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COURT	COURT OF QUEEN'S BENCH OF ALBERTA
JUDICIAL CENTRE	CALGARY
PLAINTIFF	HSBC BANK CANADA
DEFENDANTS	PAINTEARTH ENERGY SERVICES INC., PAINTEARTH ENERGY SERVICES LTD., and PES SUBSURFACE CANADA INC.

AND IN THE MATTER OF THE RECEIVERSHIP OF
PAINTEARTH ENERGY SERVICES INC.,
PAINTEARTH ENERGY SERVICES LTD., and
PES SUBSURFACE CANADA INC.

THIRD RERORT OF THE RECEIVER

February 26, 2013

ADDRESS FOR SERVICE AND CONTACT INFORMATION OF PARTY FILING THIS DOCUMENT

RECEIVER

Ernst & Young Inc.
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INTRODUCTION

1. Ernst & Young Inc. was appointed as interim receiver of the assets, undertakings and properties of every nature and kind (the "Property") of Paintearth Energy Services Inc., Paintearth Energy Services Ltd., and PES Subsurface Canada Inc. (collectively "Paintearth" or the "Company") on September 27, 2010, pursuant to the Order of the Honourable Justice G.E.C. Hawco of Court of Queen's Bench of Alberta, Judicial Centre of Calgary (the "Court").

2. On October 27, 2010, Ernst & Young Inc. was appointed receiver and manager (the "Receiver") of Paintearth pursuant to a further Order of the Court (the "Appointment Order").

3. The Appointment Order authorized the Receiver, among other things, to carry on the business of the Company and to solicit offers to purchase the Property of the Company, subject to the approval of the Court for transactions in excess of $500,000.

4. On December 20, 2010, the Receiver sought and obtained from the Court the approval of a purchase and sale agreement for substantially all the assets of Paintearth, pursuant to a purchase and sale agreement between the Receiver and Oil Lift Technology Inc. in the amount of approximately $2.608 million subject to certain post-closing adjustments.

5. The purpose of this third report (the "Third Report") of the Receiver is to provide the Court with:

   a) The proposed distribution to HSBC Bank Canada ("HSBC");

   b) The Receiver's consolidated final statement of receipts and disbursements;

   c) The fees and disbursements of the Receiver and its counsel; and

   d) The discharge of Ernst & Young Inc. as Receiver of the Property.

6. Capitalized terms not defined in this Third Report are as defined in the Appointment Order. All references to dollars are in Canadian currency.

BACKGROUND

7. Paintearth was an oilfield services company that operated in the United States ("US") and Canada through Paintearth Energy Services Inc. ("Paintearth Corporate") and its subsidiaries Paintearth Energy Services Ltd. ("Paintearth US") and PES Subsurface Canada ("Paintearth Canada").

8. The Company was headquartered at their Canadian location in Calgary, Alberta, with sales and stocking points in Edmonton and Lloydminster, Alberta. In addition, the Company operated in the United States through a main location in Victoria, Texas with sales and stocking points in Odessa, Texas and Oklahoma City, Oklahoma. The premises at all locations were subject to third party leases.

9. Paintearth had two main operating divisions, one division with respect to the manufacturing and selling of subsurface tools and a second division with respect to the provision of protective coating services on downhole tool products. The subsurface tools division was focused primarily on the distribution and manufacturing of an array of downhole tool products, including artificial lift tools, completion tools and flow control tools. The protective coating division was focused on the boronizing process of steel coating.

TERMS OF REFERENCE

10. In preparing this Third Report, the Receiver has relied upon unaudited financial information and company records of the Company. The Receiver has not performed an audit, review or other verification of such information.

PROPOSED FINAL DISTRIBUTION TO HSBC

11. Upon investigation into the Contested Flint Funds (as defined in the Receiver's Second Report which is attached as Exhibit A to the Affidavit of Neil Narfason (the "Narfason Affidavit") sworn May 20, 2011) and based on the Receiver's legal advice regarding the priority to the Contested Flint Funds, the Receiver is proposing to distribute all remaining funds in the Paintearth estate to HSBC.

12. As shown below, the Receiver currently holds $379,484 in funds and there are no remaining assets other than that cash in the Paintearth estate.

13. As set out in the Narfason Affidavit, the Receiver has obtained an independent security review of the HSBC security documents from its Canadian counsel indicating that, subject to the usual and customary qualifications, the security granted by Paintearth to HSBC constitutes a valid and enforceable first charge security interest in the present and future acquired assets, property and undertaking of Paintearth.

14. The Receiver has also consulted with its independent US legal counsel with respect to whether there are any creditors which would rank in priority to HSBC over Paintearth. The Receiver's independent US legal counsel has advised that, subject to the usual and customary qualifications, there are no US creditors which would rank in priority to HSBC.

15. In addition, the Receiver obtained independent legal advice as to the priority over the Contested Flint Funds which concluded that HSBC has the better argument with respect to the priority to these funds. The Receiver's independent legal advice and written opinion was shared with both HSBC and Flint well in advance of this Third Report. The legal opinion is attached as Appendix "A" to this Third Report.

16. The Receiver proposes a final distribution to HSBC for all remaining funds within the Receivership (the "HSBC Distribution"). In addition, the Receiver, as discussed further below, anticipates the payment of one remaining accounts receivable balance over the course of the next eight months. The Receiver proposes to distribute these receivables as collected to HSBC. HSBC is owed in excess of $1 million; therefore, there will not be any recovery to Paintearth's remaining creditors.

STATEMENT OF RECEIPTS AND DISBURSEMENTS

17. A final statement of receipts and disbursements, including the Final HSBC Distribution, from September 27, 2010 to February 26, 2013 (the "Reporting Period") is attached as Appendix "B" to this Third Report.

18. The following is a description of the major components of the above Statement of Receipts and Disbursements:

a) Collection of accounts receivable and realization on other assets relates to the collection of accounts receivable both in existence at the date of the Appointment Order as well as accounts receivable generated by limited production runs completed by the Receiver. The Receiver anticipates total accounts receivable of approximately $32,000 to be recovered in monthly instalments for the next eight months from a customer located in India. As these amounts are collected, the Receiver would pass them on to HSBC as collected. The Receiver has exhausted all efforts to collect any further outstanding accounts receivable and has concluded that, aside from the approximate $32,000, no further accounts receivable collection is expected;

b) Sale of Paintearth assets relates to the gross proceeds received pursuant to the Oil Lift PSA;

c) Initial cash on hand relates to the cash on hand of Paintearth as at the date of the Appointment Order;

d) An initial distribution was paid to HSBC in May 2011;

e) Employee payroll and related costs relates to salaries, wages and employment expenses for employees as well as the costs of independent contractors retained by the Receiver to facilitate the operation of Paintearth to maintain operations until the sale to Oil Lift could be concluded;

f) Rent and property taxes paid relate to the amounts paid on the various leased locations throughout the US (Victoria, Texas, Odessa, Texas and Oklahoma City, Oklahoma) and Canada (Calgary, Alberta, and Lloydminster, Alberta);

g) Operating expenses relate to payments required to facilitate the operations until the sale to Oil Lift could be consummated as well as to complete limited production runs to protect the value of accounts receivable. The material payments made by the Receiver are as follows:

i. Approximately $13,000 related to payments under various license agreements;

ii. Approximately $12,000 related to the acquisition of materials;

iii. Approximately $11,000 related to payments on various leased assets required for partial periods; and

iv. Approximately $8,000 for various freight, storage and repair and maintenance related charges; and

h) The Receiver's fees and disbursements relate primarily to the cost of managing and operating the business which included time spent in each location with staff, conducting inventory and asset verification procedures, conducting the fulsome sales process, dealing with the multitude of landlord related issues, transitioning the business to Oil Lift as well as collection procedures on the outstanding accounts receivables. The Receiver has accrued for estimated fees and disbursements, including storage and destruction of records, to complete the administration of this estate.

