

CANADA / JUDGMENT

Aros Investment Ltd.. v. Picchi

2003 BCSC 78

COURT

Supreme Court of British Columbia

DECIDED

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2003BCSC0078

Citation: Aros Invst. v. Picchi et al.

Date: 20030116
2003 BCSC 78Docket: H020661
Registry: Vancouver
IN THE SUPREME COURT OF BRITISH COLUMBIA
RE: PID: 014-376-725
THE WEST ½ OF SECTION 20 TOWNSHIP 17
RANGE 16 WEST OF THE 6TH MERIDIAN
KAMLOOPS DIVISION YALE DISTRICT
IN THE PROVINCE OF BRITISH COLUMBIABETWEEN: AROS INVESTMENT LIMITED
PETITIONERAND: GIOVAN BATTISTA PICCHI also known as
GIANNI PICCHI, SZEGED HOLDINGS LTD. and
ROYAL BANK OF CANADA
RESPONDENTS

REASONS FOR JUDGMENT

OF THE

HONOURABLE MR. JUSTICE CULLEN

(IN CHAMBERS)

Counsel for the Petitioner:

D. Moonje

Counsel for the Respondent Szeged Holdings Ltd.

R.J. Olson

Counsel for the Respondent

Royal Bank of Canada

B.E. Albrecht

Date and Place of Hearing:

November 20, 2002

Vancouver, BC

[1] This application requires consideration of the principles determining the validity of the applicant's, Aros Investments Limited ("Aros"), claim against the respondent Giovan Picchi ("Picchi") for proceeds of the sale of felled timber under a general security agreement and a timber assignment agreement, as against the claims of Szeged Holdings Ltd. ("Sgezed") and the Royal Bank of Canada ("RBC") which arise from writs of seizure and sale executed in accordance with the Court Order Enforcement Act, R.S.B.C. 1996, c. 79.

THE FACTS

[2] On August 9, 1999 Picchi granted a second mortgage to Aros over property legally described as:

PID: 014-376-725

The West ½ of Section 20 Township 17

Range 16 West of the 6th Meridian

Kamloops Division Yale District

("the property") in the amount of \$110,000. The mortgage contained a personal covenant.

[3] The first mortgage was held by Stump Lake Cattle Company Ltd. ("Stump Lake"). Also in August of 1999, Picchi and Aros entered into a general security agreement and a timber assignment agreement to provide further security for the indebtedness.

[4] The effect of the timber assignment agreement was to transfer Picchi's rights to the proceeds of the timber to be harvested on the property to Aros as additional security for the payment of the funds owing under the mortgage granted by Picchi to Aros.

[5] Picchi defaulted on the Aros mortgage and fell into arrears on the Stump Lake mortgage. On March 6, 2002 Aros commenced foreclosure proceedings and on June 4, 2002 was granted an immediate order absolute of foreclosure. None of the respondents resisted the June 4th order. Aros did not bring an action on the personal covenant in the mortgage.

- [6] On June 6, 2002 Szeged filed a writ of seizure of sale arising from default judgment it had obtained against Picchi on November 21, 2000 in the amount of \$77,167.69. On July 9, 2002 RBC filed a writ of seizure and sale arising from judgment it obtained against Picchi on May 9, 2001 in the amount of \$59,866.80. Both judgment creditors caused timber which had been felled and was stacked on the property awaiting sale, to be tagged by the bailiff pursuant to the writs of seizure and sale.
- [7] The total net value of the timber is estimated to be approximately \$86,000. At the time of the hearing before me, some of the timber had been sold and the sum of \$24,000 had been paid into the trust account of Aros' solicitor pending determination of this application. The net value of the remaining timber was estimated to be \$62,000.
- [8] The principal basis on which Szeged and RBC oppose Aros' claim of a right to the felled timber and/or the proceeds from its sale, is found in the provisions of s. 32 of the Property Law Act R.S.B.C. 1996, c. 377. Section 32 reads as follows:

Enforcement of Personal Covenant

32 After the making of an order absolute for foreclosure or for cancellation of an agreement for sale, a mortgagee or vendor

