SUPERIOR COURT OF JUSTICE

COUNSEL SLIP

COURT FILE NO.: CV-22-00676573-00CL

DATE: September 21, 2022

NO. ON LIST 3

TITLE OF PROCEEDING

BUSINESS DEVELOPMENT BANK OF CANADA
v.
BAIG INSULATION INC. et al

BEFORE MR. JUSTICE PENNY

COUNSEL FOR:

☒ PLAINTIFF(S)
☐ APPLICANT(S)
☐ PETITIONER(S)

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☒ DEFENDANT(S)
☐ RESPONDENT(S)

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JUDICIAL NOTES:

Reasons for Decision
Released: September 26, 2022

In this motion, the Business Development Bank seeks an order declaring that a debt owed by Mr. Baig to BDC in the principal amount of $97,805.63 (plus interest and costs) is a debt incurred through fraudulent misrepresentations to BDC, a debt within the meaning of s. 178 (1)(e) of the *Bankruptcy and Insolvency Act*, and that the debt shall not be released by Mr. Baig's discharge from bankruptcy.

As I will discuss below, the motion is granted in part.

Background

BDC is an agent of the federal Crown under the *Business Development Bank of Canada Act*.

Baig Insulation Inc. is an Ontario corporation with its registered head office in Milton. Mr. Baig is an individual residing in Milton, Ontario. He is the sole director of Baig Insulation Inc.

Mr. Baig, in spite of having had ample opportunity to do so, filed no evidence on this motion. He did, however, attend the hearing (albeit 45 minutes late) and made brief submissions. His trustee did not appear but indicated to the court in a written communication that it took no position on BDC's motion.

The only evidence before the court is that on February 15, 2017, Mr. Baig submitted a loan application on behalf of Baig Insulation to BDC for the advance of a $100,000 loan. Baig Insulation was represented to be a sole proprietorship. In the loan application, Mr. Baig, on his own behalf and on behalf of Baig Insulation, made the following representations:
(a) Baig Insulation was an operating business which required a loan to be used as working capital and to purchase equipment;
(b) Baig Insulation was operating out of a Mississauga property on Hillcrest Avenue and that Mr. Baig/Baig Insulation owned Hillcrest;
(c) Hillcrest was worth approximately $700,000 and subject to a mortgage in the amount of approximately $450,000;
(e) Mr. Baig's total annual household income was approximately $85,000; and
(f) Mr. Baig had no unsecured personal debts.

By the express terms of the loan application, Mr. Baig and Baig Insulation acknowledged and agreed that by signing the application, "they declare and affirm that all information contained in the … application…are true and correct…" They also acknowledged and agreed that BDC would be using the information provided by them as the basis upon which to decide whether to grant the requested loan.

The loan agreement itself was executed on March 19, 2017. The loan agreement provides that BDC made the loan in reliance on the representations made in the borrowers' application. Mr. Baig unequivocally guaranteed the loan to Baig Insulation. The borrowers also agreed that all the information provided to BDC in the loan application was and remained accurate.

In early 2018, Baig Insulation defaulted on its repayment obligations under the loan. BDC made demand in April 2018. No further payments were made. In May 2018, BDC commenced an action against the borrowers. They failed to defend. In September 2018, the defendants were noted in default. BDC obtained default judgment against both defendants in the principal amount of $97,805.63, plus interest and $1,570 in costs.

On October 9, 2018, Mr. Baig made an assignment into bankruptcy. Later that month, BDC received the supporting documents from Mr. Baig's trustee in bankruptcy. This documentation included Mr. Baig's statement of affairs. Mr. Baig identified, as his first obligation, an unsecured debt owing to BDC of $95,175. Mr. Baig swore in his statement of affairs that:
(a) Baig Insulation had ceased operations on December 1, 2016, over two months before the defendants submitted the loan application to BDC;

(b) Mr. Baig did not own any real property and had not disposed of any real property within the five years preceding his assignment into bankruptcy, notwithstanding his representation in the loan application that he owned Hillcrest which had a net value of about $250,000;
(c) Mr. Baig owed a total of $734,198 in unsecured liabilities, none of which, excluding the BDC loan, was disclosed in the loan application; and
(d) Mr. Baig's annual income was approximately $24,000, rather than the $85,000 represented in the loan application.