19. The total receipts collected and disbursements incurred during the Reporting Period of $5,380,825 and $5,013,257, respectively, result in $367,568 available as the HSBC Distribution.

APPROVAL OF THE FEES AND EXPENDITURES OF THE RECEIVER AND ITS COUNSEL

33. The following table shows the calculation of the fees of the Receiver and its counsel incurred and paid to February 26, 2013 including the estimated fees that are forecasted to be incurred by the Receiver and its counsel with respect to completing the proceedings:

	Fees Incurred	WIP and Costs to Complete	Total Fees
Receiver	$456,227	$ 5,000	$461,227
Receiver's counsel	75,155	15,000	90,155
	$531,382	$ 20,000	$551,382

34. Estimated unbilled fees and costs to complete are $5,000 for the Receiver and $15,000 for its counsel.

35. Copies of the invoices will be available to the Court at the hearing of the Application for the discharge of the Receiver, if requested.

RECEIVER'S DISCHARGE

36. In the event that this Court approves the HSBÇ Distribution, the Receiver's administration of the estate, upon closing, will essentially be complete. The Receiver may have some miscellaneous administrative items to attend to post-discharge, such as the collection of the remaining accounts receivable, but these items are immaterial and, in the Receiver's opinion, should not prevent this Honourable Court from granting an unconditional discharge effective upon the HSBC Distribution.

37. The Receiver respectfully requests that this Honourable Court approve an Order approving the HSBC Distribution and unconditionally discharging the Receiver from any and all obligations as Receiver of Paintearth effective upon the HSBC Distribution.

RECOMMENDATIONS

20. The Receiver recommends that this Honourable Court approve:

a) The HSBC Distribution;

b) The accounts of the fees and disbursements of the Receiver and the Receiver's counsel; and

c) The discharge of Ernst & Young Inc. as Receiver of Paintearth.

All of which is respectfully submitted the 26th of February, 2013.

ERNST & YOUNG INC.

in its capacity as Court Appointed Receiver of
Paintearth Energy Services Inc., Paintearth Energy Services Ltd.,
PES Subsurface Canada Inc. and not in its personal capacity.

Neil Narfason, CA•CIRP, CBV
Senior Vice-President

Cassie Riglin, CA
Manager

APPENDIX A

Memorandum

NORTON ROSE

To:	Ernst & Young Inc.	January 10, 2013
From:	Norton Rose Canada LLP	Our Ref: 01128610-0039

Trust Claims by Flint Energy Services Ltd. against Paintearth Energy Services Inc.

1) Facts and Assumptions

Flint Energy Services Ltd. ("**Flint**") purchased all of the issued and outstanding shares of PES Surface Inc. ("**PES**") from Paintearth Energy Services Ltd. ("**Paintearth**") in March of 2010 (the "**Acquisition**"). The Acquisition was documented by way of a Share Purchase Agreement executed between the parties (the "**Agreement**"). In September of 2010, Ernst & Young Inc. was appointed interim receiver of Paintearth, and in October of 2010 it was appointed receiver ("**Receiver**"). We act for the Receiver.

Pursuant to the Agreement, Paintearth made the following representations and warranties concerning PES's assets:

> **1.1 Definitions**
>
> [...]
>
> (p) "Corporation's Assets" means all of the assets, properties and rights of the Corporation and the Vendor (in relation to the Business);
>
> [...]
>
> **3.2 Representations and Warranties of the Vendor and the Corporation**
>
> [...]
>
> *Assets*
>
> (ff) as at the Closing Date the Corporation shall be the beneficial and (where its interests are registrable) the registered owner of the Corporation's Assets, with good and valid title, free and clear of all Encumbrances other than Permitted Encumbrances. In particular, without limiting the generality of the foregoing, there has been no assignment, subletting, or granting of any license (of occupation or otherwise) of or in respect of the assets of the Corporation or any granting of any agreement or right capable of becoming an agreement or option for the purchase of any of the assets of the Corporation;
>
> [...]
>
> (ii) the accounts receivable of the Corporation and the Vendor (in relation to the Business), in all material respects, are good and collectible at the aggregate recorded amounts, except to the extent of any reserves provided for such accounts in the Books and Records, and are not subject to any defence, counterclaim or set-off;

Section 4.4 of the Agreement established a "transition period" whereby PES was permitted to use Paintearth's Calgary office and shop space to conduct PES business for a period of six months subsequent to the

Acquisition. Paintearth further agreed to maintain, and administer the payroll for, certain employees during the transition period.

Flint and PES assert that the parties further agreed that Paintearth would assist in providing other management services to PES, including management of PES's accounts payable and accounts receivable.

Prior to the Acquisition, Paintearth maintained an HSBC account held in the name of PES (the "**PES Account**"). Subsequent to the Acquisition, Paintearth continued to use the PES Account for its own purposes, which included making electronic payroll remittances. Paintearth also deposited certain cheques made payable to PES into the PES Account, presumably in the course of providing management services to PES. Periodic transfers were made to and from Flint from the PES Account.

At all times, Paintearth also maintained a general HSBC bank account in the name of Paintearth (the "**Paintearth Account**"). Flint and PES assert that, on certain occasions, customers of both Paintearth and PES issued cheques payable to Paintearth for services that had actually been rendered by PES. Paintearth deposited these cheques into the Paintearth Account.

Flint and PES assert that, subsequent to the Acquisition, Paintearth was required to segregate funds collected by Paintearth relating to PES's accounts receivable (the "**Funds**"). Flint and PES further assert that PES has a trust claim over the Funds.

2) Issues

a) *Are the Funds impressed with a trust in favour of PES?*

b) *If the Funds are impressed with a trust in favour of PES, what is the effect of the commingling of the Funds with other monies belonging to Paintearth?*

3) Conclusions and Analysis

a) *Whether or not the Funds are impressed with a trust in favour of PES is highly dependent on the facts of the case. The court will not impress a trust upon the Funds if it can be established that the relationship between Paintearth and PES was that of a debtor and creditor rather than a trustee and beneficiary. Several factors indicate in this case indicate that the relationship was that of a debtor and creditor: no intention to create a trust was expressed in the Agreement, nor can such an intention be implied; PES did not impose any requirements as to the segregation or management of the Funds in the hands of Paintearth; PES was aware, or should have been aware, of Paintearth's other secured creditors and conducted itself accordingly; and the arrangement by which the Funds, or a portion of the Funds, was to go from Paintearth to PES was something more than a merely "flow-though" transaction. On the basis of the facts as they are presently known, the better view is that the Funds are not impressed with a trust.*

There are three types of trusts that are relevant to the current matter: "express" trusts, "implied" trusts, and "constructive" trusts. Generally speaking, an express trust arises when the party or parties involved clearly state that specific property is to be held in trust.[1] An implied trust arises when the party or parties do not expressly create a trust, but the language used between them demonstrates an intention to create a trust.[2] A constructive trust is generally imposed by the court as a remedy, whereby trust machinery is employed to describe one party's obligation to transfer specific property to another.[3]

[1] Donovan W.M. Waters, *Waters' Law of Trusts in Canada* (Toronto: Carswell, 2012) ["**Waters**"] at p 20.
[2] Waters at p 20.
[3] Waters at p 23.

