

POST UP: CREDITOR ORDERED TO DEPOSIT SECURITY FOR COSTS IN BRITISH COLUMBIA BANKRUPTCY PROCEEDING

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The tension between a trustee seeking to facilitate a proposal for the benefit of all creditors and a single creditor being forced to release its rights for the “greater good” was front and center in a recent case before the Supreme Court of British Columbia. In *Asian Concepts Franchising Corp., Re.*,^[1] the Proposal Trustee appointed under the *Bankruptcy and Insolvency Act* applied for an order requiring a creditor to post security for costs. In doing so, the Trustee sought to prevent the erosion of the pool of funds to be distributed to creditors in the contemplated proposal as a result of challenges by the creditor aimed at defeating the proposal.

Background

Asian Concepts Franchising Corp. (“Asian Concepts”) was party to a development agreement with Adrenaline Drive Inc. (“Adrenaline”). Asian Concepts filed a notice of intention to make a proposal. Adrenaline claimed in the proposal proceeding that Asian Concepts breached the development agreement resulting in damages to Adrenaline of \$8,166,774.82. The Proposal Trustee allowed the claim for only \$754,720.25. With claims in the proceeding totaling \$3,090,011.40, Adrenaline was not going to be able to affect the outcome of the vote on the proposal. A proposal will be accepted with approval of 50% of the creditors having 2/3rds of the debt.

To better its position, Adrenaline requested that the Proposal Trustee disallow the proofs of claims of four other creditors, investigate third party claims and disclose various documents. When negotiations between Adrenaline and Asian Concepts with respect to how Adrenaline’s claim might be dealt with under the proposal broke down, Adrenaline applied for an order permitting it to acquire the Proposal Trustee’s powers to review and disallow various claims. The Proposal Trustee brought an application for security for costs in response.

Decision of the Court

Adrenaline admitted that recovery in bankruptcy was not its motivation for its requests of the Trustee. If approved, the proposal would preclude it from advancing its claims in an action it had commenced in Alberta against Asian Concepts and some of Asian Concepts’ creditors. Those creditors were contributing to the pool of funds that would be distributed as part of the proposal, and the proposal thus provided for a release for

those contributing creditors. It was the loss of its claims in Alberta that Adrenaline sought to avoid by blocking the proposal.

Based on the *Bankruptcy Rules* the Registrar concluded that whether security for costs ought to be granted, and the quantum of such security, would be determined in accordance with the ordinary practice in British Columbia courts. The ordinary practice was the common law test developed under s. 236 of the *British Columbia Business Corporations Act*. As there was no evidence before the Court to contradict the prima facie case made by the Proposal Trustee that Adrenaline had no assets in British Columbia or Alberta, the Court granted the order for security for costs. The Court held that it was proper for the Proposal Trustee to seek and be awarded security for costs based on its obligations to all creditors in the bankruptcy, particularly in this case where Adrenaline had an interest in pursuing its claims that was completely outside the proposal proceeding. The Court observed as follows:

A proposal trustee has an obligation to all of the creditors to maximize their recovery. In those circumstances, in my view, it is not only incumbent upon the trustee to bring or defend applications or actions, but it is most appropriate that costs should be awarded to the trustee should circumstances warrant.^[2]

The Court held that the Trustee's opportunity to recover any such awarded costs ought to be protected.

Protection for Stakeholders Through Security for Costs

Security for costs is often posted by foreign litigants who initiate claims in Canada. Awarding of security for costs against a creditor advancing its perceived rights in an insolvency proceeding is, however, rare.

The result in *Asian Concepts* may have significant implications for future proceedings under the *Bankruptcy and Insolvency Act* and other insolvency legislation. While there will certainly be instances where it would be entirely unfair for a creditor, drawn into insolvency proceedings through no fault of its own, to then pay more money in the form of security for costs just to pursue its rights, circumstances may warrant some measure of protection for other stakeholders. Parties with a duty to maximize recovery for all creditors may rely on this decision to require a creditor to post security for costs whenever there is a perception that a creditor is seeking to impact the rights of others solely for its own benefit rather than for the benefit of creditors generally.

by Jeffrey Levine and Lauren Ray

[1] *Asian Concepts Franchising Corp., Re*, 2016 BCSC 1581[ps2id id='1' target='']

[2] *Asian Concepts Franchising Corp., Re*, 2016 BCSC 1581, at 70.[ps2id id='2' target='']

A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against



making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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