Analysis

The Legal Framework

This case began as a civil action on a debt. BDC obtained a default judgment. It was only after that judgment that Mr. Baig filed his proposal. BDC had no knowledge of what it now says were fraudulent misrepresentations made in the loan application until it saw Mr. Baig's statement of affairs. Although there has been a circuitous procedural route leading to this motion, BDC obtained leave of the Registrar to bring the motion prior to Mr. Baig's discharge hearing. McEwen J. approved the transfer of this matter to the Commercial List. My jurisdiction to make the order sought, including the power to make declaratory orders in this matter, arises from s. 183(1) of the BIA.

Section 178(1) of the BIA contains exemptions to the general principle that a bankrupt will be released from his or her debts following discharge from bankruptcy. These exemptions are based on public policy considerations such as s. 178(1)(e), which is designed to protect creditors against fraudulent or deceitful conduct and to ensure that the BIA is not used to reward bankrupts by releasing them from conduct that is unacceptable to society.

Specifically, s. 178(1)(e) of the BIA provides that:

> 178(1) An order of discharge does not release the bankrupt from…
> (e) any debt or liability resulting from obtaining property or services by false pretences or fraudulent misrepresentation, other than a debt or liability that arises from an equity claim.

This debt/liability did not arise from an equity claim.

False pretences or fraudulent misrepresentation requires proof of five requirements:

(a) the defendant made a representation that was false;
(b) the defendant knew the statement was false, or was indifferent to its truth or falsity;
(c) the defendant had the intent to deceive the plaintiff;
(d) the false statement was material and induced the plaintiff to act; and
(e) the plaintiff suffered damages as a result.

A debtor's misrepresentation in a loan application can constitute a fraudulent misrepresentation where the five requirements have been met: see *CMHC v. Hollancid*, 2014 ONSC, at para. 74, affirmed 2015 ONCA 359; *Vanc City Savings Credit Union v. Phelps*, 2006 BCSC 134 at paras. 44-46.

Where a judgment creditor had no prior knowledge of the conduct which engages s. 178(1), the court has the power to determine that a pre-existing judgment or other obligation survives bankruptcy. In *Royal Bank of Canada v. Kim,* 2019 ONSC 798 at para 53, Justice Broad explained the rationale for this as follows:

> In my view, to bar a judgment creditor who had no reasonable means of discovering the fraudulent conduct prior to commencing action or obtaining judgment from continuing pursuit of the fraudulent bankrupt after discharge would have the effect of rewarding the bankrupt for successfully concealing his or her fraud from the creditor.

Application to This Case

The question for resolution on this motion is whether the evidence of representations in the loan documents from February/March 2017, read in light of the subsequent sworn statement of affairs from October 2018, meet the test for a fraudulent misrepresentation.

Two of the statements relied on, it seems to me, can be discounted immediately. BDC asks me to infer from the conflict in the statements about liabilities (zero in the loan documents versus $734,198 in the statement of affairs) and annual income ($85,000 in the loan documents versus $24,000 in the statement of affairs) that the statements in the loan documents were known to be false and made with intent to deceive. The problem with this submission is that 19 months separates the two events. A lot can happen in 19 months. BDC asks that adverse inferences be drawn from the failure of Mr. Baig to explain these discrepancies. However, before an inference can be drawn from failure to adduce evidence on a matter, there must be sufficient evidence to demand an explanation. It cannot be reasonably and logically inferred that, because Mr. Baig swore he had $734,198 in liabilities and a $24,000 annual income in October 2018, he knowingly and with intent to deceive made a false statement in March 2017 when he said that he had no liabilities and a $85,000 annual income.

The issues of whether Baig Insulation was carrying on business at the time of the loan, and the ownership and value of Hillcrest, however, require closer scrutiny because the sworn statement of affairs indicates Baig Insulation, both the sole proprietorship and the corporation, had ceased carrying on business months before the loan application for a loan to Baig Insulation was made and that Mr. Baig has never owned or had equity in Hillcrest or any other real property for at least five years prior to his proposal.

Mr. Baig's statement of affairs indicates that as of May 30, 2016, his insulation business ceased to be a sole proprietorship and that as of December 1, 2016, he had ceased to operate his insulation business through Baig Insulation Inc. The loan application was made in February 2017 and the loan agreement was signed, and funds advanced, in March 2017. By that time,

according to the sworn statement of affairs, Mr. Baig's insulation business was conducted through 10519065 Canada Inc., a corporation not mentioned or identified in the loan documents. However, the inference to be drawn from the statement of affairs is that it was the same business throughout; in other words, Mr. Baig did not cease to operate his insulation business and remained personally on the hook for the indebtedness. While I accept it would have been material for BDC to know, and it should have been informed, that Baig Insulation was no longer a sole proprietorship, I am unable to conclude that what is a very common error among laypeople operating small businesses was made, in this case, with knowledge and intent to deceive.

