

IN THE SUPREME COURT OF BRITISH COLUMBIA

BETWEEN:

TRUMPET CAPITAL CORP.

PETITIONER

AND:

OCTAGON PROPERTIES LTD., MARCO DEDOMINICIS,
STONESET EQUITIES LTD., BKDI ARCHITECTS a
partnership, HAYESBORNE HOLDINGS INC., COLIN
LAWSON, and STONESET ONE MORTGAGE
CORPORATION

RESPONDENTS

RESPONSE TO PETITION

Filed by: Stoneset Equities Ltd. and Stoneset One Mortgage Corporation (the “petition respondents”)

THIS IS A RESPONSE TO the petition filed August 12, 2011.

Part 1: ORDERS CONSENTED TO

The petition respondent(s) consent(s) to the granting of the orders set out in the following paragraphs of Part 1 of the petition: NONE

Part 2: ORDERS OPPOSED

The petition respondent(s) oppose(s) the granting of the orders set out in ALL paragraphs of Part 1 of the petition.

Part 3: ORDERS ON WHICH NO POSITION IS TAKEN

The petition respondent(s) take(s) no position on the granting of the orders set out in paragraphs NIL of Part 1 of the petition.

Part 4: FACTUAL BASIS

1. For ease of reference the same definitions are used herein as in the Petition.
2. Stoneset Equities entered an agreement (the “Purchase and Sale Agreement”) for the purchase of the Properties from Octagon on May 17, 2007.
3. The Purchase and Sale Agreement provided for a purchase price of \$23 million, comprised of \$4 million at the purchase date and a vendor take back mortgage (the VTB Mortgage) of \$19 million.
4. Pursuant to the Purchase and Sale Agreement, Octagon conveyed title to the Properties to Stoneset Equities and Stoneset Equities paid \$4 million to Octagon and granted the VTB Mortgage, all of which occurred on or about October 26, 2007.
5. Prior entering the Purchase and Sale Agreement, Octagon represented to Stoneset Equities:
 - (a) That the Properties were in total 12.34 acres, and in other representations, 12.5 acres;
 - (b) That the Properties had a fair market value of \$25 million (in an appraisal provided by Cushman Wakefield based on an acreage of 12.34 acres) and in its own cost projections, \$30 million;
 - (c) That a development on the Properties involving 570 condos, a 144 room hotel and conference centre, and 45,000 square feet of commercial space, was feasible given the zoning, bylaws, and other legal requirements (another representation was for 570 condos, a 120 room hotel and conference centre, and 60,000 square feet of commercial space); and
 - (d) That Octagon’s principal, Marco DeDominicis (“DeDominicis”), had the expertise and experience to develop the Properties in such a manner as part of a joint venture with Stoneset Equities.
6. In fact:
 - (a) The Properties are in total only 9.732 acres;
 - (b) The fair market value in 2007 was not reasonably close to \$25 million and an appraisal by Colliers International in 2010 valued the Properties at \$10.9 million;

- (c) The contemplated development is impossible given (i) the density-based zoning bylaw and the actual acreage and (ii) the zoning bylaw requiring a boardwalk on the portion of the Properties over which a CPR statutory right of way exists, which CPR has refused to permit;
 - (d) DeDominicis did not have the expertise or experience required for the contemplated development.
7. Stoneset Equities relied on the representations made in purchasing the Properties and Stoneset Equities has paid \$22,729,355.00 in direct costs for the development of the Properties, including the \$4 million downpayment, \$13,075,601 in payments on the VTB Mortgage, and various other consulting, pre-development and interest expenses.
 8. It was a condition precedent and fundamental to the Purchase and Sale Agreement that Stoneset Equities enter joint venture and management agreements with a company nominated by DeDominicis and controlled by DeDominicis. Stoneset Equities in fact entered into a Joint Venture Agreement (the "JVA") with Navigator Development Invermere Corporation ("Navigator Invermere") on May 15, 2007. Stoneset Equities in fact entered into a management agreement (the "Management Agreement") with Navigator Development Corporation ("Navigator Dev") on May 15, 2007. Both Navigator Invermere and Navigator Dev were controlled and represented by DeDominicis.
 9. The Navigator companies did not perform their obligations under the JVA and the Management Agreement, in not providing project financing and not managing the development.
 10. Construction of the development has not occurred on the Properties.
 11. The \$25 million Cushman appraisal of the Properties was prepared by Brad Kroeker. Brad Kroeker also prepared another appraisal for Octagon of lands commonly called "Symons Valley Ranch" in Calgary, Alberta, in 2008 for \$20.68 million. In 2009, in an appraisal prepared for Trumpet, the lands were valued at \$11,072,000. Trumpet foreclosed on a mortgage on the Symons Valley lands which was assigned by Octagon as security for a loan given by Trumpet to Octagon.

