IN THE SUPREME COURT OF NOVA SCOTIA
IN BANKRUPTCY
Citation: Dorey (Re), 2008 NSSC 234

Date: 20080731
Docket: B 31844
Registry: Halifax

District of Nova Scotia
Division No. 1 - Halifax
Court No. 31844
Estate No. 51-933191

In the Matter of the Bankruptcy of Gregory Paul Dorey

IN THE MATTER OF THE APPLICATION OF GENEVA FLORENCE HEMEON FOR LEAVE TO CONTINUE AN ACTION AGAINST THE BANKRUPT'S INSURER

- and -

2006 S.K. No. 268782

IN THE SUPREME COURT OF NOVA SCOTIA

BETWEEN:

GENEVA FLORENCE HEMEON

PLAINTIFF

- and -

THE MUNICIPALITY OF THE DISTRICT OF WEST HANTS, CHERYL LYNN LAWRENCE, ~~JOHN KENNETH LAWRENCE~~ and GREGORY DEAN DOREY

DEFENDANTS

D E C I S I O N

Registrar: Richard W. Cregan, Q.C.

Heard: May 30, 2008

Counsel: Matthew Moir representing the Applicant, Geneva Hemeon
Philip M. Chapman and Andrew Gough representing the bankrupt, Gregory Dorey
David A. Graves, Q.C. representing the Municipality of the District of West Hants
Francyne Hunter and Emilie Garnier representing the Office of Superintendent of Bankruptcy

[1] This is an application by Geneva Florence Hemeon, the Plaintiff in this action, for an order under Section 69.4 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, (*BIA*), to permit her to continue the action against Gregory Paul Dorey, one of the Defendants, notwithstanding the stay which was imposed on the action by Mr. Dorey's assignment in bankruptcy on February 20, 2007, and subsequent discharge on November 21, 2007.

[2] In 2005, Mrs. Hemeon purchased a house in Windsor, but shortly thereafter detected the presence of mold in it, possibly caused by the deficiency of the drainage surrounding the house. She brought this action against the Defendant Municipality alleging its failure to properly inspect the building and its misrepresentation respecting its compliance with by-laws, against the Defendant Mrs. Lawrence from whom she had purchased the house alleging breaches in various terms, conditions and warranties of the agreement of purchase and sale between them, and against Mr. Dorey, who had been the contractor who built the house, alleging misrepresentation on his part respecting compliance with by-laws and codes.

[3] Mr. Dorey was covered by a policy of insurance issued by the Economical

Insurance Group at the time his alleged misrepresentations were made.

Section II of the policy reads in part:

> You are insured for claims made against you arising from ... 1. Personal Liability - legal liability arising out of your personal action anywhere in the world.

[4] Mrs. Hemeon is no longer able to pursue this claim against Mr. Dorey, as by his discharge from bankruptcy he is released from it. However, she wished to continue with the action against him so as to obtain a judgment against him which she may be able to enforce against his insurer.

[5] Mr. Dorey's trustee, BDO Dunwoody Goodman Rosen Inc., does not object to these proceedings provided no action is taken against Mr. Dorey personally.

[6] The Municipality appeared at the hearing through its solicitor David A. Grave, Q.C. It supports Mrs. Hemeon's application.

[7] Andrew Montgomery, the solicitor for Mrs. Lawrence, advised the court by letter that she does not take issue in this application.

[8] Mr. Dorey responds to this application through his solicitor Philip M. Chapman, who was represented at the hearing by Andrew Gough, then an articled clerk. They were appointed by Mr. Dorey's insurer to act in his defense in this action, but on the understanding that there is a high possibility that indemnity will not be provided.

[9] The following Sections of the *BIA* are relevant:

> 69.3 (1) - Subject to subsections (2) and (3) and sections 69.4 and 69.5, on the bankruptcy of any debtor, no creditor has any remedy against the debtor or the debtor's property, or may commence or continue any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy, until the trustee has been discharged.
>
> 69.4 - A creditor who is affected by the operation of sections 69 to 69.31 or any other person affected by the operation of section 69.31 may apply to the court for a declaration that those sections no longer operate in respect of the creditor or person, and the court may make such declaration, subject to any qualifications that the court considers proper, if it is satisfied
>
> (a) that the creditor or person is likely to be materially prejudiced by the continued operation of those sections; or
>
> (b) that it is equitable on other grounds to make such a declaration.