A constructive trust can be imposed in cases of "unjust enrichment" or where "good conscience" otherwise dictates (i.e. where there has been some sort of wrongful conduct on the part of the trustee).[4] Three elements must be present in order to establish a constructive trust on the basis of unjust enrichment:[5]

(1) The enrichment of the defendant;

(2) The corresponding deprivation of the plaintiff; and

(3) The absence of a juristic reason for the enrichment.

Four conditions should generally be satisfied in order to establish a constructive trust on the basis of wrongful conduct:[6]

(1) The defendant must have been under an equitable obligation, that is, an obligation of the type that courts of equity have enforced, in relation to the activities giving rise to the assets in his hands;

(2) The assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant in breach of his equitable obligation to the plaintiff;

(3) The plaintiff must show a legitimate reason for seeking a proprietary remedy, either personal or related to the need to ensure that others like the defendant remain faithful to their duties and;

(4) There must be no factors which would render imposition of a constructive trust unjust in all the circumstances of the case; e.g., the interests of intervening creditors must be protected.

In the present case, the Agreement does not contain express language establishing a trust over accounts receivable, nor has other documentation been provided establishing an express trust.

In the absence of clear language establishing a trust, the court will focus on the relationship between the parties. The characterization of the relationship between the parties -- as either one of trustee and beneficiary or debtor and creditor -- is central to the court's analysis in imposing an implied or constructive trust.

In the case law involving trust claims over accounts receivable, many of the same concepts arise whether the court conducts its analysis on the basis of an implied trust or a constructive trust. In some cases, the court does not engage in a constructive trust analysis at all, possibly because the same subject matter is covered in its implied trust analysis (***General Publishing; Water Street***). As such, the most helpful way to proceed is by examining the relevant factors common to implied trusts and constructive trusts, rather than attempting to examine the two types of trusts independently.

The Agreement does provide that, upon closing, PES shall be the "beneficial and (where its interests are registrable) the registered owner of the Corporation's Assets". This language may provide some weak support for the interpretation that there was an intention to create an implied trust over accounts receivable. However, it is also significant that the term "beneficial interest" is not employed in section of the Agreement dealing specifically with accounts receivable.

Another important, and frequently cited, factor in characterizing the relationship between the parties is the presence or absence of a requirement that the alleged trustee keep trust funds separate from the trustee's general funds. In the 1935 Supreme Court of Canada decision of ***Hanna***, citing the 1913 King's Bench decision of ***Henry***, the Court endorsed the view that demanding the segregation of funds had the effect of impressing the funds with a trust, while allowing funds to be commingled merely created a debt. In ***Air Canada***, the Supreme

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[4] Waters at p 23.
[5] *Soulos v Korkontzilas*, [1997] 2 SCR 217 (per McLachlin J) ["***Soulos***"] at para 20.
[6] *Solous* at para 45.

Court of Canada tempered this view by observing that while commingling was "a factor to be considered" it was "not necessarily determinative".

Despite ***Air Canada***, subsequent courts have treated commingling as a very significant, if not determinative, factor with respect to characterizing the relationship between the parties. In both ***General Publishing***, a decision of the Ontario Court of Appeal, and ***Water Street***, a decision of the British Columbia Court of Appeal (both of which cited ***Hanna*** and ***Henry***, but not ***Air Canada***), the Courts concluded that the absence of any restrictions on how the alleged trustee could use trust funds demonstrated that the parties did not wish to burden themselves with setting up and administering a trust.

In the present case, the Agreement does not contain express language requiring Paintearth to segregate the Funds, nor has other documentation been provided establishing such a requirement. It might be argued that PES did not care to impose a requirement on Paintearth to segregate the Funds, and that PES was content that it would eventually be paid an equivalent amount at a latter date. PES only began to contemplate a trust, or trust-like relationship, when it realized that it might not get paid in priority to other creditors.

Another important factor in characterizing the relationship between the parties is the relationships that the trustee and beneficiary had with other creditors (often discussed under the third point of the constructive trust analysis for unjust enrichment, or under the fourth point of the constructive trust analysis for wrongful conduct).

In ***Orr & Co***, the Court emphasized that the alleged beneficiary, a sophisticated party, at least "ought to have known" that another creditor had a general security interest. As such, the beneficiary should have negotiated a subordination agreement with the other creditor, and failed to do so at its own peril.

In ***Citizens Bank***, the Court emphasized that there had been no "clear breach" of the agreement between the alleged trustee and beneficiary, and as such the prior security of the bank operated as a juristic reason for the beneficiary's deprivation and the bank's enrichment. The Court implied that the result may have been different had the trustee acted unfairly towards, or in breach of the agreement with, the beneficiary.

In ***NRS Mississauga***, although the Court ultimately declined to impose a constructive trust, it downplayed the importance of the parties' relationship with other creditors. The Court emphasized that the alleged beneficiary was not an "ordinary creditor" in the sense that it did not accept the risks of the trustee's business failure, that the bank could not have expected to be enriched through the misallocation of trust funds, and that the bank had other security in the form of guarantees that it could realize upon. Notably, however, ***NRS Mississauga*** involved breach of an express trust, which may mean that it is still compatible with the reasoning in ***Citizens Bank*** (that a trust relationship may be denied if there has been no "clear breach" or other wrongful conduct).

In the present case, it might be argued that, as sophisticated parties, Flint and PES had an obligation to take steps to secure their position vis-à-vis other legitimate creditors. In the absence of any "clear breach" of the Agreement, Flint and PES cannot succeed in a trust claim to the prejudice of other such creditors.

Yet another important factor in characterizing the relationship between the alleged trustee and beneficiary is the nature of the "working" relationship between the parties.

Of the cases reviewed in which the court declined to find a trust relationship, ***General Publishing***, ***Citizens Bank***, and ***Water Street*** all involved distribution agreements, while ***Orr & Co.*** involved a contingency fee agreement. Of the cases reviewed in which the Court did find a trust relationship, ***NRS Mississauga*** and ***Air Canada*** involved express trusts, while ***Brown & Collett*** involved a joint bidding and accounting arrangement.

The facts of ***Brown & Collett*** are particularly significant. In that case, the agreement between the alleged trustee and beneficiary provided for little more than the flow-through of funds from the payor, to the trustee, and finally to the beneficiary. The trustee dishonestly held funds beyond the agreed remittance period, inventing various excuses for the delay. The Court concluded that these facts were sufficient to impose a constructive trust, even in the absence of any intention to create a trust, in the absence of any conditions imposed with respect to the commingling of funds, and in the absence of any conditions imposed with respect the management of the funds.

On the basis of ***Brown & Collett,*** it would seem that the more a relationship resembles a situation where the alleged trustee mistakenly or gratuitously holds funds on behalf of the alleged beneficiary, and the less the relationship resembles a management-type relationship (or at least a mutually beneficial relationship), the more likely a court will be to find a trust relationship. In other words, where funds are intended to merely flow through the trustee, and that process is inhibited without good reason, the court may be reluctant to prejudice a beneficiary to the advantage of other creditors.

