CITATION:, 2019 ONSC 6127
First National Financial GP Corporation and
Golden Dragon Ho 10 Inc. and Golden Dragon Ho 11 Inc.
COURT FILE NO.: 17-73967
DATE: 20191023

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: First National Financial GP Corporation, Applicant

AND

Golden Dragon Ho 10 Inc. and Gorden Dragon Ho 11 Inc., Respondent

BEFORE: The Honourable Justice C. T. Hackland

COUNSEL: S. Dewart, for First National Financial GP Corporation

D. Preger, for Deloitte Restructuring Inc. Court Appointed Receiver

M. Deigel, for the Respondents

T. Conway and K. Caron for Liahona Mortgage Investment Corp.

K. Perron for Royal United Investments Limited

R. Garrett for Quex Property Corporation

Genevieve Langlais for City of Ottawa Affordable Housing

HEARD: October 11, 2019

ENDORSEMENT

[1] At the conclusion of argument on this motion on October 11, 2019, I granted approval to the court appointed receiver, Deloitte Restructuring Inc. to proceed to close an Agreement of Purchase and Sale ("APS") by which the purchaser Royal United Investments Limited ("Royal United"), is to acquire two properties, 345 and 347 Barber Street, (referred to as "345" or "347"), Ottawa, which are subject to the receivership. I further ordered the receiver or its counsel to hold

in trust out of the net proceeds of sale, the sum of $1.7 million pending the court's further ruling on a disputed prepayment penalty claimed by First National GP Corporation ("F.N.") which holds a first mortgage on both properties,

[2] For reasons outlined below, I have concluded that there must be a trial of an issue with respect to F.N.'s entitlement to payment of this penalty from the proceeds of sale, which I will refer to as "the yield maintenance penalty".

[3] The court appointed receiver recommended that the court approve the APS. I granted approval on the receiver's recommendation and on the basis of my finding that a fair process had been followed, in strict accordance with the court's previous directions and sound business practices, and upon being satisfied by the evidence filed in the Receiver's Seventh Report to the court, that fair market value had been achieved in this sale.

[4] Two parties opposed the sale. F.N.'s opposition had nothing to do with the fairness of the process, nor the sale price, both matters about which they were completely satisfied. Rather, F.N.'s position was that its agreement to have the receiver sell the properties upon motion by Liahona Mortgage Investment Corporation ("Liahona"), which holds a second mortgage on 345, was premised on F.N. receiving payment from the sale proceeds of its yield maintenance penalty. F.N. submits that if it is precluded from receiving the yield maintenance penalty, (about $1.7 million), it wishes in that event, to maintain the mortgage in place until the end of its term (approximately another 8 years) or until such time as the properties are sold by the mortgagors. F.N. points out that the rental income from these two properties is now sufficient to pay the current arrears on the F.N. mortgages and receiver's costs and other charges,, and to return the mortgages to good standing. The proceeds of sale in the proposed transaction are sufficient to pay out the principal

and interest on F.N.'s mortgages and receivership costs, including the yield maintenance penalty. Clearly, the approval of the sale will preclude F.N. from maintaining the mortgage in place, but as noted, the proceeds of sale are sufficient to cover any claim for F.N.'s yield maintenance penalty.

[5] The other objector to the approval of the APS is the mortgagor Golden Dragon Ho 10 Inc. and Golden Dragon Ho 11 Inc., both controlled by Mr. Chi Van Ho. The mortgagor did not file any materials challenging the process or the purchase price. Mr. Ho did file an affidavit making reference to a late offer from a third party that has since been revoked. He also offered the opinion that the properties should have been marketed on the MLS service and further, in his opinion, the per unit (i.e. rental unit) value on this proposed sale is lower than in the sales referenced in the appraisals relied on by CBRE. and the receiver. I do not accept Mr. Ho's opinion that the per unit price achieved is determinative of the adequacy of the sale price in this transaction.

[6] The receiver filed a "Supplemental Report to the Seventh Report of the Receiver" as well as a "Second Supplemental Report", both of which adequately respond to Mr. Ho's concerns. The receiver noted that its agent conducting the marketing and sale of the properties CBRE, "confirmed that when the marketing process was being developed, it did not recommend marketing the Property through MLS because MLS is not a suitable means to attract buyers of multi-residential apartment buildings of a size such as the Property, as qualified buyers for properties over $10 million do not source deals on MLS."