- (a) has no right to enforce the personal covenant of the mortgagor or the purchaser to pay, and
 - (b) may not issue execution on a judgment taken on the covenant to pay unless by process of law the order absolute is set aside or reopened.
- [9] It is the respondents' submission that by obtaining the order absolute on June 4, 2002, the petitioner has lost its right to enforce Picchi's personal covenant through executing against the timber which was felled but not sold prior to June 4, 2002. The respondents submit that the effect of s. 32 is to extinguish any indebtedness between the mortgagor and mortgagee once the order absolute is obtained and thus the mortgagee's right to any collateral or additional security is similarly extinguished. It follows, the respondents submit, that Aros' claim to the felled timber and/or the proceeds of its sale must give way to theirs.
- [10] The respondents rely on the explication of the meaning and effect of the remedy of foreclosure provided by Esson J.A. in *Federal Business Development Bank v. F.J.H. Construction Ltd. et al.* (1988), 48 R.P.R. 194 (B.C.C.A.) at p. 199:

The essence of foreclosure is that the mortgagee takes the property in satisfaction of the debt for which the mortgage is security. The final step in that procedure is the order absolute. Once that order is made, the mortgagee's rights are exhausted but he owns the land free of any obligation to the mortgagor. The essence of sale is that the property is sold with a view to satisfying the mortgage debt out of the proceeds of sale. The final step in that procedure, equivalent to the order absolute, is the vesting of title in the purchaser under court order. That step "forecloses" the mortgagor out of the equity of redemption as effectively as does an order absolute. But in other respects, the consequences as between mortgagor and mortgagee are different. If the

proceeds exceed the amount owing to the mortgagee, he must account for the balance. If the proceeds are inadequate to satisfy the mortgage debt, the mortgagee retains his right to pursue the mortgagor on the personal covenant.

[11] The respondents submit that Aros, having obtained an order absolute of foreclosure in the present case, has exhausted its remedies vis-a-vis the debt secured by its mortgage, and cannot claim against the collateral.

[12] The respondents also rely on *Harbour Way Motel Ltd. v. Westcoast Savings Credit Union* (1986), 3 B.C.L.R. (2d) 161 (C.A.).

[13] In that case the creditor, Westcoast Savings, held security which included a land mortgage and a chattel mortgage and brought foreclosure proceedings on the land mortgage in which it obtained a judgment on the covenant to pay before obtaining an order absolute of foreclosure. On the issue whether the creditor retained any right under the Chattel Mortgage Act, R.S.B.C. 1979, c. 48 to seize goods held as additional security for the same indebtedness, Lambert J.A. for the court ruled that it did not. He noted that the Chattel Mortgage Act proscribed a grantee from enforcing his claim to money due and owing by both taking possession of the chattels and suing the grantor of the debt, and that the creditor's claim for personal judgment on the personal covenant in the land mortgage in that case constituted a suit "against the grantor" for the money due and owing, thus extinguishing the right to seize the chattels under the Chattel Mortgage Act.

[14] Lambert J.A. went on to say as follows, at pp. 164-165:

It could perhaps be argued that the action on the covenant in the land mortgage was based on a different obligation than either the debt itself or the obligation recorded in the chattel mortgage; in short, that there were three separate obligations and that an action for a judgment on one of those obligations did not constitute suing on either of the other two obligations. But that interpretation cannot stand with s. 28 of the Property Law Act, which reads like this:

28. After the making of an order absolute for foreclosure or for cancellation of an agreement for sale, a mortgagee or vendor has no right to enforce the personal covenant of the mortgagor or the purchaser to pay. He may not issue execution on a judgment taken on the covenant to pay unless by process of law the order absolute is set aside or reopened.

If the argument that I have set out were correct, then s. 28 would be rendered ineffective because the obligation recorded in the chattel mortgage and the debt itself would be separate from the personal covenant in the land mortgage and would survive the order absolute. So a creditor could obtain the land and also obtain and enforce a judgment for the debt. That would be contrary to the intention of the enactment.