12. DeDominicis verbally represented to Tony Argento of Stoneset Equities that the Properties had an acreage of 12.34 acres prior to the date of the Cushman appraisal which stated the Properties were 12.34 acres.
13. Trumpet has stated that the amount due to it under the VTB Mortgage is the amount outstanding on the Loan, in both (a) a request from Stoneset for a statement of debt under the VTB Mortgage and (b) in invoices for outstanding amounts under the VTB Mortgage.

Part 5: LEGAL BASIS

1. There are two defences to this petition:
 - (a) The Petitioner took the VTB Mortgage subject to the equities between Octagon and Stoneset Equities, which include a right to rescission of the VTB Mortgage for fraudulent or innocent misrepresentation and a set-off for damages for negligent misrepresentation; and
 - (b) The Petitioner's interest in the VTB Mortgage is limited only to the amount outstanding on the Loan.
2. This Petition should be absolutely dismissed or alternatively remitted to trial pursuant to Rule 22-1(7)(d).

Test for Remitting to Trial: Bona Fide Triable Issue

3. The test for remitting a petition to trial is summarized in *TCC Mortgage Holdings Inc. v. Alysen Place Developments Inc.* 2011 BCSC 383:
 - (a) The onus is on the Petitioner to show that there are no triable issues (para. 13);
 - (b) Unless it is manifestly clear that the mortgagors are without a defence that deserves to be tried, the matter should be remitted to trial (para. 14);
 - (c) The threshold to establish a triable issue is not high (para. 14).
4. In *Willowdale Holdings Ltd. v. Shaw Ranches Ltd.* [1982] B.C.J. No. 646 (S.C.), the court remitted a foreclosure petition to trial in like circumstances. The mortgagor purchased the property from the mortgagee petitioner and alleged a misrepresentation that only 300

of the 2,488 acres were not under cultivation, whereas in fact 800 acres were not. The court stated at paras. 10 and 11:

To recapitulate, assuming that there was a misrepresentation the respondent's remedies would be:

- (1) damages for negligent representation;
- (2) rescission for misrepresentation of a material fact substantially affecting the consideration;
- (3) rescission for fraudulent misrepresentation;
- (4) damages for the tort of deceit arising from the fraudulent misrepresentation.

The misrepresentation alleged by the respondent concerns the contract for the sale of the land rather than the mortgage. All of the remedies hereinbefore set out relate to the contract of sale rather than to the mortgage. Only if the covenants contained in that sale agreement merge into the mortgage could the respondent raise these questions of misrepresentation directly against the mortgage. However, if the contract of sale is rescinded then the mortgage would fail for lack of consideration as the respondent would have no interest in the land to give in return for the borrowed money. In that sense, therefore, the issue of a misrepresentation allowing rescission could substantially affect the mortgage foreclosure.

5. The British Columbia Court of Appeal has stated the following regarding the rescission of mortgages which are one part of a larger transaction between the parties: “[T]he mortgages are merely security for the payment of the cash consideration for the exchange, and should be rescinded along with the rescission of the whole transaction”: *Kupchak et al. v. Dayson Holdings Co. Ltd. et al.* [1965] 53 D.L.R. (2d) 482 (B.C.C.A.) at para. 15.

Assigned VTB Mortgage Subject to Rescission

6. It is trite law that an assignee of a mortgage takes it subject to the equities that exist as between the mortgagor and the original mortgagee (see for example *Law and Equity Act*, section 36, which permits assignees to sue in their own name but preserves the existing equities).