[7] As to the revised late offer referred to by Mr. Ho, among other problematic aspects, it was conditional on the buyer obtaining approval from F.N. and Liahona to their existing mortgages on the property being assumed whereas F.N.'s counsel advised the receiver that F.N. would not consider an application from this purchaser to assume the F.N. mortgage.

[8] In oral submissions Mr. Ho's counsel reiterated his client's concern that the sale price was too low when calculated on a per unit basis, notwithstanding that the overall price for the properties was supported by the appraisals commissioned by the mortgagees.

[9] The receiver advised the court (via its Seventh Report of the Receiver dated September 27, 2019). that the expected allocation of sale proceeds, net of sales commission to CBRE, (the commercial real estate firm retained to handle the marketing and sale of the properties) was approximately $12.8 million of which $10.1 million would be distributed to F.N. This would be sufficient to pay out F.N.'s mortgages, all arrears and receiver's charges as well as the yield maintenance penalty. On this scenario, a further $2.6 million would then be paid out to Liahona, leaving a shortfall on Liahona's second mortgage of approximately $1.2 million. I would observe that F.N.'s distribution would be reduced by approximately $1.7 million in the event the yield maintenance penalty is found to not be payable, in which event this sum would flow to Liahona and the debtors.

[10] In summary, the receiver's recommendation to the court to approve the APS with Royal United is fully justified on the evidence before the court, both in terms of the fairness of the sale process carried out by CBRE under the receiver's direction as well as the sale price and terms achieved. There was no credible evidence to the contrary.

[11] The Court of Appeal in *Royal Bank v Soundair Corp.* 1991 Carswell Ont 205 held that when a receiver has followed a court mandated process to liquidate a security and agreed to a reasonable market price, the efficacy of the court receivership process mandates the transaction being approved. Galligan J.A. stated at para 42 and 43:

> 42. While it is accepted that the primary concern of a receiver is the protecting of the interests of the creditors, there is a secondary but very important consideration, and that is the integrity of the process by which the sale is effected.
>
> 43. The importance of a court protecting the integrity of the process has been stated in a number of cases. First, I refer to *Re Selkirk*, supra, where Saunders J. said at p. 246 [C.B.R.]:
>
> > In dealing with the request for approval, the court has to be concerned primarily with protecting the interest of the creditors of the former bankrupt. A secondary but important consideration is that the process under which the sale agreement is arrived at should be consistent with commercial efficacy and integrity.
> >
> > In that connection I adopt the principles stated by Macdonald J.A. of the Nova Scotia Supreme Court (Appeal Division) in *Cameron v. Bank of N.S.* (1981), 38 C.B.R. (N.S.), where he said at p. 11:
> >
> > > In my opinion if the decision of the receiver to enter into an Agreement of sale, subject to court approval, with respect to certain assets is reasonable and sound under the circumstances at the time existing it should not be set aside simply because a later and higher bid is made. To do so would literally create chaos in the commercial world and receivers and purchasers would never be sure they had a binding agreement. On the contrary, they would know that other bids could be received and considered up until the application for court approval is heard – this would be an intolerable situation.

[12] Counsel for the proposed purchaser Royal United pointed out that her client had expended considerable amounts in the pursuit of this transaction and had successfully negotiated an arrangement with the City of Ottawa and the Government of Ontario to deal with the affordable housing security registered on title, as a grant had originally been received to support the construction of affordable housing units in the building. This security will remain in place and be assumed by Royal United in this transaction. This is to the advantage of all parties. As stated by Galligan J.A. in *Soundair*, "...where a purchaser has bargained at some length and doubtless at considerable expense with the receiver, the interests of the purchaser ought to be taken into

account. … I think (case references omitted) clearly imply that the interests of a person who has negotiated an agreement with a court-appointed receiver are very important."