In the present case, although highly dependent upon further facts, it might be argued that management of the Funds was complicated by the very close working relationship between the parties, that Paintearth was entitled to a portion of the Funds or to (at least) set-off certain amounts from the Funds, or that Paintearth did not unfairly delay the payment arrangements agreed to by the parties.

b) If the Funds are impressed with a trust in favour of PES, then PES will have a priority claim over the "lowest intermediate balance" in both the PES Account and the Paintearth Account.

Commingling funds is not only relevant to the *existence* of a trust, as discussed above, but also to the amount that can be *recovered* from a mixed account by a beneficiary.

As summarized in ***Vanquish***, if the Funds are indeed found to be impressed with a trust, then they will become trust funds as they are deposited into the PES Account and the Paintearth Account. New Funds received into the Accounts will increase the amount of trust funds contained in the Accounts, as will the addition of other such trust funds.

If monies are removed from the Accounts for non-trust purposes, to the point where the total balance in the Accounts falls below the total trust funds that have been paid into the Accounts (the "lowest intermediate balance"), and the Accounts are not replaced with further funds specifically intended to replenish the dissipated trust funds, then the addition of general funds to the Accounts will not have the effect of increasing the trust fund balance. In other words, PES is only entitled to priority over the lowest intermediate balance of trust funds contained in the Accounts.

The only difference between the PES Account and the Paintearth Account is that it may be easier for PES to argue that Paintearth "intended" to replenish trust funds in the PES Account, owing to the fact that, at certain times, the PES Account may have been dedicated to PES business.

4) Case Law: Imposing a Trust Over Accounts Receivable

a) Air Canada

In *Air Canada v M & L Travel Ltd.,*[7] the defendant travel agency entered into an agreement with Air Canada authorizing the agency to issue Air Canada tickets directly to the public. The agreement expressly stipulated that the agency was required to hold any money collected from the sale of Air Canada tickets in trust and that the agency was required to pay Air Canada twice a month. Trust accounts were set up by the agency, but they were never used. Money received from the sale of airline tickets was deposited into the agency's general operating account.

Air Canada sued the agency, and the directors personally, for amounts owing for Air Canada ticket sales. Iacobucci J's decision is usually cited for its discussion of "knowing receipt" and "knowing assistance", which are doctrines that can impose liability upon a "stranger" to trust (in that case, the directors of the agency). However, Iacobucci J also provided a detailed discussion of the effect of commingling of funds on the creation of a trust. Iacobucci J cited authority on both sides of the matter, most notably *M.A. Hanna Co. v Provincial Bank of*

[7] *Air Canada v M & L Travel Ltd.,* [1993] 3 SCR 787 (per Iacobucci J) ["***Air Canada***"].

Canada[8] and *Henry v Hammond*.[9] Iacobucci J ultimately concluded that a commingling of funds is simply one of many indicia of the presence or absence of a trust relationship:

> 25 While the presence or absence of a prohibition on the commingling of funds is a factor to be considered in favour of a debt relationship, it is not necessarily determinative. See *Lowden v. R.* (1981), 27 A.R. 91 (C.A.), at pp. 101-102; *Bank of Nova Scotia v. Société General (Canada)*, [1984] 4 W.W.R. 232 (Alta. C.A.), at p. 238; *McEachren v. Royal Bank* (1990), 78 Alta. L.R. (2d) 158 (Q.B.), at p. 183; *Stephens Travel Service International Pty. Ltd. (Receivers & Managers Appointed) v. Qantas Airways Ltd.* (1988), 13 N.S.W.L.R. 331 (C.A.) [hereinafter "*Qantas*"], at p. 341. In *Lowden, supra*, McGillivray C.J.A. stated as follows at pp. 101-102:
>
> [...]
>
> 26 The appellant relied on the decision of this Court in *M.A. Hanna Co. v. Provincial Bank of Canada*, [1935] S.C.R. 144. In that case, the Court dealt with the relationship between a supplier of coal and its sales agent. The Court concluded that the relationship was one of debtor-creditor, citing the fact that the parties had specifically cancelled a portion of their agreement requiring the separation of the funds collected by the sales agent. The sales agent paid the supplier by cheques drawn on its general account. The supplier's acquiescence to this practice, and the fact that the agent had use of the funds before payment came due, indicated to this Court that the parties viewed their relationship as one of debtor-creditor. The Court relied on the following passage from *Henry v. Hammond*, [1913] 2 K.B. 515, at p. 521:
>
>> It is clear that if the terms upon which the person receives the money are that he is bound to keep it separate either in a bank or elsewhere, and to hand that money so kept as a separate fund to the person entitled to it, then he is a trustee of that money and must hand it over to the person who is his cestui que trust. If on the other hand he is not bound to keep the money separate, but is entitled to mix it with his own money and deal with it as he pleases, and when called upon to hand over an equivalent sum of money, then, in my opinion, he is not a trustee of the money, but merely a debtor.
>
> [...]
>
> 31 In conclusion, it is well established that the nature of the relationship between the parties is a matter of intention. In the present case, the relationship of trust is further evidenced by the express prohibition restricting the use of the funds, and the supervision and control of the carrier over the financial dealings of M & L. Since there is clear evidence of intention to create a trust in the agreement between M & L and the respondent airline, the absence of a prohibition on the commingling of funds is not determinative, although it may be a factor to be taken into account by the trial judge, as it was here. Moreover, in the present case M & L acted in accordance with that intention and set up trust accounts, which, although never used, confirm that the relationship was viewed by the directors as a trust relationship. Finally, it must be noted that the nature of the relationship is consistent with trust as the IATA agreement allowed M & L to affect Air Canada's legal responsibilities.

b) Orr & Co.

In *Orr & Co. v Saskatchewan Economic Development Corp.*[10], a company called Rendamax took a loan from the respondent, Sedco. Sedco registered a general security interest. The applicants, Orr & Co., were retained by Rendamax to audit its financial statements. Orr & Co. identified certain work performed by Rendamax that might qualify for a tax credit. Rendamax orally agreed to an assignment of the tax credit to Orr & Co. to the extent

[8] *M.A. Hanna Co. v Provincial Bank of Canada*, [1935] SCR 144 ["***Hanna***"].
[9] *Henry v Hammond*, [1913] 2 KB 515 ["***Henry***"].
[10] *Orr & Co. v Saskatchewan Economic Development Corp.*, 24 CBR (3d) 196 (1994 SKQB per McLellan J) ["***Orr & Co.***"], aff'd *Orr & Co. v Saskatchewan Economic Development Corp.*, 125 Sask R 80 (1994 SKCA).

necessary to pay Orr & Co.'s account. A receiver was appointed for Rendamax. After the receiver was appointed, Rendamax reduced the assignment of the tax credit to writing. The proceeds of a substantial tax credit were ultimately paid to the receiver. Orr & Co. brought an application, *inter alia*, for a declaration that the tax credit was impressed with a constructive trust to the extent necessary to pay their account.