- [15] The respondents submit Lambert J.A.'s exposition above, is apposite to the case at bar and should govern my disposition of this application. It should be noted that s. 28 referred to by Lambert J.A. in *Harbour Way Motel*, supra, is the predecessor to s. 32 of the Property Law Act.
- [16] Aros' position is that s. 32 does not apply to the facts in the case at bar and points to evidence that the timber which is the subject of this application was sold to Aros prior to the commencement of the foreclosure proceedings, and therefore falls outside of any process engaging s. 32. In the alternative, counsel for Aros submits that even if s. 32 is applicable, its effect is only to extinguish Aros' right to enforce Picchi's personal covenant under the land mortgage and does not preclude it from realizing on the collateral security pursuant to the general security agreement and the timber assignment agreement.
- [17] The evidence that Aros relies on to establish the prior sale of the timber from Picchi to Aros is set out in the affidavit of Picchi, sworn September 9, 2002, the affidavit of Brian Chatfield ("Chatfield"), sworn August 8, 2002, and the third affidavit of Reinhard Behrend ("Behrend"), sworn August 8, 2002. The essence of the evidence relied on by Aros is that an oral agreement was reached between Picchi and Behrend, an officer and director of Aros, which was witnessed by Chatfield, a mortgage broker who arranged the second mortgage financing between Aros and Picchi, that Aros would apply for an order absolute of foreclosure, would either pay out or assume the Stump Lake first mortgage and would take ownership of the timber on the property.
- [18] The circumstances of the agreement are set out in paras. 6-13 of Behrend's third affidavit sworn August 8, 2002, as follows:
6. After Mr. Picchi defaulted, he and I discussed his intentions on several occasions in late 2000. Mr. Picchi advised me that he knew of a party interested in the Property. Mr. Picchi was confident that he could arrange a sale of the Property that would pay out the first and second mortgages. I agreed to give Mr. Picchi until July 2001 to sell the Property.
 7. By the Fall of 2001, Mr. Picchi still had not been able to arrange a sale of the Property. At that point in time, I began to consider the prospect of logging the Timber.
 8. In or about October 2001, I met with Mr. Picchi. The mortgage broker who arranged the financing of the Mortgage, Mr. Brian Chatfield, attended as well. I explained that I was considering logging in January or February 2002. Mr. Picchi was still hopeful he could sell the Property before that time, but agreed that it would be beneficial to commence logging. Mr. Picchi and I agreed that if he sold the Property, any proceeds from any logging would be applied to his indebtedness to Aros under the Mortgage.
 9. In or about early February, 2002, I commissioned an appraisal of the Property. Now shown to me and marked as Exhibit "C" to this my affidavit is a true copy of the appraisal of February 12, 2002 showing a value for the Property at \$192,000. Upon my review of the appraisal, I concluded that Mr. Picchi would be unlikely to obtain a buyer to pay enough to

pay out the first and second mortgages, and that the best option to Aros was to try and take over ownership of the land and the Timber, log and hold on to the Property. I was undecided whether to hold the Property until market conditions changed or to develop the Property.