[13] As noted, I acknowledge that approval of the APS will foreclose F.N.'s option to maintain its mortgages after terminating the receivership. I have given this factor due consideration, but I find off-setting factors carry more weight in the present circumstances, i.e.:

- The sale process, although initiated by Liahona, was agreed to and encouraged by F.N.
- F.N. further supported the sale process by consenting to have the receiver include the 347 property in the sale to maximize the recovery (Liahona has no security on 347).
- F.N., on the evidence, was reluctant to re-establish a relationship with the debtor with whom there had been a litany of disputes and where a clear lack of trust existed. F.N.'s counsel put this reason forward during negotiations between the mortgagees to explain F.N.'s support for selling the properties.
- With or without a sale of the properties, F.N.'s full legal entitlement will be paid out. The issue of the payment of the yield maintenance penalty primarily impacts Liahona's recovery as second mortgagee and the recovery of the debtor.

[14] For all these reasons the APS was approved. I will also approve a distribution order subject to the proviso, noted previously, that the amount of the yield maintenance penalty claimed by F.N. be withheld in trust by the receiver or its counsel from the net proceeds of sale, pending a determination by the court as to whether this penalty or some other compensatory amount is payable to F.N. on this sale.

[15] I will now outline the basis of the dispute which has arisen concerning the yield maintenance penalty. I do so only briefly because I have determined that the trial of an issue is required to properly determine this issue. The questions to be tried can be stated as follows, although counsel may agree to revise my suggested wording:

> 1. Is the yield maintenance penalty (approximately $1.7) due to F.N. on the closing of the court-appointed receiver's sale of the properties herein?
>
> 2. Was there an agreement between F.N. and Liahona that the yield maintenance penalty be payable and if so, should the agreement be enforced by the court and does such agreement bind subsequent creditors or the debtor?
>
> 3. If the yield maintenance penalty is not payable, is F.N. entitled to compensation resulting from the court-appointed receiver's sale of the properties, and if so, on what basis and in what amount?

[16] With respect to the yield maintenance agreement, F.N. contends that the sale herein by the court appointed receiver terminates this closed mortgage which had a remaining term of approximately 8 years. F.N. submits it is entitled to compensation for the lost interest which would have been earned over the balance of the term. This is payable pursuant to the yield maintenance agreement which is part of the mortgage contractual documentation and is also due at common law. F.N. points out that it made its claim for the yield maintenance penalty explicitly clear to Liahona from the commencement of discussions leading to the Expanded Powers Order in May 2019, which authorized the receiver to proceed to market and sell the properties. This order provided that F.N. is deemed not to be realizing on its security by participating in the sale. F.N. then carefully refrained from taking steps itself to realize on its security, so as not to trigger an equity of redemption,. reiterated this claim to the yield maintenance penalty before agreeing with Liahona to instruct the receiver to accept the APS with Royal United and then specifically agreed

with Liahona on the distribution of the proceeds of this sale, which included the payment of the yield maintenance penalty.

[17] Liahona's basic position is that there is no contractual or other legal basis to support F.N.'s claim for the yield maintenance penalty. Further Liahona submits the termination of F.N.'s mortgages will not create a loss to F.N. so far as the evidence on this motion demonstrates because upon payment to F.N. of the full principal and interest due under its mortgages it can mitigate and avoid any loss from the early termination of its mortgage, by lending out its money at current interest rates. Liahona further claims that on a close view of the course of negotiations and communications between Liahona and F.N., Liahona did not specifically address the issue of F.N.'s entitlement to the yield maintenance penalty nor explicitly agree to the inclusion of the penalty in the distribution of the proceeds of sale.

[18] The debtor's counsel maintained in his oral submissions that in substance F.N. must be said to have realized on their security in all the circumstances leading to this sale so that an equity of redemption arises by operation of law and no penalty is payable. Counsel submits that his clients, the debtors, are not bound by any agreements made between the mortgagees without the debtor's explicit concurrence.

[19] The parties have raised serious questions, as set out previously, which require evidence not presently before the court and also raise certain credibility issues.

[20] I request counsel to arrange a case conference before me to agree on a timetable for a trial of the above noted questions pertaining to the claimed yield maintenance penalty and to resolve any ancillary issues.

Hackland J.

Justice Charles T. Hackland

Date: October 23, 2019.

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ENDORSEMENT

Justice C.T. Hackland

Released: October 23, 2019.