McLellan J concluded that a constructive trust did not attach and that Sedco had priority over the proceeds of the tax credit:

> 28 [...] Sedco advanced substantial amounts of money to Rendamax to undertake the operations which gave rise to the tax credit. Without the financing from Sedco the investments would not have been made. In my view, it would not be an unjust enrichment if those tax credit monies are paid to it. Nor am I prepared to accept the applicants' argument that:
>
> > (a) the investment tax credit was not contemplated as part of the security of Sedco; and
> >
> > (b) but for the services provided by the applicants, Sedco would not have received any portion of the investment tax credit.
>
> 29 A secured creditor is not required to identify the collateral that is included in the description "all the present and after-acquired property". It is possible to ascertain all of the present property of its debtor but there is no way the parties can predict what property will be acquired by the debtor in the future. That is precisely why the PPSA authorizes the parties to use "a statement that a security interest is taken in all of the debtor's present and after-acquired property".
>
> 30 It is entirely speculative to say that Sedco would not have retained the services of accountants with similar expertise as that of the applicants and that such accountants would not have discovered the entitlement to the tax credit.
>
> 31 In addition, the applicants knew that Sedco had provided financing to Rendamax. If they did not know that Sedco had a security interest in all of Rendamax's present and after-acquired property they at least ought to have known.
>
> 32 The applicants could have approached Sedco before they undertook the work, to request a subordination agreement from Sedco as to a portion of the tax credit in an amount sufficient to cover their fees and disbursements. It is difficult to imagine that Sedco would not have agreed to such a subordination. It had nothing to lose. If somebody had not performed the work required to apply for the tax credit, its debtor Rendamax would not have received anything from Revenue Canada. The applicants have only themselves to blame for the dilemma which they now face. There is no merit to their suggestion that I apply a constructive trust to defeat the security interest of Sedco.

c) *Brown & Collett*

In *Brown & Collett Ltd., Re,*[11] the parties to the application were stationary suppliers. The respondent, Brown & Collett, had undergone a CCAA restructuring. A plan of compromise and arrangement had been approved by Brown & Collett's creditors. The plaintiff, Hay, made a trust claim against Brown & Collett. Trust claims were not compromised by the plan. The other facts of the case were helpfully set out by Winkler J:

> 32 The facts may be summarised as follows. Brown & Collett and Hay entered into an oral agreement to jointly supply Ford; Brown & Collett to supply the Oakville location and Hay to supply Windsor and Talbotville. Neither supplier would invoice for goods shipped. Each would service its designated locations and ship from its own inventory. They agreed between

[11] *Brown & Collett Ltd., Re*, 11 ETR (2d) 164 (1996 ONSCJ per Winkler J) ["***Brown & Collett***"].

themselves on pricing. They stipulated to Ford that payment would be remitted for goods supplied by both companies to Brown & Collett in cheques payable to Brown & Collett. Brown & Collett undertook to reconcile the accounts as between the two suppliers and remit funds owing to Hay forthwith. Meanwhile the cheque from Ford was deposited in the Brown & Collett general account.

[...]

36 Although the funds were deposited in the Brown & Collett account upon receipt, it was not a term of the agreement that Brown & Collett would be entitled to use the funds attributable to Hay for its own purposes, pending reconciliation. Brown & Collett had no right, title or interest in the monies.

37 In my opinion, for the purposes of collection, reconciliation and remission of funds between Brown & Collett and Hay, Brown & Collett acted as Hay's agent. The terms of the agreement were clear and not disputed. Brown & Collett was to reconcile and remit to Hay forthwith after receipt from Ford.

Winkler J concluded that there was no evidence of an "express" or "implied" trust:

41 Counsel for Hay submits that, in the absence of clear and certain language demonstrating the intention to form a trust, the court may interpret the language and behaviour of the alleged settlor as evidencing such certain intention, and may imply a trust; and that the evidence in the instant matter supports such a conclusion. I disagree.

42 The evidence is categorical that the parties did not intend to create an express trust. Similarly, there is no evidence to support the implication of a trust. It was the evidence of Mr. Clark that the creation of trust was never mentioned by either party, nor were the subject monies ever referred to as trust funds in discussions between Brown & Collett and Hay, or internally at Hay. The funds attributable to Hay were not intended to be, nor were they segregated. This submission is without merit.

Winkler J then discussed the emerging case law on unjust enrichment. Applying the law to the facts before him, Winkler J had little difficulty concluding that there had been (1) a deprivation and (2) a corresponding enrichment. Winkler J then engaged in a fulsome analysis as to whether there was (3) a "juristic reason" for the enrichment. Winkler J rejected Brown & Collett's arguments that the doctrine of unjust enrichment should be applied sparingly in the commercial context, that the principle of unjust enrichment should not apply where the parties are governed by contractual obligations, and that the Court should not make a better bargain than that negotiated by the parties. Winkler J ultimately concluded that Brown & Collett had been unjustly enriched by the payments from Ford that were not remitted to Hay:

68 The terms of the agreement were as simple as they were clear. Brown & Collett was expected to receive, reconcile and remit that [sic] funds attributable to Hay. Although it was to deposit the funds in the general account, it was not to apply the funds to its own use. The agreement was that Brown & Collett was to reconcile and remit forthwith! Instead, under the guise of difficulties encountered in reconciliation, it applied the funds during this period of delay to its own use. This did not come within the stated purview of the contract. Rather, it was a blatant breach of the agreement, which cannot, with any force, be said to justify the enrichment.

69 Hay went along with delays in remittance to it. It was mislead as to the reason for these delays, and as a consequence suffered prejudice. I cannot accede to a submission that there was a juristic reason for this enrichment and perforce it is, in my view, unjust.

While Winkler J concluded that there had been an unjust enrichment, he was not convinced by Hay's submission that a constructive trust should attach to all of the assets of Brown & Collett, and he declined to impose a constructive trust at that stage of the proceedings (despite acknowledging that a constructive trust was a recognized remedy for unjust enrichment). Instead, Winkler J observed that "it is trite law that a constructive trust must attach to specific property and that there be a direct link between the contribution giving rise to the unjust enrichment and the property in which the trust is claimed."

Pending the determination of the potential constructive trust property, and the proper application of any tracing principles, Winkler J scheduled a continuation of the hearing. It does not appear that the further hearing went forward.

d) General Publishing

The decision of *General Publishing Co., Re*[12] involved a priority dispute arising during the course of a CCAA restructuring of a book distributor. Two publishers claimed that they had maintained title to books that they had delivered to the distributor. As such, the publishers "owned" the accounts receivable when the books were sold. The trial judge found that when the books were sold to the ultimate customer, two "simultaneous sales" occurred: one from the publisher to the distributor, and another from the distributor to the customer. The Court of Appeal did not see the need to revisit the lower Court's "simultaneous sale" analysis, instead citing *Hanna* and *Henry* to find that the commingling of funds in the distributor's accounts indicated that the relationship between the publisher and distributor was that of creditor and debtor rather than trustee and beneficiary:

> 4 In our view, in these circumstances accounts receivable stand on no different footing than money. In the instant case there is neither in the agreement nor in the conduct of the parties any suggestion that when GDS received the proceeds of the sales of the books of the publishers, it was to segregate those funds. It was free to deposit the funds and to mingle them with its own money. It follows that the relationship between GDS and a publisher was not that of trustee and beneficiary but of debtor and creditor.
>
> [...]
>
> 6 Whether or not GDS "owned the receivables" as found by Ground J., or the publishers "owned the receivables", as they allege, the fact is that the arrangement required and permitted GDS to collect the money and to put it into its own account. From that account GDS was bound to pay a publisher within 93 days for any books sold to purchasers, whether or not the purchaser had paid for the books. This requirement, it seems to us, negates any suggestion of a trust relationship and leaves the relationship between publisher and distributor as one of creditor and debtor.

e) *Citizens Bank*

In *Citizens Bank of Rhode Island v Paramount Holdings Canada Co.*[13], the insolvent debtor, IC, manufactured greeting cards. A creditor, Transcorp, distributed the cards to customers. Transcorp did not pay cash for the inventory it acquired from IC. When the inventory was sold by IC to Transcorp, IC recorded an account receivable from Transcorp. IC then invoiced the ultimate customer, and in turn issued a credit note to Transcorp for the amount invoiced to the customer.

