Court of Queen's Bench of Alberta

Citation: Contessa (Re), 2018 ABQB 608

Date: 20180815
Docket: B203 287217
Registry: Edmonton

In the Matter of the Bankruptcy
of John Luigi Contessa

Reasons for Decision
of
W.S. Schlosser, Registrar in Bankruptcy

Introduction

[1] This is a bankrupt's Application for a discharge with some section 173 facts proved. There is a large exempt asset. The Application is opposed by the bankrupt's largest creditor. The central issue is how an exempt asset should be treated in determining the terms for discharge.

List of Authorities by the parties:

- ***Storey (Re)***, 2012 ABQB 746 (per Smart R);
- ***Fredette (Re)***, 2003 MBQB 167 (per Ring R);
- *Bankruptcy and Insolvency Act*, RSC 1985 c B-3.

List of Authorities by the Court:

- "407 ETR, Moloney and the Contested Meeting of Rehabilitation in Canada's Personal Bankruptcy System", A Lund, Saskatchewan Law Review, 2016 Volume 79;
- Roderick J Wood, *Bankruptcy and Insolvency Law*, 2nd edition, Toronto ON; Irwin Law Inc, 2015;
- "Does No Mean No? The Treatment of Exempt Assets on Discharge from Bankruptcy: Are the [2007] Amendments to the BIA Pro-Debtor?" AM Diamond (then Deputy Registrar in

Bankruptcy, Ontario Superior Court of Justice in Bankruptcy) Annual Review of Insolvency Law, ed Janis P Sarra, Thomson Carswell;

- ***Poettcker (Re)***, 2007 ABQB 718; (2007), 38 CBR (5th) 259 Alta QB per Bielby (now JA);
- ***Nelson (Trustee of) v Nelson***, [1995], 33 CBR (3d) 292 (Sask QB);
- ***Gustafson (Re)***, 2018 ABQB 77;
- 'BIA Preference Payments: Evidence Rebutting the Presumption must be Objectively Reasonable' Jasmine Girgis ABlawg, March 8, 2018.

Facts

[2] Until about 15 years ago, the bankrupt worked as a school teacher and built up RRSP's totalling over $500,000. Then he started a business; Lenaco Homes Master Builder Inc. ATB financed the company. The bankrupt guaranteed his company's debts.

[3] The company ran into trouble. Despite attempts at restructuring, the business ended in spectacular failure. The company is now bankrupt and so is Mr. Contessa. The ATB's proven claims are close to $24 million dollars. It is not known what will be recovered in the corporate bankruptcy.

[4] The s 173 facts that are proved or admitted are: first, that the bankrupt's assets were less than 50 cents on the dollar compared to his unsecured liabilities (s 173(1)(a)). Second, it appears that Mr. Contessa borrowed some money from his wife late in the day and, on the eve of his bankruptcy, made some payments on behalf of the corporation; preferring some corporate creditors over others (s 173(1)(h)). Approximately $203,000 was transferred to Mr. Contessa by his wife and used to pay trades in an effort to keep the company operating. Mr. Contessa thought he was doing this with the blessing of the ATB. Finally, it appears that Mr. Contessa's company continued to trade after becoming aware of being insolvent (s 173(1)(c)).

[5] When s 173 facts are proved, s 172(2) requires that the Court choose one of the three following options:

a) refuse the discharge of the bankrupt;

b) suspend the discharge for such period as the Court thinks proper; or

c) require the bankrupt, as a condition of his discharge, to perform such acts, pay such monies, . . . or comply with such other terms as the Court may direct.

[6] The bankrupt is a 'first-timer'. He has complied with all of his duties under the Act and has no surplus income. But for the s 173 facts, he would be entitled to an automatic discharge with no conditions.

[7] The bankrupt's lawyer (and the trustee) suggest that the Court grant the discharge but suspend it for one month.

[8] The ATB would like a Conditional Order with a hefty monetary condition roughly matching the value of the RRSPs.

[9] The bankrupt is 59. There is no evidence of his financial prospects for the future, or his employability. Upon discharge, the bankrupt might begin to draw upon his Canada Pension and

his RRSPs and enjoy a “fresh start” that is more a primrose path than the steep and rocky road experienced by most other bankrupts.

[10] The question is whether, in these circumstances, the Court should grant a discharge and, if so, on what terms.

Balancing

[11] Though it and the case referred to were s 172(1) cases, Registrar Smart, in ***Re Storey***, sums up the balancing exercise expected of the Court; citing Justice Wedge in the earlier ***Re Nelson*** decision at para 17:

> Section 172(1) gives this court the discretion to grant or refuse an absolute discharge although no bankruptcy offence has been committed. It is well established that in exercising its discretion a court must balance three things: The interest of the creditors in being paid, the interest of the rehabilitation of the bankrupt and the integrity of the bankruptcy process and the public's perception of it (see for example Re Shakell (1988), 70 C.B.R. (N.S.) 270 (Ont. S.C.)). In an oft-quoted passage, the court in Re Crowell (1989), 74 C.B.R. (N.S.) 121 (N.S.T.D.), said that the whole matter must be looked at in "the light of reason, common sense and humanity", having regard to the fundamental policy of the Act.

