

## A Failure to Communicate: Trustee's Claim to Non-Exempt Equity in Bankrupt's Property Should be Declared at Time of Assignment in Bankruptcy

Bankruptcy trustees should clearly communicate to the bankrupt their intent to make a claim against the non-exempt equity in the bankrupt's property at the time of the assignment into bankruptcy, according to the recent decision of the British Columbia Supreme Court in *Re Barter*.<sup>1</sup> A failure to communicate such an intent may result in the trustee being unable to realize the non-exempt equity or, as in *Re Barter*, the absolute discharge of the bankrupt, without requiring the bankrupt to pay to the estate the price agreed upon for the right to sell the property.

The property of the bankrupt, including the non-exempt equity in the bankrupt's home, vests in the trustee upon the assignment into bankruptcy.<sup>2</sup> The trustee is permitted, but not required, to register the bankruptcy order on title to the bankrupt's real property.<sup>3</sup>

In *Re Barter*, the bankrupt's property was subject to foreclosure proceedings and, at the time of his assignment into bankruptcy,

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<sup>1</sup> 2014 BCSC 528 [*Re Barter*].

<sup>2</sup> RSC 1985, c B-3, s 71 [*BIA*].

<sup>3</sup> *BIA*, s 74(1).

the bankrupt had listed the property for sale in the hopes of avoiding a shortfall on the mortgage which would save his wife from also assigning into bankruptcy. When he attended the trustee's office to sign the assignment documents, the bankrupt alleged he was not told that he was not allowed to sell the property. The trustee, in fact, did not register against title the trustee's interest in the property, because the trustee estimated there was no realizable equity in the property.

The Court held that it was not until six months later that the trustee advised the bankrupt that he did not have a right to sell the property. According to the Court, the trustee only did so after learning that the bankrupt had received an offer for the property and was intending to make a counteroffer. At which time, the trustee told the bankrupt he could only sell the property if he purchased the interest in the property from the estate. In light of the trustee's advice, the bankrupt agreed to pay \$2,000 for the right to sell the property. The sale ultimately fell through and the property was sold with a shortfall on the mortgage. Upon his application for discharge, the bankrupt objected to paying the \$2,000 to the estate as a condition of his discharge.

While acknowledging case law which suggests the trustee may declare an intention to claim the non-exempt equity in the bankrupt's property at any time up until the discharge of the bankrupt, the Court held that the best time to declare such an intention is at the beginning of the bankruptcy when the value is estimated.<sup>4</sup> The Court cited the Saskatchewan Court of Appeal in *Deloitte, Haskings & Sells Ltd. v. Zemlak*,<sup>5</sup> for the minimum requirements to be met when dealing with non-exempt equity in the bankrupt's home, namely:

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<sup>4</sup> *Re Barter*, at para 23.

<sup>5</sup> (1987) 66 CBR (NS) 1 ["*Zemlak*"].

- (a) the trustee's report on the bankrupt's application for discharge should set out the value of any non-exempt equity if the trustee intends to attach it for future realization;
- (b) the notice to creditors of the discharge application should also indicate if the trustee intends to maintain a caveat against the property after the bankrupt's discharge; and
- (c) the trustee should advise the bankrupt to have independent legal advice for the discharge application.<sup>6</sup>

The minimum requirements were not applicable in *Re Barter*, because the trustee was asserting the claim at the discharge hearing rather than after the bankrupt's discharge; however, the Court concluded that the *Zemlak* decision established a minimum standard, which requires the trustee to clearly communicate to the bankrupt the trustee's intention to make a claim against the non-exempt equity.<sup>7</sup>

The Court held the trustee failed to meet the minimum standard by advising the bankrupt of the trustee's intent to claim against the non-exempt equity only after the bankrupt indicated his intent to negotiate a sale of the property. Any discussion about the right to purchase an asset from the trustee should have occurred at the beginning of the bankruptcy.<sup>8</sup> Consequently, the bankrupt was granted an absolute discharge and was relieved from paying the \$2,000 price for the right to sell the property.

Trustees should take note of the Court's comments in *Re Barter*, namely that the intent to make a claim against the non-exempt

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<sup>6</sup> *Re Barter*, at paras 27-28, citing *Zemlak*, at 11-12.

<sup>7</sup> *Re Barter*, at para 29.

<sup>8</sup> *Re Barter*, at para 37.

equity in the bankrupt's property should be clearly communicated to the bankrupt at the beginning of the bankruptcy. Failure to do so could result in trustees being unable to realize against non-exempt equity in the bankrupt's property where the minimum requirements set out in *Zemlak* are not adhered to.

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#### a cautionary note

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