IC offered "volume" and "early payment" discounts to customers. IC recorded these amounts as receivables. Monies collected from the customer were placed into IC's general bank account without segregation. The difference between the price at which Transcorp purchased the inventory from IC, and the amount invoiced to the ultimate customer, was Transcorp's distribution fee. This system was referred to as the "credit and rebill program".

Over time, as a result of the "credit and rebill program", Transcorp eventually became a significant creditor of IC. IC became insolvent, entered bankruptcy, and a receiver was appointed. Transcorp asserted a trust claim against IC's accounts receivable in the hands of the receiver.

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[12] *General Publishing Co., Re*, 161 OAC 202 (2002 ONCA per Austin, Rosenberg, Laskin JJA) ["***General Publishing***"].
[13] *Citizens Bank of Rhode Island v Paramount Holdings Canada Co.*, [2008] WDFL 2607 (ONSCJ per A. Hoy J) ["***Citizens Bank***"].

Hoy J found that there was no evidence of an "express trust" in the agreements executed between the parties relating to the "credit and rebill program". Hoy J then went on to consider whether an "implied trust" existed between the parties:

> 20 In the absence of formal trust documentation, the Court must consider the circumstances and evidence as to what the parties intended, what was actually agreed to and how the parties conducted themselves to determine if the requisite clear intention to create a trust is present.
>
> 21 Factors the Court will consider include the content of any agreements between the parties, whether the alleged trust property is held in a separate account, whether the alleged trustee is permitted to commingle the alleged trust funds with his or her own funds or use the funds for his or her own general business purposes and, past events and conduct that may suggest that the parties treated the funds as trust funds.
>
> 22 The presence or absence of a prohibition on the commingling of funds is not necessarily determinative. *Commercial Union Life Assurance Co. of Canada v. John Ingle Insurance Group Inc.*, [2000] O.J. No. 3289 (Ont. S.C.J.), paras. 300-305 (affirmed [2002] O.J. No. 3200 (Ont. C.A.).

Hoy J found that an "implied trust" did not exist between the parties. IC's payments to Transcorp were designed to pay down IC's general indebtedness to Transcorp. Accounts receivable did not simply "pass through" IC to Transcorp. There was no requirement for IC to segregate funds. There was no evidence that the word "trust" was used in the parties' discussions regarding payment.

Hoy J also considered whether a constructive trust existed between the parties:

> 23 Constructive trust is an equitable remedy that may be granted in order to prevent an unjust enrichment of a person. In order to impose a constructive trust based on unjust enrichment there must be (1) enrichment; (2) a corresponding deprivation; and (3) no juristic reason for the deprivation.
>
> 24 A "juristic reason" means some underlying justification, grounded in a legal or equitable basis, for the circumstances that have arisen. The juristic reason may arise out of a relationship between the person enriched and some other person, and need not by tied to the person who asserts the unjust enrichment. *Canada (Attorney General) v. Confederation Life Insurance Co.*, [1995] O.J. No. 1959 (Ont. Gen. Div.) (affirmed (1997), 32 O.R. (3d) 102 (Ont. C.A.), paras. 176, 193-194).

Hoy J found that a constructive trust did not exist between the parties, emphasizing that the relationship appeared to be that of creditor-debtor arising out of contract. The interests of the other creditors, and in particular "the security interest of the Bank", provided a "juristic reason" for the enrichment of the other creditors to the detriment of Transcorp. Hoy J specifically considered and distinguished *Brown & Collett:*

> 33 Transcorp is an unsecured creditor of IC. The indebtedness arose out of a contractual business relationship. There was no dishonest or underhanded conduct on the part of IC.
>
> 34 Moreover, as noted in *Confederation Life*, a juristic reason may arise out of a relationship between the person enriched and some other person and (para. 208), in the context of a constructive trust claim against the assets of an insolvent person who is allegedly a constructive trustee, it is important to be aware of the interests of the insolvent's other creditors as well as those of the constructive trust claimant. The security interest of the Bank is a further juristic reason for the deprivation.
>
> 35 This case can be distinguished from *Brown & Collett Ltd., Re*, [1996] O.J. No. 625 (Ont. Gen. Div. [Commercial List]) on which Transcorp relies. In that case, Winkler J. (as he then was) found that there was no implied trust but there was an agreement that funds would be forwarded

by the defendant to the plaintiff as soon as they had been received, and the accounts were reconciled, and that the defendant had breached that agreement. He accordingly concluded that the debtor-creditor relationship arising out of the agreement did not amount to juristic reason because the enrichment was in clear breach of the agreement. He did not determine whether or not a constructive trust was an appropriate remedy in the circumstances. In this case, the enrichment did not arise out of the breach of an agreement between the parties.

f) *NRS Mississauga*

In *Ontario (Director, Real Estate & Business Brokers Act) v NRS Mississauga Inc.*[14], a real estate brokerage, NRS, became insolvent. NRS had a trust account in which it deposited funds to be used in various real estate transactions. An investigation revealed that NRS had misappropriated funds from the trust account for its daily operations. The bank (which held a general security interest) seized all of the assets of the brokerage, with the exception of the remaining funds in the trust account. The beneficiaries of the trust account, represented by the director of the Real Estate and Business Brokers Association, brought an action asserting a constructive trust over the general accounts receivable of the brokerage to the extent that there was a deficiency in the trust account. Doherty JA concluded that the beneficiaries did not have a valid constructive trust claim:

> 30 [...] The Bank was unjustly enriched only if the accounts receivable were impressed with a constructive trust. If they were not, the Bank was entitled to the proceeds. To speak of the Bank as being unjustly enriched by realizing on the accounts receivable is to presume the existence of the very fact in dispute, that is the existence of the constructive trust.
>
> 31 I think the Director's contention that the proceeds of the accounts receivable should be impressed with a constructive trust should be examined first from the perspective of the relationship between the trust claimants and NRS and the conduct of NRS. Viewed in that way, there is no doubt that NRS, a fiduciary, misappropriated trust property by a wrongful act.
>
> 32 In *Soulos, supra*, at 230, McLachlin J. identified four conditions which were generally necessary before a court would impose a constructive trust based on wrongful conduct:
>
> > (1) The defendant must have been under an equitable obligation, that is, an obligation of the type that courts of equity have enforced, in relation to the activities giving rise to the assets of his hands;
> >
> > (2) The assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant in breach of his equitable obligation to the plaintiff;
> >
> > (3) The plaintiff must show a legitimate reason for seeking a proprietary remedy, either personal or related to the need to ensure that others like the defendant remain faithful to their duties and;
> >
> > (4) There must be no factors which would render imposition of a constructive trust unjust in all the circumstances of the case; e.g., the interests of intervening creditors must be protected.
>
> [...]
>
> 35 The second prerequisite identified in *Soulos, supra*, the connection between the assets over which it is sought to impose a constructive trust and the misconduct of the trustee raises considerable difficulties in this case. The evidence offered by the Director speaks at a level of generality that makes it very difficult to draw a direct and clear link between any of the accounts receivable and the misappropriation of trust funds.