The exercise is the same here. The central issue is how the bankrupts RRSP assets figure into the balancing exercise.

RRSPs

[12] The purpose of RRSPs is to insure against becoming a burden on society when you are too old to work. As Professor Wood puts it (at p 114), the purpose of exempting certain assets is to enable a debtor “. . . to preserve his or her independence and self-sufficiency so the cost of the continued maintenance of the debtor does not fall to society.” (***Re Pearson*** (1997) 46 CBR (3d) 257 (AltaQB); ***Investors Group Co v Eckhoff***, [2008] 9 WWR 306 (SaskCA)).

[13] RRSP investments are supported by the *Income Tax Act*, RSC 1985, Chapter I (5th supplement) as a tax free (trust) arrangement. They are exempt from seizure under s 92.1(2) of the Alberta’s *Civil Enforcement Act*, RSA 2000, Chapter C-15, and s 580(2) of the *Alberta Insurance Act*, RSA 2000, Chapter I-3.

[14] RRSPs do not form part of the property of the bankrupt (*Bankruptcy and Insolvency Act*, s 67(1)(b.3). This specific July 2007 amendment added to the general exclusion of exempt assets under s 67(1)(b).

[15] The question posed by Registrar Smart was:

> . . . But should [an exemption] overrule the more general consideration that in arriving at appropriate financial conditions in a discharge order, the court should have regard to the bankrupt's financial situation as a whole? (***Re Storey*** at para 8)

[16] The existence of this asset appears to touch all of the three arms of the balancing equation: the interest of creditors, the rehabilitation of the bankrupt, public perception and the integrity of the system. It is not difficult to find examples of exempt assets being taken into

account (eg: ***Re Nelson*** and ***Re Fredette***) though most of these cases are pre-Amendment and outside of this province.

[17] Deputy Registrar Diamond (as he then was) put it this way (in 'Does No Mean No' at p 476)

> The issue of the proper treatment of exempt assets is particularly important in Alberta where significant real property is protected from seizure. If the value of exempt assets is not taken into account, bankrupts may be discharged from bankruptcy while still having a significant net worth and their creditors receive nothing.

[18] There are other exemptions both in this province and under the *Bankruptcy and Insolvency Act*, which are not insignificant. The *Bankruptcy and Insolvency Act* treats income below a threshold set by the Superintendent, as essentially exempt from consideration. Other significant exempts are found in s 88(f) and (g) of *Albertas Civil Enforcement Act*, which, together with the *Regulations*, exempts $40,000 worth of equity in the bankrupt's principal residence and up to 160 acres of farmland, if an enforcement debtor's primary occupation is farming. These exemptions are imported into the Bankruptcy and Insolvency realm by virtue of s 67(1)(b).

[19] The treatment of exempt assets seems to vary from province to province. In Alberta, for example, trustees do not seem to be reticent to sell assets with an exempt portion to obtain non-exempt equity for the benefit of creditors. This does not appear to the case in Saskatchewan, for example, where the entire homestead appears to be exempt from sale (eg ***Nelson***). But none of this detracts from the central issue of how these assets should be considered on discharge.

[20] Professor Lund has made a number of scholarly contributions to the area of the exercise of judicial discretion at discharge applications; not only in the form of her doctoral thesis but in the paper noted above. She finds generally that there are divergent views about how judicial discretion should be exercised at discharge applications, especially on the issue of rehabilitation. It is no different here. The discretion to impose terms seems largely unfettered by case law or principle.

[21] In his paper, Registrar Diamond notes the Alberta case of a bankrupt elk farmer in ***Re Poettcker***. In that case, Bielby J (now JA) affirmed the decision of Registrar Wacowich and permitted a unconditional discharge in the face of roughly $380,000 of assets exempt at the time of the bankrupt's assignment into bankruptcy). ATB was the objecting creditor in that case as well.

[22] After a review of authority (though all pre-Amendment) Bielby J stated at para 34:

> I conclude that the Registrar made no error in the result by declining to require this Bankrupt to make further payments through imposing a conditional discharge from bankruptcy. If his decision is to be interpreted as indicating that he believed he had no discretion to consider the size of this Bankrupt's exemptions, or that the legislative provisions creating those exemptions compelled him to discount them entirely when deciding whether to grant a conditional discharge, then it may have constituted an error.

[23] Regrettably for us, the learned justice does not weigh in on whether the amendments to the Federal legislation that occurred roughly contemporaneously with the decision should inform the result in future cases and her dicta in ***Re Poettcker*** does not finalize the matter.

[24] Registrar Diammond treats ***Re Poettcker*** as a significant shift in Alberta law and goes on to say that earlier cases in the Province treated the exemptions as "absolute" (at pg 477) or "sacrosanct" (at pg 478). Like Registrar Smart, (and with respect), I am not sure Alberta Courts have been quite so religious.

[25] In my view, if there is no evidence of financial means to satisfy a monetary condition other than the involuntary liquidation of an exempt asset, it should not be ordered. In this type of fact scenario, no really does mean no.