[10] In essence, as a result of Mr. Dorey's assignment Mrs. Hemeon has not been able to continue her action against Mr. Dorey, nor for practical reasons against the other defendants and will not be able to do so, until Mr. Dorey's

trustee is discharged. This may take time which will delay the advance of the action.

[11] However, Section 69.4 permits the court to lift this stay. The question before me then is whether there are grounds to do so.

[12] In *Advocate Mines Ltd. (Re)* (1984), 52 C.B.R. (N.S.) 227, (Ont.), Registrar Ferron noted in paragraph 2 a number of situations where courts have found it appropriate to remove stays of proceedings. Of relevance is the following:

> 4. Actions brought to establish judgment against the bankrupt to enable the plaintiff to recover under a contract of insurance or indemnity or under compensatory legislation.

[13] I was asked in *Jenkins Re: Brookville Carrier Flatbed GP Inc.* v. *Blackjack Transport Ltd.,* 2005 NSSC 234, for similar relief. This was a case where an action was brought against several defendants, but was subject to a stay as against one defendant who was under a Division I Proposal.

In paragraphs [6] to [11] of my decision I gave the following review of the law:

> Section 69.4 has been recently interpreted by the Ontario Court of Appeal

in *Re Ma* (2001), 24 C.B.R. (4th) 68. This case concerned the creditor of an undischarged bankrupt bringing a motion for an order lifting the stay of proceedings to permit the commencement of a fraudulent misrepresentation action against the bankrupt.

The central issue was whether an applicant is required to establish a *prima facie* case for the proposed action. This question was earlier reviewed in *Re Francisco* (1995), 32 C.B.R. (3rd) 29 (Ont. Bktcy.), affirmed at (1996), 40 C.B.R. (3rd) 77 (Ont. C.A.)

In that case a *Construction Lien Act* proceeding involved an action against a director who became bankrupt. Leave was sought to proceed against the bankrupt. Adams J found that the pleadings were sufficient to bring the claim arguably within s.178(1)(d) and lifted the stay.
He said at page 30:

> In considering an application for leave, the function of a bankruptcy court is not to inquire into the merits of the action sought to be commenced or continued. Instead, the role is one of ensuring that sound reasons, consistent with the scheme of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c .B-3, exist for relieving against the otherwise automatic stay of proceedings. (underlining added)

In *Re Ma* this statement was affirmed.

The point is also expressed using a different adjective to describe the reasons required in *Wychreschuk v. Sellors* (1988), 71 C.B.R. (N.S.) 37 (Man. Monnin J.) in paragraph 5:

> In order for leave to be granted, an applicant must demonstrate to the court that there exits compelling reasons to permit an action either to commence or proceed. (underlining added)

The practical result of these authorities is that the applicant in a section 69.4 application is not required to prove a *prima facie* case, or actually prove any facts respecting the case, rather it is for the applicant to satisfy the court either that it is likely to be materially prejudiced by the stay or that there are other equitable grounds for lifting it.

[14] The thrust of the Applicant's submission centres on *Superline Fuels Inc.* v. *Buchanan* (2007), NSCA 68, 32 C.B.R. (5th) 1.

The question in this appeal is stated in the first paragraph.

> 1 An absolute order of discharge releases a bankrupt from all claims provable in bankruptcy. But how does that order affect a claimant which, before the bankrupt made an assignment in bankruptcy, brought an action against him but had not obtained judgment before the absolute discharge order, and where, at all material times, the bankrupt had insurance against the type of loss claimed? Does the order act as a complete defence to the claim? Or can a claim against the insurer survive that order?