[14] *Ontario (Director, Real Estate & Business Brokers Act) v NRS Mississauga Inc.*, 170 OAC 259 (2003 ONCA per Doherty JA) ["***NRS Mississauga***"].

[...]

39 In the light of the application judge's finding that the evidence showed no more than that trust monies were used for the general business purposes of NRS, a finding with which I fully agree, it was inappropriate to impose a constructive trust on the accounts receivable. The Bank was entitled, under the terms of its security agreements with NRS, to realize on those accounts receivable.

40 Although I would not impose a constructive trust given the absence of any clear connection between the misappropriation of trust funds and the accounts receivable collected by the Bank, I will consider the fourth prerequisite identified in *Soulos*, *supra*, for the sake of completeness. That condition speaks to a consideration of the equities as between the victim of the misconduct and third parties such as creditors. In one sense, the Bank can justifiably claim that the imposition of a constructive trust would be unjust. It had perfected security on the accounts receivable which predated the misappropriation of the trust funds by several years. Realistically speaking, the Bank could not be expected to have guarded against the misconduct of NRS.

41 While this view of the events is not unattractive, I think the equities as between the Bank and the trust claimants would justify the imposition of a constructive trust if a clear connection between the misconduct and the assets over which the trust was sought to be imposed had been established. I say that for three reasons. First, the trust claimants were not, and never intended to be, creditors of NRS in the ordinary sense. By depositing trust funds with NRS, the trust claimants were not accepting any risk of economic harm should NRS become insolvent. They were entitled to expect that their money would be kept separate and apart from the assets of NRS and would be returned to them in its entirety in the event of insolvency. The Bank was a creditor. As such, it must be taken to have assumed the economic risks associated with the potential insolvency of the borrower.

42 Second, while the Bank could reasonably expect to have recourse to the assets of NRS should NRS default on the loan, the Bank could not reasonably expect that the value of those assets would be increased through the misappropriation of trust funds by NRS and the use of those funds to augment the value of the business assets of NRS. In other words, the Bank could not expect its borrower to become a thief in order to enhance or protect the value of the Bank's security.

43 Third, the Bank had recourse to other security in the form of personal guarantees and collateral mortgages. That security was solid and initially the Bank had intended to look to that security for recovery. It is appropriate when considering the equities as between trust claimants and the Bank to bear in mind that the Bank had other security which could have fully satisfied the debt of NRS.

44 In summary, I think the application judge erred in imposing a constructive trust on the accounts receivable. As I would not impose a constructive trust on those assets, the question of whether the Bank was in knowing receipt of trust assets does not arise. Given my conclusion that the Bank was entitled to realize on the accounts receivable, it has no interest in the other assets in issue in this proceeding. I will address those assets in the context of the Crown's appeal.

g) *Water Street*

In *Water Street Pictures Ltd. v Forefront Releasing Inc.,*[15] a television producer, Water Street, produced a series of television shows entitled "Edgemont Road". Water Street entered into two agreements with a distributor, Forefront. Pursuant to the agreements, Forefront was to pay all revenues received from the distribution of Edgemont Road, less Forefront's fees, to Water Street in six month intervals. After Forefront encountered difficulties, Water Street purported to terminate the agreements with Forefront, at which point Forefront's secured creditors, VanCity and BDC, realized upon their security. The assets realized by VanCity and BDC included the funds received by Forefront for distributing Edgemont Road. Water Street commenced an action against Forefront, VanCity, and BDC, alleging that the Edgemont Road funds were held in trust by Forefront for

[15] *Water Street Pictures Ltd. v Forefront Releasing Inc.*, 2006 BCCA 459 (per Lowry JA) ["***Water Street***"].

Water Street. Citing both *Hanna* and *Henry*, Lowry JA concluded that no trust relationship existed between Water Street and Forefront, overturning the decision of the trial judge and allowing the appeal for VanCity and BDC:

> 14 The [trial judge's] analysis consists of a number of conclusory statements that regretfully I find to be of little assistance now in understanding the reasoning the judge employed. She made reference to the reality of the situation (both of the agreements and the industry), the commercial circumstances of the industry, the surrounding circumstances of the agreements, the markets in which the parties were operating, the nature of the business and of the contractual relationship, as well as the true nature of the relationship between Water Street and Forefront, without saying what it was about any of these considerations that is significant, or saying what it was about any of them that supports her conclusion that the distribution agreements were to be interpreted as providing for the creation of a trust in respect of "Edgemont Road" distribution revenue. I have difficulty seeing on what evidentiary basis it can be said there was anything remarkable about the industry or the relationship between the producer and the distributor that bears on the way the agreements are to be interpreted.
>
> 15 I have difficulty seeing on what basis it can be said, on the one hand, that, on a plain reading of the contractual language, the agreement provides for the establishment of a trust (para. 107), and, on the other hand, that the agreement contains an ambiguity that bears on that very issue (para. 101). More importantly and in any event, the judge did not explain what it was about the ambiguity she identified that she found confusing and how that confusion bore upon the issue of whether the agreements provide for a trust.
>
> [...]
>
> 17 It may well have been convenient for Forefront to open the account at the TD Bank for the purpose of depositing revenue received from the distribution of "Edgemont Road", but the fact that it opened an account does not mean it had any obligation to do so. It never agreed to open an account much less keep revenue separate.
>
> 18 The judge attached significance to the absence of any provision in the agreements permitting the commingling of funds in the accounts. But what appears to me to be significant is that Forefront was in no way precluded from operating the accounts as it did. The absence of any restriction on what Forefront did with revenue received from the distribution of "Edgemont Road" appears to me to be indicative of there being no intention that Forefront be burdened with trust obligations which may well have been thought to be unnecessary. The significance of not requiring that funds be kept separate was stated by the English Court of Appeal in *Henry v. Hammond*, [1913] 2 K.B. 515 (Eng. K.B.) at 521:
>
> [...]
>
> 42 It would have been a simple matter for the parties to have made provision for distribution revenue to be held in trust, but they did not see fit to do so, nor did they even provide for the revenue being kept in a separate account when it is evident they turned their mind to Forefront being required to maintain separate books of account for the "Edgemont Road" series as distinct from its other distribution business.
>
> 43 The time during which substantial distribution revenue remained in Forefront's bank accounts was as long as half a year, yet no restrictions were imposed on what Forefront could do with the money in all that time. In my view, as in the minority's view in *M.A. Hanna Co.*, it was open to Forefront to use the money as it did, subject only to remitting to Water Street a sum of money equivalent to distribution revenue to which it was entitled every six months, consistent with the principle stated in *Henry v. Hammond*, where there is no obligation to keep money separate. The provisions of the distribution agreements created no trust that deprived the Banks of the priority to Forefront's bank accounts that they otherwise had.

h) Vanquish

In *Brookfield Bridge Lending Fund Inc. v Vanquish Oil & Gas Corp.*,[16] Vanquish, the operator of an oil well, was required to remit a percentage of revenues generated by the well to two co-owners, Karl and Choice. Pursuant to the 1990 CAPL, a trust was imposed upon the well revenues held by Vanquish. The trust permitted Vanquish to commingle funds. All revenues received from the well were paid into Vanquish's general bank account. The lowest balance reached in the account was approximately $40,000.00. A further $40,000.00 of revenue from the well was later deposited. Further deposits unrelated to the well were made, which eventually brought the balance up to approximately $400,000.00. Vanquish ultimately went into receivership, at which point it was in default of approximately $300,000.00 owing to Karl and Choice. Karl and Choice advanced a trust claim for full reimbursement of revenues owed.