7. The right to rescission arising from circumstances existing at the time of making a mortgage is an equity to which an assignee of the mortgage is subject: *London and Western Canada Investment Co. v. Dolph* (1918), 43 O.L.R. 449 (H.C.J.), cited with approval in *Costco Wholesale Canada Inc. v. Cavalet* 2008 BCSC 952 at para. 18.

Alternatively, Trumpet's Interest in Mortgage Limited to Outstanding Loan Amount

8. The Petitioner would be unjustly enriched if it received from the VTB Mortgage more than the amount owing on the Loan. If the Petitioner obtains an order for sale of the Properties, then the proceeds in excess of the Loan and the permitted expenses should be paid into court to the credit of the action.
9. The Petition states that Octagon's interest in the VTB Mortgage was assigned to the Petitioner as security for the Loan; and the Petitioner has adduced a Loan Agreement (Exhibit A to affidavit #1 of James Gordon David) clearly showing at para. 6 that security for the Loan shall include the assignment and transfer of the VTB Mortgage.
10. The difference between an assignment as security and an absolute assignment was summarized in *Alberta (Treasury Branches) v. M.N.R.* [1996] 1 S.C.R. 963 ["ATB"] at para. 15:

[...] the same instrument cannot be both a "security interest" and an "absolute assignment". If an instrument is an absolute assignment, then since it is complete and perfect in itself, there cannot be a residual right remaining with the debtor to recover the assets. By definition, a complete and perfect assignment cannot recognize the concept of an equity of redemption. An absolute assignment cannot function as a means of "securing" the payment of a debt since there would be no basis for the debtor to recover that which has been absolutely assigned. An absolute assignment is irrevocable. To say that the same instrument can operate both as an absolute assignment and as a security interest is to simultaneously put forward two incompatible positions. The two conflicting concepts cannot live together in the same document.
11. An absolute assignment of the VTB Mortgage would amount to factoring (*ATB*, paras. 30-31): the Petitioner purchasing a receivable at a substantial discount (the amount outstanding to Octagon under the VTB Mortgage was and is far in excess of the Loan).

But the Petition does not state that Trumpet took the assignment in extinguishment of the Loan debt; to the contrary, Trumpet seeks payment of the Loan debt.

12. To determine whether a document is an absolute assignment or merely a charge, it is necessary to determine the nature of the transaction and the real facts and intentions of the parties. The manner and form of the assignment is immaterial provided the intention of the parties is clear. To discern the intention, the court must consider the language of the document itself, the evidence of the parties as to the surrounding circumstances existing at the time of the document's creation; in other words, the overall factual matrix at the relevant time: *Winnipeg Enterprises Corp. v. 4133854 Manitoba Ltd.* 2008 MBCA 23 at paras. 16-19.
13. In *ATB* the Honourable Mr. Justice Major, while in dissent on the outcome, agreed with the majority that the equity of redemption applies when an assignment is taken as security (at para. 96):

At base, the equity of redemption is no more than a recognition that the assignment of debts to the creditor, while immediate and absolute, is for a limited purpose. In equity, the creditor cannot unjustly enrich itself by realizing on more security than the value of the loan which is secured. At any given time the value of the security may exceed the value of the loan, but upon termination of the lending relationship, the assignor of the security is entitled, in equity, to an accounting.

14. The Petitioner is therefore liable to account for the surplus of sale proceeds of the Properties to Octagon, and the proceeds should be held in court for the benefit of Octagon and Stoneset, pending resolution of the equities and setoffs between Stoneset and Octagon. (The setoffs include the claims by Stoneset against Octagon for misrepresentations giving rise to the VTB Mortgage and for breach of the subsequent joint venture agreement between them).

Part 6: MATERIAL TO BE RELIED ON

1. Affidavit #1 of Tony Argento sworn September 26, 2011.

The petition respondent(s) estimate(s) that the application will take 2 hours.

Date: September 26, 2011.

Signature of lawyer for petition respondent
Andrew Bird

Petition respondents' address for service: Suite 202, 502 Third Avenue, Fernie, British Columbia, V0B 1M0

Fax number for service (if any): N/A

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Name of the petition respondent's(s') lawyer, if any: Andrew Bird