10. In or about mid-February, I met again with Mr. Picchi at Mr. Chatfield's office. At this time of this meeting, Mr. Picchi's indebtedness under both mortgages was approximately \$325,000. By then, I had discussed with Stump Lake Cattle Company Ltd. ("Stump Lake") Aros making regular payments and bringing the first mortgage up to date.
 11. Mr. Picchi and I discussed the matter. We agreed that Aros would take over ownership of the Timber, and hire a logging contractor. The profits from the logging would belong to Aros. We also discussed the Mortgage. I explained that Aros wanted to apply to the Court to take over ownership of the Property and to assume the first mortgage. I noted that this would release Mr. Picchi of any responsibility under both mortgages. Mr. Picchi agreed that Aros would take over ownership of the Timber and commence logging, and that Aros would apply to Court to take ownership of the Property and assume responsibility for the first mortgage.
 12. A few days later and to allow Aros access to the Property to start logging, Mr. Picchi gave Mr. Chatfield the key to the lock and chain that closed off entry to the Property.
 13. After concluding negotiations with Mr. Picchi for the transfer of ownership in the Timber and his consent to an application by Aros to take over ownership of the Property, I reached an agreement with Stump Lake to bring the first mortgage up to date and make regular payments.
- [19] Both Picchi and Chatfield confirm the existence and nature of the agreement deposed to by Behrend in their respective affidavits.
- [20] On that basis the petitioner submits, s. 32 of the Property Law Act has no application to the timber as title to it had passed to Aros before the order absolute was granted and hence it was not "collateral security" for the mortgage subject to realization under the Personal Property Security Act, R.S.B.C. 1996, c. 359 or pursuant to the timber assignment agreement.
- [21] In the alternative, counsel for Aros submits that, in any event, s. 32 only restricts a mortgagee who has taken an order absolute of foreclosure from proceeding to enforce the personal covenant to pay, it does not proscribe realization of other security in relation to the same debt.
- [22] The applicant relies on *Edmonton Airport Hotel Co. v. Credit Foncier Franco-Canadien*, [1965] S.C.R. 441 (S.C.C.); *Household Finance Corporation of Canada v. Mogck et al.* (1984), 54 B.C.L.R. (1) (S.C.); *Harbour Way Motel Ltd., supra*, *Canim Lake Farms (1969) Ltd. v. Toronto-Dominion Bank* (1987), 47 R.P.R. 78 (B.C.S.C.) and *Guaranty Trust Company of Canada v. Yukon Properties Ltd. et al.* (5 November 1976), Vancouver D40321/75 (B.C.S.C.) in support of its submission on this point. Each of those authorities cited by the applicant touches upon the issue of the effect of obtaining an order absolute of foreclosure in light of various statutory provisions conditioning a mortgagee's entitlement to realize on additional or

collateral security in respect of the mortgage debt.

- [23] In the final alternative, Aros submits, in effect, that the oral agreement between Picchi and Aros altered the contractual relationship such that Aros' right to the timber arose, not from the original mortgage debt, but from its agreement to assume the Stump Lake first mortgage and seek an order absolute of foreclosure foregoing any claim on Picchi's personal covenant.
- [24] Aros submitted further, that in the circumstances Szeged and RBC's tagging of the timber constituted a trespass warranting a nominal award of general damages and, as special damages, the solicitor/client costs associated with asserting its right to the timber.
- [25] The respondent Szeged and RBC questioned the credibility of Aros' assertion of an oral agreement in relation to the timber, pointing to certain inconsistencies in the affidavits of Behrend, Picchi and Chatfield. They also point to the materials filed by Aros in support of its application for an absolute order of foreclosure, in particular, the assertion in Behrend's second affidavit, sworn May 29, 2002 in support of that application, in which he asserts at para. 3 as follows:
3. Neither the Petitioner nor any person who is authorized to receive funds on behalf of the Petitioner, received from the Respondents, or from anyone on their behalf, the amount due to the Petitioner pursuant to the mortgage that is the subject of these proceedings, or any security in satisfaction for the same or any part thereof except the mortgage described in the Petition herein as assigned, and the whole of the said sum remains justly due and owing to the Petitioner under the said Mortgage.
- [26] The respondents also point to the appraisal of the property appended to Behrend's second affidavit which states as follows:

There may be some timber value on the subject site, but this has not been addressed in this report.

- [27] It is the respondents' submission that the effect of Aros' material put before the court to obtain the order absolute of foreclosure is to negate the existence of the oral agreement asserted and has the effect of estopping the petitioner from now claiming differently.
- [28] The respondents further submit that there is no evidence of what, if anything, remains of the debt. It is their submission that in the absence of such evidence, given the granting of the order absolute, to grant the petitioner the order it now seeks would be tantamount to permitting them to seize chattels ad infinitum without regard to the mortgagor's indebtedness or the rights of other creditors.
- [29] Aros points to para. 14 of the third Behrend affidavit sworn August 8, 2002 in answer to the respondents' assertion that they are estopped from asserting that title to the timber was passed. Paragraph 14 reads as follows:

14. In my negotiations with Mr. Picchi, I believed Aros needed his agreement to transfer ownership of the Timber. This way Aros would own the unfelled trees and not just the proceeds, and could then log without any involvement of Mr. Picchi. I would not have decided to log the Timber, reach agreement with the first mortgagee, make payments to the first mortgagee and then apply for order absolute without the agreement of Mr. Picchi that I owned the Timber. Further, if Mr. Picchi had not agreed to transfer ownership of the Timber, then as I had a security interest in the proceeds of any sale of the Timber, I would have included the Timber in the foreclosure proceeding.

