.: CV-13-10280-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

B E T W E E N :

DBDC SPADINA LTD.
AND THOSE CORPORATIONS LISTED ON SCHEDULE A HERETO

Applicants

- and -

NORMA WALTON, RONAULD WALTON,
THE ROSE & THISTLE GROUP LTD. and EGLINTON CASTLE INC.

Respondents

- and -

THOSE CORPORATIONS LISTED ON SCHEDULE B HERETO,
TO BE BOUND BY THE RESULT

FACTUM OF THE MOVING PARTY

December 18, 2013

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Lawyers for CDPQ Mortgage Investment Corporation

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PART I—OVERVIEW

1. Otera Capital, servicer and agent of CDPQ Mortgage Investment Corporation ("**Otera**") in relation to the mortgage of the land and buildings located at 1500 Don Mills Road, Toronto and related personal property (the "**Property**"), brings this motion to exclude the Property and El-Ad (1500 Don Mills) Limited ("**El-Ad**"), registered owner of the Property, and Donalda Developments Ltd. ("**Donalda**"), the beneficial owner of the Property (collectively, the "**Borrower**") from the application of the order of Justice Newbould dated November 5, 2013 (the "**Receivership Order**").

2. Otera is the first mortgagee on the Property. The mortgage is in default – with serious events of default (preceding the Receivership Order) including an unauthorized second mortgage and failure to pay water bills.

3. Otera seeks to be able to exercise its rights and remedies in relation to the Property and the Borrower.

4. There is no basis to stay Otera from exercising its rights and remedies in the circumstances of this case. In addition, the Property and Borrower should not have been grouped together with other unrelated properties and entities in one receivership, which gives rise to conflicts and prejudice. Moreover, the terms of the Receivership Order, including priming charges imposed without notice to Otera, are highly prejudicial to Otera.

5. The Property and the Borrower should be excluded from the application of the Receivership Order.

PART II—FACTS

The Property and Mortgage: 1500 Don Mills

6. The Property is located at the south-east corner of Don Mills and York Mills in Toronto. The building on the Property is a 10-storey multi-tenant office building, constructed in 1979. It has been occupied by a diverse group of 19 tenants, with low historical vacancy rates, and has been cash flow positive.[1]

7. There will be a significant vacancy of approximately 1.5 floors as of June 30, 2014 unless another tenant is found promptly.[2]

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[1] Affidavit of Robert Duranceau, Motion Record of Otera, Tab 2 (**"Duranceau Affidavit"**), at paras. 3-5

[2] Duranceau Affidavit at para. 6

8. Otera is the first mortgagee on the Property. The mortgage was granted pursuant to a commitment letter and related first mortgage and other security (collectively, the "**First Mortgage**") with the Borrower.[3]

9. Otera provided a mortgage loan to the Borrower in the principal amount of $31,000,000 (the "**First Mortgage Loan**") to assist with the purchase of the Property by the Borrower.[4] The First Mortgage Loan is secured in first priority and the principal amount presently outstanding is $30,308,322.01, plus interest, fees and other costs, which continue to accrue.[5]

10. The First Mortgage was granted to the Borrower in reliance on various documents and representations, including the Officer's Certificate of Donalda, which did not reveal any involvement in that entity by Dr. Bernstein or any Applicant, and in reliance on the delivery of first-ranking security and various terms and protections provided in the First Mortgage.[6]

Receivership Order Granted Without Notice to Otera

11. Otera did not have notice of the Receivership Order until it received a letter dated November 19, 2013 from counsel to Schonfeld Inc. Receivers + Trustees (the "**Manager**") attaching a copy of the Receivership Order and endorsement of Justice Newbould dated November 5, 2013. Otera did not have prior notice of the motion to obtain the Receivership Order, did not have knowledge of the motion, did not attend at the hearing of the motion, and did not consent to the Receivership Order.[7]

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[3] Duranceau Affidavit at para. 2
[4] Duranceau Affidavit at para. 7
[5] Duranceau Affidavit at para. 14
[6] Duranceau Affidavit at para. 12
[7] Duranceau Affidavit at paras. 16-17