This leaves the issue of ownership of Hillcrest and its purported equity of $250,000. Given Mr. Baig's sworn statement of affairs, he must be taken to have known that he did not own Hillcrest or have equity in any real property worth $250,000 at the time he made those representations in February/March 2017. Further, although this was not a secured loan, Mr. Baig must be taken to have understood that ownership of real property with equity substantially in excess of the loan amount would be a material factor in BDC's willingness to advance the loan. Thus, it must be inferred, in the absence of countervailing evidence, that Mr. Baig made the representation that he owned real property with equity of $250,000: a) knowing it was false; and, b) for the purpose of leading BDC to believe he had significant assets when he did not – in other words, for the purpose of deceiving BDC about a material fact in order to increase the prospect of getting the loan.

There is uncontradicted evidence that BDC regarded the ownership of real property with significant equity as material, relied on that representation and suffer damages as a result because it advanced funds to Mr. Baig on the basis of this deceit and could not collect when the loan went into default.

As noted earlier, Mr. Baig submitted no evidence. While he is unrepresented, he clearly understands the role and purpose of legal counsel. I say this because his largest single creditor is a law firm which he retained prior to filing his proposal in bankruptcy. Mr. Baig's submission at the hearing was that he did not fill out or sign the loan application to BDC. He says this was done by a friend who acted as his agent, for a 30% fee, in obtaining the BDC loan. Thus, Mr. Baig maintained that the alleged misrepresentations in the loan application were not his misrepresentations but those of his friend and agent. It appeared to be Mr. Baig's position that he should not, as a result of these circumstances, be found to have engaged in deceitful conduct that would bring him within the ambit of s. 178(1)(e).

The first problem with Mr. Baig's submission is that it is not evidence. Not being evidence, BDC has been deprived of the opportunity to refute or cross-examine on it. It would be grossly improper, not to mention unfair, to determine BDC's motion on the basis of unsworn, obviously self interested, submissions, unsupported by any evidence, made for the first time during the hearing.

The second problem with this submission is that, even if it were accepted as true, it is not clear how it would help Mr. Baig in the circumstances. If Mr. Baig's agent made representations on

his behalf, they would be legally binding on him. Mr. Baig received the benefit of the loan – this is not in dispute. Although Mr. Baig claims he did not sign the loan application, he agreed that he probably signed the loan agreement itself. The loan agreement incorporates the representations in the loan application by reference. Even if Mr. Baig did not personally make the false representations that he own Hillcrest and had $250,000 in equity, it was his responsibility to ensure that all representations made on his behalf were accurate. Thus, even if Mr. Baig was unaware of the false statements made in the loan application (although even his submission did not go this far), it was an obvious or serious risk to allow someone else to submit a loan application on his behalf without ensuring the application was true and correct in all material respects. By failing to do so, Mr. Baig knowingly and consciously put his head in the sand and declined to make inquiries because he did not care to know, or was reckless about, the contents of his application to BDC for the loan.

Thus, on the issue of the false statement about ownership of Hillhurst and its associated net equity, I find that Mr. Baig knowingly made false representations with intent to deceive, or that he recklessly ignored whether the representations were true, in order to derive the benefit of the loan.

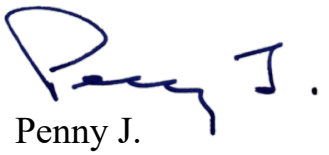
There is a claim for ongoing interest and full indemnity costs. I find that the application of s. 178(1)(e) is limited to the amount of the indebtedness as of October 9, 2018. Accruing interest and any enforcement costs incurred after October 9, 2018, are not subject to the application of s. 178(1)(e).

Conclusion

In conclusion, the declaration is granted in part. I declare that the debt owing by Mr. Baig to BDC as of October 9, 2018, was incurred on the basis of a fraudulent misrepresentation such that the obligation owed by Mr. Baig to BDC as of October 9, 2018 survives bankruptcy under s. 178(1)(e). Any amounts accruing under the loan agreement after that time are not subject to the s. 178(1)(e) exception.

Costs

Subject to the proviso above, BDC is entitled to costs of the motion on a partial indemnity basis in the amount of $9,000.



Penny J.