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How real are your rights? The Court of Appeal clarifies jurisdiction to vest real property rights off title

In *Third Eye v Dianor*, the Court of Appeal for Ontario revitalized the law of vesting orders, confirming that a motion judge of the Superior Court of Justice has jurisdiction to extinguish interests in land in a receivership, and setting a new test for when that power should be exercised. The Court also clarified the precedence between the 10-day appeal period set out in the *Bankruptcy and Insolvency Act* (“BIA”) Rules, and the 30-day period prescribed through the *Courts of Justice Act* (“CJA”).

The decision is good news for insolvent corporations, who are now more attractive to purchasers skittish about encumbered assets. It will also have implications for how future royalty deals in the mining industry are negotiated and structured.

Background

Dianor was a mining company with mining claims over a project in Wawa, Ontario. It purchased those claims from 2350614 Ontario Inc (“235Co”) in exchange for a Gross Overriding Royalty (“GOR”) for diamonds and other metals and minerals.

In 2015, Dianor became insolvent and went into receivership. Third Eye offered to purchase Dianor’s mining claims for \$2 million, on the condition that it would acquire the asset unencumbered by 235’s GORs. As part of the proposed deal, Third Eye offered to pay 235Co \$250,000, representing the fair market value of the GORs as appraised. 235Co rejected the offer.

The motion judge approved the sale, holding that the GORs were not an interest in land, and extinguishing them from title. 29 days after the Approval and Vesting Order was granted (8 days after the sale transaction had closed), 235Co filed a notice of appeal. In March of 2018, the Court of Appeal found that the GORs did constitute an interest in land, and asked the parties for further argument on a number of issues related to the extinguishment of the GORs.

The second phase of the appeal was argued in September of

2018. The main questions before the Court were:

- Whether a third party interest in land in the nature of a GOR could be extinguished by a vesting order in a receivership proceeding; and
- Whether the appeal period in the *BIA* (as opposed to that in the *CJA*) governs the appeal from the order of the motion judge.

Jurisdiction to Extinguish an Interest in Land Using a Vesting Order

Prior to this case, there had been little judicial consideration of a motion judge's jurisdiction to extinguish interests in land during a receivership, although this was frequently done and in fact finds articulation in the Model Approval and Vesting Order.

The Court undertook a comprehensive analysis of the *BIA* and its legislative history, ultimately concluding that s. 243(1) provides a court with the jurisdiction to approve a sale proposed by a receiver, and that this jurisdiction extends to the implementation of the sale through the use of a vesting order.

The Court recognized the possibility that s. 21 of the *Conveyancing Law of Property Act* also provides authority for vesting property in purchasers free and clear of encumbrances, but decided against determining that issue as it was not before the motion judge.

Having found that jurisdiction exists under s. 243(1) of the *BIA* to grant a vesting order, the Court considered whether it was appropriate to vest out 235Co's GORs. This analysis, the Court noted, was not one of jurisdiction, but rather related to the scope and "appropriateness" of the vesting order.

The Test for Extinguishing an Interest in Land

The Court established a two-part test for determining whether a third party interest should be extinguished:

- First, the court should consider the nature and strength of the interest that is proposed to be extinguished; and
- Second, the court should consider whether the interest holder has consented to the vesting out of its interest.

The Court observed that interests in land fall on a spectrum, ranging from an ownership interest tied to the inherent characteristics of the property (such as a fee simple), to a fixed monetary interest that is extinguished when the monetary obligation is satisfied (such as a mortgage). The Court noted that a reasonable expectation of the owner of the former type of

interest is that its interest is of a continuing nature, and that it will not be extinguished for payment without consent.

With respect to the consent element, the court should consider “whether the parties have consented to the vesting of the interest either at the time of the sale before the court, or through prior agreement”.

The Court directed that if the two considerations set out above prove to be inconclusive, then the court may engage in a consideration of the equities to determine if a vesting order is appropriate in the circumstances. At this stage, the court should consider (among other factors):

- whether there is any prejudice to the third party interest holder;
- whether the third party may be adequately compensated for its interest;
- Whether there is any equity in the property; and
- Whether the parties are acting in good faith.

Application of the Test

Relying on the decision of the Supreme Court of Canada in *Bank of Montreal v Dynex Petroleum Ltd.*, 2002 SCC 7, the Court clarified that a GOR is an interest in the gross product extracted from the land, and not a fixed monetary sum. Importantly, the Court expressed that the GORs “did not exist simply to secure a fixed finite monetary obligation; rather they were in substance an interest in a continuing and an inherent feature of the property itself”. On that basis, the Court found that the motion judge had erred in granting an order extinguishing 235Co’s GORs.

Appeal Period

In a closely followed decision on the timing for an appeal in respect of vesting orders, the Court, relying on the doctrine of federal paramountcy, decided that the 10-day appeal period set out in Rule 31 of the *BIA Rules* takes precedence over the 30 day appeal period prescribed by Rule 61.04(1) of the *Rules of Civil Procedure*. The Court confirmed that this 10-day period begins to run from the date of the order or *decision* of the motion judge. The Court further directed that a receiver should wait out the 10-day appeal period before closing a sale transaction to which the vesting order relates.

The Court found no evidence that 235Co. intended to appeal within the applicable time period, and ultimately refused to grant an extension of time to appeal *nunc pro tunc*.

In the result, Third Eye was successful as a result of 235Co’s

failure to appeal the motion judge's decision in time.

With notes from Adil Abdulla.