12. In particular, Otera did not consent to the imposition of the Manager's Charge or the Manager's Borrowings Charge (as defined in the Receivership Order, the "**Priming Charges**"), which purport to have first priority ahead of Otera, as first mortgagee.[8]

13. It is unclear whether the First Mortgage, Otera's interests (including the fact that serious events have default had already occurred under the First Mortgage) or the fact that Otera was not provided with notice of the motion was sufficiently disclosed to Justice Newbould on the motion.[9]

14. There does not appear to be any relationship between the Borrower and the Property, on the one hand, and any other entity or property subject to the Receivership Order, on the other, except to the extent that the entities listed on Schedule "B" to the Receivership Order are alleged to each be separately incorporated entities that have common shareholders.[10]

Defaults under the Mortgage

15. At the time the Receivership Order was granted, the First Mortgage was in default.[11]

16. Among other events of default, an unauthorized second mortgage was placed on the Property on August 1, 2013 in favour of Windsor Private Capital Inc. in the principal amount of $3,000,000. Otera had no knowledge of this second mortgage before it was added and did not approve it.[12]

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[8] Duranceau Affidavit at para. 29
[9] Duranceau Affidavit at para.18
[10] Duranceau Affidavit at para. 19
[11] Duranceau Affidavit at para. 20
[12] Duranceau Affidavit at para. 21

17. In addition, the Borrower failed to pay certain water bills relating to the Property as they became due, which gives rise to an event of default. On November 15, 2013, Otera paid $37,229.24 to the City of Toronto from the tax reserves in satisfaction of the overdue water bills to ensure continued supply of water to the Property.[13]

18. On November 15, 2013, Otera sent a letter to the Borrower noting the water tax arrears, which Otera paid in full after receiving a Final Notice, and the second mortgage that Otera had discovered, stating "Both matters have caused our mortgage to be in default."[14]

19. Further, Otera later learned that Dr. Bernstein was allegedly a shareholder of Donalda Developments Ltd. ("Donalda"). This too is an event of default as it implies the representations made by the Borrower to Otera were incorrect or that the Borrower failed to strictly and fully observe or perform its covenant not to make any changes to the authorized share capital or allocation or ownership of Donalda, which would result in a change of voting control or beneficial ownership thereof without the prior written consent of Otera.[15]

Unrelated Fees Paid from Property Revenue

20. On or about December 3, 2013, Otera learned that the Manager had applied its *entire* November fees and expenses as against the Property and three other properties, with the largest portion (approximately $53,000) coming from the Property revenue, apparently because there were funds available in the accounts relating to such properties.[16]

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[13] Duranceau Affidavit at paras. 22-23
[14] Duranceau Affidavit at para. 24
[15] Duranceau Affidavit at para. 25
[16] Duranceau Affidavit at paras. 36-37

PART III—ISSUES

21. The main issue to be determined on this motion is whether the Borrower and the Property should be excluded from the broad receivership in which it is grouped together with separate entities and properties. Otera submits that carving the Borrower and Property out of the Receivership Order - either by way of an order amending, varying or setting aside the Receivership Order as it relates to the Borrower and the Property, or by way of lifting the stay of proceedings to permit Otera to exercise its rights and remedies (and varying and/or amending the Receivership Order to subordinate the Priming Charges) – is just and appropriate.

PART IV—LAW AND ARGUMENT

This Court Has Jurisdiction to Vary, Amend or Set Aside the Receivership Order

22. Rule 37.14 of the *Rules of Civil Procedure* provides as follows:

> 37.14 (1) A party or other person who,
>
> (a) is affected by an order obtained on motion without notice;
>
> (b) fails to appear on a motion through accident, mistake or insufficient notice; or
>
> (c) is affected by an order of a registrar,
>
> may move to set aside or vary the order, by a notice of motion that is served forthwith after the order comes to the person's attention and names the first available hearing date that is at least three days after service of the notice of motion.
>
> (2) On a motion under subrule (1), the court may set aside or vary the order on such terms as are just.

23. The Receivership Order was granted without notice to Otera (indeed the First Mortgage and the defaults arising thereunder may not have been sufficiently disclosed to Justice Newbould on the motion).