[30] In my opinion, it is not possible to reconcile para. 3 of Behrend's May 29, 2002 affidavit with para. 14 above. Whether by estoppel or by deficiency of proof the petitioner's assertion of a prior oral agreement respecting title to the timber fails. That leaves the issue whether Aros can realize on its security interest in the timber notwithstanding the grant of the order absolute of foreclosure on June 4, 2002.

[31] As I read s. 32 of the Property Law Act and the decisions applying it, its predecessor section, s. 28, and related provisions in other jurisdictions, the proscription imposed on a mortgagee who has obtained an order absolute of foreclosure relates to the enforcement of the personal covenant on the land mortgage but does not prohibit realization of additional security granted by the mortgagor to secure the same debt. In *Harbour Way Hotel*, supra, Lambert J.A. in obiter dicta stated at p. 165:

And, of course, even where a land mortgage and a chattel mortgage secure the same debt, enforcement of both instruments may well be possible by bringing an action for foreclosure of the land mortgage, without any action on the covenant, obtaining a realization either by sale or by order absolute, and later seizing under the chattel mortgage.

[32] In that case, as earlier noted, Lambert J.A. determined that the defendant's attempt to realize on the security of a chattel mortgage was defeated by the combined effect of s. 28 of the Property Law Act (the predecessor to s. 32) and s. 23(1) of the Chattel Mortgage Act because of its action on the personal covenant under the land mortgage, but not because of the grant of the order absolute of foreclosure.

[33] Similarly, in *Edmonton Airport Hotel Co. v. Credit Foncier*, supra, the Supreme Court of Canada decided that the Alberta Judicature Act, which precluded an action on the covenant in an action for foreclosure, and provided that the mortgagee's right to recover money under the mortgage ceased on a final vesting order, was not infringed where the creditor sought to enforce its security under a land mortgage, a chattel mortgage and a personal guarantee, because it never sued directly on the debt.

[34] In *Canim Lake Farms (1969) Ltd.*, supra, the defendant was named as a loss payee on a composite insurance policy held by the plaintiff on a barn located in lands not covered in the mortgages held by the defendant. The defendant brought foreclosure proceedings in relating to the mortgages and claimed the proceeds of the insurance when the barn burned down. Relying on the judgment of Lambert J.A. in *Harbour Way Motel*, supra, Robinson

L.J.S.C. (as he then was) concluded that the mortgagee was entitled to the insurance proceeds as collateral security to the mortgage debt despite obtaining an order absolute of foreclosure. Robinson L.J.S.C. noted at p. 82 as follows:

My interpretation of the wording of s. 28 of the Property Law Act ... is that the rights of a mortgagee who has taken order absolute, continue undisturbed where collateral security exists, and such mortgagee may realize that upon such collateral security, where a deficiency is proven to exist following realization by way of order absolute.

- [35] In the case at bar there was no action brought by Aros against Picchi on the personal covenant so as to preclude its realization on collateral or additional security by virtue of s. 32. In my opinion, while taking an order absolute of foreclosure on the mortgage extinguishes Aros' other remedies under the mortgage, it does not preclude it from realizing on other securities to cover deficiencies arising from the debt covered by the mortgage.
- [36] In submissions counsel for the respondents referred to the possibility that permitting a mortgagee to obtain an order absolute of foreclosure and realize on collateral or additional securities, could lead to a situation in which the mortgagee recovered more than what is owed to it without need of an accounting. While I am prepared to make the order sought by the petitioner, Aros, that proceeds of the sale of the felled timber be released to it, I grant liberty to the respondents to apply for any order as to an accounting should they regard it as necessary in the circumstances.
- [37] As mentioned, Aros also sought damages for trespass against Szeged and RBC based on their actions in tagging the timber. Giving my findings with regard to the agreement relating to the prior transfer of title of timber to Aros by Picchi, this portion of Aros' application must fail.

"A.F. Cullen, J."

The Honourable Mr. Justice A.F. Cullen

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