Slatter JA concluded that an express trust attached to the "lowest intermediate balance" in Vanquish's bank account, plus the additional revenues deposited with respect to the well, totalling approximately $80,000.00:

> 15 The law is summarized in Goff & Jones, *The Law of Restitution*, 7th ed. (London: Sweet & Maxwell, 2007) at para. 2-038 with this example:
>
> > A trustee mixes his own money with trust money; he withdraws money from the mixed fund, dissipates some of it and then deposits more money into the mixed fund. Subsequent deposits of the fiduciary into the mixed fund are not presumed to be impressed with the trusts in favour of the beneficiary. [Citing *Roscoe v. Winder*, [1915] 1 Ch. 62, 69, *per* Sargant J.; *Bishopsgate Investment Management Ltd. v. Homan*, [1995] 1 All E.R. 347, 354, *per* Dillon L.J.] Consequently if the trustee is insolvent, that part of the mixed fund, equal to the amount paid in, will normally pass to the trustee's general creditors. The beneficiary will be entitled to additions to the mixed fund only if he can prove that thereby the trustee intended to make restitution to the trust. It follows that the trust is entitled only to the lowest intermediate balance of the mixed fund. So, if the fund is wholly dissipated before any additions are made to it, the interest of the trust in the mixed fund is extinguished. Professor Scott has justified this result on the ground that "the real reason for allowing the claimant to reach the balance [of the mixed fund] is that he has an equitable interest in the mingled fund which the wrongdoer cannot destroy as long as any part of the fund remains; but there is no reason for subjecting other property of the wrongdoer to the claimant's claim any more than to the claims of other creditors merely because the money happens to be put in the same place where the claimant's money formerly was, unless the wrongdoer actually intended to make restitution to the claimant." [*Scott on Trusts* § 518.1]
> >
> > Thus the further deposits to the account are not presumed to have the effect of replenishing the trust fund: *Ontario (Director, Real Estate & Business Brokers Act) v. NRS Mississauga Inc.* (2003), 64 O.R. (3d) 97, 226 D.L.R. (4th) 361 (Ont. C.A.) at para. 49; *1653 Investments Ltd., Re* (1981), 129 D.L.R. (3d) 582 (B.C. S.C.), at pp. 597-9, 32 B.C.L.R. 71.
>
> 16 If the trust funds were segregated, the outcome would be clearer. If the trustee misappropriated segregated funds, and then deposited non-trust funds into the segregated account, the intent must have been to replenish the trust account. But where the trust funds are commingled with other funds, the intent is not so clear. Since the trustee by definition is using the account for trust and non-trust purposes, the deposits might simply be made to enable further non-trust expenditures. Where the beneficiary has created the risk of this type of expenditure by allowing commingling, it should not be allowed to easily divert funds from the other creditors of the trustee. Absent a clear intention by the trustee to replenish the trust, which is not found on this record, further deposits are not attached by the express trust.

[16] *Brookfield Bridge Lending Fund Inc. v Vanquish Oil & Gas Corp.*, 2009 ABCA 99 (per Slatter JA) ["***Vanquish***"].

Slatter JA also concluded that Vanquish was not entitled to additional amounts on the basis of a constructive trust:

> 18 As mentioned, Vanquish was clearly in breach of trust by expending the trust funds in unauthorized ways. As such it was in breach of its fiduciary duties as trustee. While the express trust created by the Operating Procedure no longer attached to the funds, are Karl or Choice entitled to a remedial constructive trust for the clear breach of the fiduciary duty by their trustee? In *Soulos v. Korkontzilas* at para. 45 the Court identified four conditions which were generally necessary before a court would impose a constructive trust based on wrongful conduct:
>
> [...]
>
> The second and fourth preconditions are absent on this record.
>
> 19 There was no satisfactory evidence on this record of what, if any, specific assets Vanquish purchased with trust funds. The ability to trace the trust funds into specific assets has always been central to the imposition of a constructive trust in circumstances like this.
>
> [...]
>
> 20 It therefore cannot be shown that the trust proceeds were expended on any of Vanquish's assets that formed a part of the eventual realization by the receiver, so as to satisfy the second precondition. Since Vanquish's wrongdoing cannot be traced into any asset, that precludes the imposition of a constructive trust: *Bassano Growers Ltd. v. Price Waterhouse Ltd.*, 1998 ABCA 198, 66 Alta. L.R. (3d) 296 (Alta. C.A.) at para. 13. The trust funds were apparently used for Vanquish's general ongoing operations. As said in *NRS Mississauga Inc.* at para. 37, it is insufficient "that some unspecified amount of trust funds were used at some unspecified time in some unspecified way to assist to some unspecified degree in maintaining the operation of the business."
>
> 21 The fourth precondition in *Soulos v. Korkontzilas* is also missing. The appellant had a perfected prior secured interest. The decision under appeal essentially assumes that a secured creditor has a positive duty to monitor the fiduciary activities of its borrowers. On the assumption that the secured creditor has a "better opportunity" to prevent breaches of trust, it essentially becomes a guarantor for any such breaches of trust. This analysis discounts the fact that the underlying risk of misappropriation was created by the respondents allowing the commingling of the trust funds, and transfers the duty of monitoring that risk to the appellant. This is contrary to the principle stated in *Soulos v. Korkontzilas* that "the interests of intervening creditors must be protected": *Barnabe v. Touhey* (1995), 26 O.R. (3d) 477 (Ont. C.A.).

APPENDIX B

Paintearth

Final Cosolidated Statement of Receipts and Disbursements
For the period September 27, 2010 to February 26, 2013

	Amount	Notes
RECEIPTS		
Collection of accounts receivable and realization on other assets	$ 2,930,766.68	a
Sale of Paintearth Assets	2,321,949.78	b
Initial cash on hand	120,696.00	c
Other	7,412.52	
TOTAL RECEIPTS	$ 5,380,824.98	
DISBURSEMENTS		
Other		
Distribution to HSBC	$ 3,800,000.00	d
Payroll and related costs	283,302.56	e
Insurance	26,668.51	
Receiver's fees and disbursements	461,227.04	h
Legal fees and disbursements	90,155.38	
GST paid - operations	25,191.46	
Rent and property taxes paid	133,041.83	f
Ad valoreum property taxes paid	54,692.92	
Telephone, utility and computer services	83,727.81	
Other operating expenses	53,085.60	g
Other administrative expenses	2,164.24	
TOTAL DISBURSEMENTS	5,013,257.35	
RECEIPTS LESS DISBURSEMENTS	$ 367,567.63	
PROPOSED FINAL HSBC DISTRIBUTION	367,567.63	
ENDING CASH	$ -	