24. As holder of the First Mortgage on the Property that is subject to the Receivership Order, Otera is negatively affected and significantly prejudiced by the Receivership Order.

25. This motion has been brought promptly after the Receivership Order came to the attention of Otera (2 weeks after it was issued) and after attempts to consensually address the deficiencies in the Receivership Order with the Manager and the Applicant. As such, the Receivership Order may be set aside or varied under on such terms as are just.

26. In this case, varying the Receivership Order as requested by Otera is just for the reasons set out herein.

It is Inappropriate to Stay the First Mortgagee

27. Including the Property and Borrower in the Receivership Order and imposing a stay of proceedings that purports to stay Otera's rights and remedies as first mortgagee in relation to the Property was not appropriate relief.

28. The First Mortgage was in default at the time the Receivership Order was granted, with serious events of default having occurred including the imposition of a second mortgage on the Property without Otera's knowledge or consent, and failure to pay taxes to the City of Toronto, which resulted in Otera being forced to pay such amounts.

29. Otera holds first-ranking security on the Property and should be entitled to exercise its rights and remedies in relation to its collateral. There is no allegation of fraud or bad faith on the part of Otera and the circumstances do not justify restraining Otera from a proper exercise of its contractual rights.[17]

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[17] *Arnold v. Bronstein et al*, [1971] 1 O.R. 467-470 (Ont. H.C.J.).

30. Permitting a shareholder (of whom Otera had no knowledge) to prevent Otera from exercising its rights and remedies as first mortgagee in furtherance of a shareholder dispute – particularly without providing notice to Otera or conspicuous disclosure to the Court regarding Otera's rights and interests (including the serious defaults under the First Mortgage) – is inappropriate.

The Property Should Not Be Grouped With Unrelated Properties in One Receivership

31. In addition, and in any event, the Property and the Borrower should not be grouped into this broad receivership.

32. The Schedule "B" corporations subject to the Receivership Order are separate corporations. There is no apparent relationship between the Borrower and the Property, on the one hand, and any other entity or property subject to the Receivership, on the other, except to the extent that the entities listed on Schedule "B" are alleged to be separately incorporated entities that have common shareholders.

33. This is not a case in which there is a central, integrated business in which each corporation is a necessary part of the whole or in which corporations are supported by inter-corporate guarantees. Rather, each corporation is a separate entity with separate assets and creditors.

34. While the Schedule "B" entities allegedly have common shareholders, even the shareholder agreements allegedly also required the corporations to be treated separately. The Endorsement describes at paragraphs 23-24 that the agreements between Dr. Bernstein and the Waltons required each company to be treated separately but that, contrary to those agreements, the Waltons co-mingled funds among companies, noting the following, among other things:

> "It is clear that the Waltons did not treat each company separately as was required in the agreements for each company." (at paragraph 24)
>
> "The Inspector reports, however, that there has been extensive co-mingling of bank accounts and that funds were routinely transferred between the company accounts and the Rose & Thistle account." (at paragraph 23)
>
> "The co-mingling of accounts and the cash sweep into the Rose & Thistle accounts was a breach of agreement and unfairly prejudicial to Dr. Bernstein and a disregard of his interests." (at paragraph 46(3))

35. The fact that a shareholder allegedly wrongly co-mingled funds among separate corporations is no reason to group those entities together in one receivership and, in essence, appoint a receiver of all of the properties to do the same thing. The Receivership Order continues to leave properties and their stakeholders exposed to having funds expropriated without their consent to fund expenses incurred for the benefit of the stakeholders of other corporations.

36. Moreover, combining such entities together in one receivership puts the Manager in an impossible position of conflict. Each of the corporations has separate interests, which conflict, and there is no integrated, overarching operating business to benefit from cooperation among the separate estates.