[15] In effect this decision says that the order does not act as a complete defence. A claim against an insurer may survive discharge and the claimant may be able to take advantage of Section 28 of the *Insurance Act*, RSNS 1989, c. 231, which I quote:

> (1) Where a person incurs a liability for injury or damage to the person or property of another, and is insured against such liability, and fails to satisfy a judgment awarding damages against him in respect of his liability, and an execution against him in respect thereof is returned unsatisfied, the person entitled to the damages may recover by action against the insurer the amount of judgment up to the face value of the policy, but subject to the same equities as the insurer would have if the judgment had been satisfied.
>
> (2) This section does not apply to motor vehicle liability policies.

[16] The effect of the lengthy decision of Oland J A is expressed in paragraph 58

> I am not persuaded that the bankrupt judge erred by relying on the

> reasoning in *Miller (Re)*, supra and the cases referred to therein and thereafter that, although s. 178(2) releases the bankrupt from claims provable in bankruptcy, it does not extinguish the debts that form the basis of such claims. In the appeal before us, this means that s. 178(2) releases Buchanan, from having to satisfy the debt, but it does not extinguish the underlying legal obligation. As I will explain, that underlying obligation survives for the purpose of the insurance policy and s. 28 of the *Insurance Act*, whether the extent of the obligation is crystallized by settlement or judicial determination before or after the order for discharge issues. (underlining added)

[17] I need not proceed to review the reasoning in this decision. Mr. Dorey's counsel conceded that where there is insurance in place the decision is determinate of the right for a creditor to have a stay lifted so that it can pursue a judgment, which although not enforceable against the now discharged bankrupt, can be enforceable against his insurer under the above quoted section of the *Insurance Act.*

[18] However, he says that it is not applicable to the situation where coverage is denied or not admitted. He is thus saying that establishing insurance coverage is a condition precedent to having a stay lifted under the authority of the *Buchanan* case. I think the principle of the case as quoted in [16] is unaffected by whether there is insurance coverage or not.

[19] An applicant should be able to proceed to prove its case. If successful, obtain its judgment and seek relief under Section 28 of the *Insurance Act*. It is at this point that the issue of coverage should be determined.

[20] To follow submissions of Mr. Dorey's counsel in an application such as this would be to allow an insurer to unilaterally frustrate creditors with claims which may possibly be indemnified by making self serving statements regarding coverage, without having to submit such statements to judicial scrutiny. I do not think that such should be allowed.

[21] However, I think the problem of whether the *Buchanan* case covers the situation where insurance coverage is in question can for the present purposes be avoided. Instead I rely on the cases mentioned in the passage from my earlier decision quoted in [13]. One is not required to prove that there is a *prima facie* case. Rather one is directed to look at the situation of the applicant and ask whether the applicant is likely in the circumstances to be materially prejudiced. Mrs. Hemeon is making a claim against Mr. Dorey. Mr. Dorey is no longer personally liable for the claim. Mr. Dorey has insurance which at least on the surface appears possibly to be available to

Mrs. Hemeon.

[22] A reasonable foundation particularly with the assertion in the *Buchanan* case about the underlying legal obligations remaining has been set to suggest that Mrs. Hemeon may be entitled to be paid by the insurer for any damages for which Mr. Dorey may be liable, but for his having been discharged from bankruptcy. She should have the opportunity to pursue this possibility. Otherwise I think without the declaration sought she will be "materially prejudiced" in being denied the opportunity to pursue a course of action which may be of benefit to her. Whether she will be successful or whether the insurer will have a defence is for another court to determine.

[23] I think this is a "sound reason" or a "compelling reason" for allowing the action to continue against Mr. Dorey.

[24] Mrs. Hemeon's application will be granted.

[25] The title of this application refers only to the style of the bankruptcy proceedings and not to the action itself. Houlden, Morawetz & Sarra in *The*

Annotated Bankruptcy and Insolvency Act at F§53(1), says that the application to lift a stay is to be styled both in the bankruptcy proceedings and in the action. I follow that in this decision. The order to follow should be similar and should provide for this amendment to the style.

[26] I shall hear the parties regarding costs.

R.

Halifax, Nova Scotia
July 31, 2008