[26] I do not think, it is open to me as a Registrar to find, for example, that a debtor should be able to get by with $35,000 rather than $40,000 worth of exempt equity in a principal residence, to lower the threshold of exempt income set by the Superintendent, or to erode the exemption of an RRSP; contrary to both Provincial and Federal legislation, by pointing to what I think public perception might be. If a fictional right-thinking person on the John Deere (or Case) Combine thinks otherwise, they will have to speak to their MP.

[27] I have no evidence of the bankrupt's financial prospects for the future as I would if he were a high tax debtor seeking a discharge (eg s 172.1(4)(d)). I cannot presume that the bankrupt will do any better than he has been doing for the past nine months and begin to enjoy income that exceeds the Superintendent's standards. I have no means of imputing income as I would if there were evidence that Mr. Contessa were deliberately and intentionally under-employed. The bankrupt must have had some business skills and acumen to build up his company but, on the other hand, his recent track record (and the state of the Alberta economy where home building is concerned) does not suggest that he will be eminently employable in that field. I do not know whether the bankrupt could requalify as a teacher.

[28] On this basis, I am not inclined to impose a financial requirement as a condition for discharge.

[29] I do this whether the *Bankruptcy and Insolvency Act* is self-contained and whether debt relief and rehabilitation are synonymous or whether it would be appropriate to go further and be satisfied that the bankrupt is unlikely to repeat the mistakes that led to the bankruptcy in the first place by imposing conditions showing financial responsibility beyond the counselling and the reporting already required by the Act. The evidence is just not there.

Two Other Factors

[30] There are, in my view, two other considerations that might impact the exercise of discretion in this case but these go primarily to the issue of a period of suspension. The first of these is the gravity of the s 173 breaches.

i) Section 173(1)(a) (Less than 50 Cents on the Dollar)

[31] In this case, the bankrupt is a corporate guarantor. Most guarantees permit direct and independent recourse against a guarantor; which is why the guarantee legislation is assiduous in requiring that the guarantors exposure be explained as a condition of the validity of the guarantee. I admit that $24 million dollars against assets of approximately $1.0 million (as per the Form 82) is staggering disparity. However, I do not have any idea of and there is no evidence

of what the recovery and the corporate bankruptcy will be. In other words, there really is no concrete proof of whether the s 173(1)(a) breach will ultimately be sustained. We will have to wait and see.

[32] I also take notice of the fact that the ATB is a high sophisticated lender. To keep things in perspective, it would be difficult to say in these circumstances that the bankrupt was profligate but that the ATB's lending practices were blameless. There is an element of conscious shared risk that deflates the s 173(1)(a) disparity somewhat.

ii) Section 173(1)(c)(h) (Preferences and Trading while Insolvent)

[33] Mr. Contessa paid some trades in an effort to keep his business going. He thought he was doing so with the blessing of the major creditor. I note that this type of preference might be excused in other circumstances if it makes objective business sense [***Gustafson (Re)***, 2018 ABQB 77 and Jasmine Girgis, ABlawg, March 8, 2018; 'BIA Preference Payments: Evidence Rebutting the Presumption must be Objectively Reasonable']. In the circumstances, I give these s 173 breaches very little weight.

Remorse and Acknowledgement of Responsibility to your Creditors

[34] I note that bankrupt's counsel seemed to put the blame on the lender for his bankruptcy, which is not a good thing for a bankrupt to do, as it would seem to be the opposite of showing remorse, or responsibility, for your financial circumstances. The bankrupt did attempt to do a workout and restructuring which, to my mind, counts almost as much as having made a creditable Proposal, in terms of showing responsibility for his financial situation.

[35] Consideration of the exempt asset in itself is not a basis for imposing a financial condition on discharge. There is no principled basis on which to presume that the bankrupt is presently able to contribute more than the threshold amount set by the Superintendent. If an objecting creditor seeks to have the financial condition imposed, or seeks a significant suspension, they should present evidence to the Court to justify it. In this case particularly, I expect that the objecting creditor is in as good a position as anyone to address these points.

[36] Furthermore, I do not believe that a lengthy period of suspension and reporting are necessary. I suppose we could suspend the discharge for a time to give the bankrupt an opportunity to 'up his game' on the income front and to see how the corporate bankruptcy plays out. But there is nothing in the conduct of the bankrupt that would particularly justify a punitive or exemplary suspension and nothing to suggest that a further period of suspension and reporting might have a salutary effect on a bankrupt's rehabilitation. If nothing else, the objecting creditor's net claim may be diminished by the recovery in the corporate bankruptcy, but I do not think that the circumstances justify a 'wait and see' approach. I might just as well pick a figure out of the air.

Disposition

[37] For all these reasons, the bankrupt's discharge is allowed but suspended for one month.

Dated at the City of Edmonton, Alberta this 15th day of August, 2018.

W.S. Schlosser
Registrar in Bankruptcy

Appearances:

John T A Stainton and Avnish Nanda
of Mintz Law
for John Contessa

Pantelis Kyriakakis
of McCarthy Tetrault
for the Trustee PricewaterhouseCoopers Inc.

John Regush
of Dentons Canada LLP
for ATB Financial