37. A court appointed receiver is an officer of the court and acts in a fiduciary capacity with respect to all parties interested in the assets under the control of the receiver.[18] In this case, separate entities with separate assets have been combined into one proceeding at the request of a shareholder that apparently has an interest in each corporation. There are no common assets or operating business nor are there inter-company guarantees linking the companies together. As a result, the Manager cannot meet its fiduciary duties to the stakeholders of one corporation in the combined receivership without, by the same act, breaching its fiduciary duty to another. As one example,

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[18] Turbo Logistics Canada Inc. v. HSBC Bank Canada, 2009 CanLII 55292 (ONSC.) at para. 13.

deducting the Manager's fees to deal with unrelated properties and expenses from the revenue of the Property may have benefitted some but plainly did not benefit and was not in the interests of stakeholders of the Property.

38. In addition, there is no legitimate reason to force the Property into a receivership together with unrelated entities. There are no efficiencies or economies of scale at issue in this case. Each property will have to be managed and sold separately in a manner that is appropriate and commercially reasonable. To the contrary, *in*efficiencies arise by grouping disparate entities and properties together in that the Manager is occupied dealing with many distinct issues and not able to apply its full attention to the specific interests of the Property.

39. The allegations of co-mingling are no reason to continue to subject the Property to this broad receivership. Otera has first-ranking security over the Property. Otera is willing and able to realize on the Property in an efficient and commercially reasonable manner. A dispute among shareholders may continue as may investigations into co-mingling among different entities in which the shareholders have invested but there is no basis for that dispute to prevent a first mortgagee from exercising its rights and remedies and no reason for it to do so.

40. In any event, the only allegations of co-mingling relating to the Property are that funds obtained from the unauthorized second mortgage flowed *out* of the Property. Any claims arising from such outflow should be pursued against the other corporations or entities into which the funds allegedly flowed, which may include other corporations subject to the Receivership Order. The Manager cannot properly perform that task without conflict.

41. Grouping the Property in with others in the Receivership Order is not appropriate or necessary for the reasons outlined above. Worse, doing so is prejudicial to Otera and the other creditors of the Borrower for the additional reasons set out below.

42. First, Otera should not be forced to subject its collateral to the substantial costs that are likely to be incurred in this contested receivership with a broad scope that is far beyond the steps required to protect and realize on the Property. This receivership, arising as it has in the context of a contested oppression application in which the relationship between the Applicants and Respondents has obviously broken down, appears to have been strongly contested throughout. Not only has each Court appearance been contested and complicated by various issues that do not concern Otera but also the Manager has been occupied with a variety of issues, including tracing of funds, and reviewing equity contributions and investments by the Applicants and Respondents that would be unnecessary in a proceeding focused on the Property.

43. Second, the Manager is occupied with numerous other properties, entities and issues in addition to the Property. Especially at this time when the Property has a significant potential vacancy that needs to be filled and will be marketed for sale, careful attention must be paid to the Property and its tenants. Otera should be entitled to ensure the Property is properly protected and that issues relating exclusively to the Property are addressed by a party focussed on the Property and not distracted by numerous unrelated issues and properties.

44. Third, and of immense concern, the Property has been used to fund fees for the Manager's work that was unrelated to the Property, and it continues to be exposed to the potential expenses, fees and borrowings of the *entire* receivership. There are no restrictions in the Receivership Order limiting the application of funds from Property revenue to expenses (including Manager fees,

expenses or borrowings) specific to the Property and, as a result, the Receivership Order does not prevent a circumstance in which *all* fees, expenses or borrowings could be applied against *one* property in priority to the first mortgagee notwithstanding that the properties are owned by separate corporations, with separate stakeholders.

45. The Property, which has been described as a one of the best properties subject to the Receivership Order, has already been a victim to this injustice when fees of the Manager, including for actions unrelated to the Property, were paid from the Property revenue without Otera's knowledge or consent. It is unfair and inappropriate to use the Property to fund fees, expenses or borrowings related to other properties when such expenditures in no way benefit the Borrower or its stakeholders, including Otera.

46. Otera's first-ranking security should not be left exposed in this manner. The Receivership Order should be varied and/or amended to remove the Borrower from the list of Schedule "B" corporations bound by the Receivership Order and/or set aside as it relates to the Borrower and the Property.

Charges Should Not be Granted in Priority to Otera

47. In the alternative (in conjunction with a lifting of the stay, if required), the Priming Charges should be subordinated to the First Mortgage. As a general rule, the security of a prior secured creditor is not to be subjected to liability for fees and disbursements of a receiver:

> When a court appoints a general receiver of the property of an individual or a corporation, at the instance of a creditor other than a mortgage lienholder, part or all of this property may be covered by liens or mortgages. The general purpose of a general receivership is to preserve and realize the property for the benefit of the creditors in general. No receivership may be necessary to protect or realize the interests of lienholders. In such cases the mortgagees and lienholders cannot be deprived of their property nor of their property rights and the receivership property cannot as a rule be used nor the business carried on and operated by the receiver in such a way as to subject

> the mortgagees and lienholders to the charges and expenses of the receivership. A court under such circumstances has no power to authorize expenses for improving or making additions to the property or carrying on the business of the defendant at the expense of prior mortgagees or lienholders without the sanction of such mortgagees or lienholders.[19]

48. There are three exceptions to that general rule:

1. If a receiver has been appointed at the request, or with the consent or approval, of the holders of security, the receiver will be given priority over the security holders;

2. If a receiver has been appointed to preserve and realize assets for the benefit of all interested parties, including secured creditors, the receiver will be given priority over the secured creditors for charges and expenses properly incurred by him; and,

3. If the receiver has expended money for the necessary preservation or improvement of the property he may be given priority for such expenditure over secured creditors.[20]

49. To grant a security in priority to a secured creditor, one of the exceptions must apply. Priority cannot be removed "by stealth or suggestion."[21] None of the exceptions apply in this case.

50. The first exception does not apply here. Otera did not consent to or approve the appointment of the Manager or the terms of the Receivership Order. Indeed, Otera was not given notice of the motion seeking the Receivership Order despite holding first-ranking security on the Property.

51. The second exception does not apply here. The Receivership Order, which groups the Property in with other unrelated properties and exposes it to the continued expropriation of funds to support unrelated expenses, is not for the benefit of the Property or its stakeholders, including Otera. The Receivership Order arose in the context of a dispute among shareholders and is not necessary to protect or realize on the interests of Otera. To the contrary, the Receivership Order has prevented

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[19] *Robert F. Kowal Investments Ltd. v. Deeder Electric Ltd.*, [1975] O.J. No. 2363 (C.A.) at para. 12 *per* Houlden J.A. [*Kowal Investments*], citing Clark On Receivers, 3rd ed., by Ralph Ewing Clark

[20] *Terra Nova Management Ltd. v. Halcyon Health Spa Ltd. (Receiver-Manager of)*, 2005 BCSC 1017 at para. 30, aff'd, 2006 BCCA 458 [*Terra Nova*], citing Kowal; See also *Alma College v. United Church of Canada*, [1996] O.J. No. 1309 (Ont. C.A.) at para. 2

[21] *Terra Nova*, *supra* at para. 44

Otera from exercising its rights and remedies as holder of the First Mortgage, has placed the Property and Property revenue under the control of another party, and has resulted in funds being taken from the Property revenue to fund expenses unrelated to the Property, among other things.[22]

52. Moreover, notice must be provided for the second exception to apply: "with regard to the first and second [exceptions], the secured creditor must either apply for, consent to, or approve of, the appointment of a receiver or have notice under the second exception."[23]

53. No notice of the Receivership Order was given to Otera and these proceedings are not for its benefit but rather are prejudicial to Otera.

54. Finally, the third exception does not apply here. This is a very narrow exception that relates solely to emergency situations not present here:

> "The third exception, it seems to me, deals with a different type of situation, really one where there are circumstances which require the receiver to do something to preserve the property in an emergency situation where there is no time to come to the court beforehand and give notice to the creditors beforehand of what he intends to do…"[24] [*emphasis added*]

55. The First Mortgage is in default. Otera should be entitled to exercise its rights and remedies and should not be subjected to prior-ranking charges to fund the broad receivership and investigations at the behest of and in the interest of a shareholder. As the Ontario Court of Appeal noted in *Alma College v United Church of Canada*:

> We are of the opinion that the appeal must succeed. The general rule that the security of a prior secured creditor is not to be subjected to liability for fees and disbursements of a receiver governs the situation at hand. The receiver's right to indemnity in so far as the

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[22] Duranceau Affidavit at para. 40

[23] *Lochson Hldg. Ltd. v. Eaton Mech. Inc.*, 1984 CanLII 444 (BCCA) at para. 11 [*Lochson*]; See also *Kowal Investments, supra* at paras. 16 and 19.

[24] *Lochson, supra* at para. 13.

> subject property is concerned is concerned to the debtor's equity in the property. The circumstances of this case are not such as to bring it within any of the exceptions to the general rule, entitling a receiver to priority over the secured interests of mortgagees…
>
> The mortgages in question have long been in default and notices exercising power of sale were served prior to the appointment of the receiver. The appellants are entitled to enforce their security; there is no reason to stay their right to do so. They have no interest in the investigation that has been or that may be conducted by the receiver into the affairs of Alma College or into assets that may be held by it in trust for restricted charitable purposes. As matters presently stand, on the figures presented to the court the appellants would be required to pay the entire costs of the receivership. Their recovery on the realization of their security cannot be subjected to charges relating to matters which are of no concern to them as mortgagees."[25]

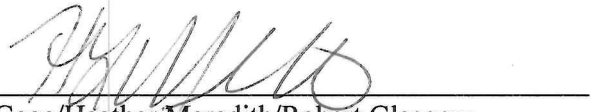
Lifting the Stay

56. To the extent a lifting of the stay is required, it is appropriate in this case as Otera is likely to be materially prejudiced by the stay's operation and it is equitable to lift the stay (for the reasons set out herein). There is no prejudice to the receiver or any other interested party in allowing the lifting of the stay to enable Otera to exercise its rights pursuant to the First Mortgage.[26]

PART V—ORDER REQUESTED

57. Accordingly, for the reasons set out herein, Otera respectfully requests the relief set out in its Notice of Motion.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.



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[25] *Alma College v. United Church of Canada,* [1996] O.J. No. 1309 at paras. 2-3.

[26] *Peoples Trust Company v. Rose of Sharon (Ontario) Retirement Community,* 2012 ONSC 7319 at para. 5; **vis** *Re Francisco*, 1995 CanLII 7371 (ON SC) at para. 1, aff'd 1996 CanLII 10233 (ON CA); *Re Ma,* 2001 CanLII 24076 (ONCA) at paras. 2-3.

SCHEDULE "A" – LIST OF AUTHORITIES

1. *Arnold v. Bronstein et al*, [1971] 1 O.R. 467-470 (Ont. H.C.J.)
2. *Turbo Logistics Canada Inc. v. HSBC Bank Canada*, 2009 CanLII 55292 (ONSC)
3. *Robert F. Kowal Investments Ltd. v. Deeder Electric Ltd.*, [1975] O.J. No. 2363 (C.A.)
4. *Terra Nova Management Ltd. v. Halcyon Health Spa Ltd. (Receiver-Manager of),* 2005 BCSC 1017, aff'd, 2006 BCCA 458
5. *Alma College v. United Church of Canada,* [1996] O.J. No. 1309 (Ont. C.A.)
6. *Lochson Hldg. Ltd. v. Eaton Mech. Inc.,* 1984 CanLII 444 (BCCA)
7. *Peoples Trust Company v. Rose of Sharon (Ontario) Retirement Community,* 2012 ONSC 7319
8. *Re Francisco*, 1995 CanLII 7371 (ON SC), aff'd 1996 CanLII 10233 (ON CA)
9. *Re Ma,* 2001 CanLII 24076 (ONCA)

SCHEDULE "B" – LIST OF STATUTES

Rule 37.14 of the *Rules of Civil Procedure*:

37.14 (1) A party or other person who,

(a) is affected by an order obtained on motion without notice;

(b) fails to appear on a motion through accident, mistake or insufficient notice; or

(c) is affected by an order of a registrar,

may move to set aside or vary the order, by a notice of motion that is served forthwith after the order comes to the person's attention and names the first available hearing date that is at least three days after service of the notice of motion.

(2) On a motion under subrule (1), the court may set aside or vary the order on such terms as are just.

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Court File No: CV-13-10280-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE - COMMERCIAL LIST

Proceeding commenced at Toronto

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