

COURT OF APPEAL FOR ONTARIO

CITATION: Convoy Supply Ltd. v. Elite Construction (Windsor) Corp.,
2023 ONCA 373
DATE: 20230525
DOCKET: COA-22-CV-0244

Trotter, Sossin and Copeland JJ.A.

BETWEEN

Convoy Supply Ltd. / Distribution Convoy Ltée.

Plaintiff (Respondent)

and

Elite Construction (Windsor) Corp.,
Kostas Michos and Dan Michos

Defendants (Appellants)

Colin J. Bondy, for the appellants

Emily Durst, for the respondent

Heard: May 10, 2023

On appeal from the order of Justice Andrew J. Goodman of the Superior Court of Justice, dated September 22, 2022, with reasons reported at 2022 ONSC 5353.

REASONS FOR DECISION

[1] The appellants appeal the order of the motion judge: (i) lifting the stay of proceedings pursuant to s. 69.3 of the *Bankruptcy and Insolvency Act*, R.S.C., 1985, c. B-3 (the “BIA”); and (ii) amending the default judgment against the

appellants, granted March 3, 2021, pursuant to rule 59.06(2) of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194, to add declarations that the debt owed by the appellants to the respondent pursuant to the default judgment arose by reason of the individual appellant having committed misappropriation or defalcation while acting in a fiduciary capacity; and, that as a result, pursuant to s. 178(1)(d) of the *BIA*, the debt survives bankruptcy.

Factual background

[2] A brief summary of the facts is sufficient to provide the context for the issues raised in this appeal. The underlying action related to construction materials supplied by the respondent to the appellants for use in various construction projects. The appellants' payment for the materials supplied was deficient.

[3] In July 2020, the respondent commenced a claim against the appellants seeking, *inter alia*, approximately \$92,000 in damages for breach of trust, or in the alternative, general damages in the amount of \$92,000. The claim included a request for an order, if required, for leave to continue the action pursuant to s. 69.4 of the *BIA* as against any defendant that has made or makes an assignment in bankruptcy, as well as an order, pursuant to s. 178(1)(d) of the *BIA*, that a damages award made in the action would not be discharged in the event that any defendant has made or makes an assignment in bankruptcy.

[4] The Statement of Claim pleaded and relied upon the *Construction Lien Act*, R.S.O. 1990, c. C.30 (the “CLA”) and the *Construction Act*, 1990, c. C.30 (the “CA”), alleging that the appellants were liable pursuant to the statutory trust provisions and that the individual appellant was an officer, director, guarantor, and directing mind of the corporate appellant. Without reproducing the claim in its entirety, it included pleadings of the following material facts:

- That the appellants failed to pay the respondent for construction materials supplied to the appellants for use on construction projects (“improvements” to land, in the language of the CA), in the amount of approximately \$92,000 plus additional interest;
- That all amounts owing to or received by the appellants for the improvements constituted a trust for the benefit of the respondent because the respondent had supplied materials for the improvements;
- That the appellants had been unjustly enriched;
- That the appellants appropriated or converted all or part of the trust funds to their own use or to a use inconsistent with the trust and trust obligations prior to paying the respondent all amounts related to each improvement, as owed by the appellants to the respondent;
- That the individual appellant, as a director, officer, guarantor, and person with effective control over the corporate appellant, assented to or acquiesced in conduct that he knew or ought to have known amounted to a breach of trust; and
- That the conduct of the appellants, in failing to preserve and properly distribute statutory trust funds, warranted an award of punitive damages as it constituted misconduct that markedly departed from ordinary standards of decent behaviour.

[5] The appellants were noted in default. Default judgment was granted by Gordon J. on March 3, 2021. The order included an award of approximately

\$92,000 in damages for breach of trust, and an award of \$7,500 in punitive damages.

[6] The respondent took various steps to attempt to enforce the default judgment. These steps are summarized in detail in the reasons of the motion judge. We will not reproduce them here, other than to note that the appellants were not compliant with the enforcement procedures – in particular, by failing to produce information and documents that they were repeatedly ordered to provide. At the time the motion under appeal was heard, the appellants remained in breach of various court orders to produce documents and attend for examination in aid of execution.

[7] Following the initiation of contempt proceedings against the appellants by the respondent in relation to orders made in the course of the respondent's attempts to enforce the default judgment, the individual appellant made an assignment into bankruptcy on December 14, 2021.

[8] By way of additional context, we note that when the motion judge heard the respondent's motion to determine whether the debt created by the default judgment survived bankruptcy, he also heard a cross-motion by the appellants to set aside the default judgment. In oral reasons, the motion judge dismissed the cross-motion. Thus, the motion judge considered the respondent's motion for a determination that the default judgment debt survived bankruptcy against the

backdrop that he had already rejected the appellants' motion to set aside the default judgment. The appellants have not appealed the dismissal of their cross-motion to set aside the default judgment.

Analysis

[9] The appellants argue that the motion judge erred in refusing to admit evidence on the motion tendered by the individual appellant about mental health issues he experienced. The appellants argue that this evidence was relevant to provide context for the deemed admissions, which form the basis for the default judgment, and whether the appellants' conduct in relation to the trust funds should be characterized as involving wrongdoing or improper conduct.

[10] We do not agree. The motion judge correctly recognized that he had a discretion to consider extrinsic evidence regarding the alleged misappropriation of trust funds on a rule 59.05(2) motion. The motion judge considered the nature of the evidence that the appellants proposed to tender and found that the evidence sought to contradict the deemed admissions that were inherent in the default judgment. The motion judge concluded that it was not appropriate to allow the appellants to seek to contradict the deemed admissions by extrinsic evidence, as doing so would be tantamount to setting aside the default judgment. He also noted that the appellants had failed to comply with court-ordered productions in the subsequent enforcement proceedings. We underline that this evidentiary ruling

was made in the context of the appellants having sought, and failed, to set aside the default judgment. We are not persuaded that the motion judge committed any palpable and overriding error in his exercise of that discretion.

[11] The appellants next argue that the motion judge erred in considering the procedural history of subsequent steps by the respondent to enforce the default judgment and the appellants' actions in the context of those enforcement steps.

[12] We see no merit in this ground of appeal. The motion judge considered the procedural history, in particular the appellants' failure to comply with court-ordered productions, as a factor in exercising his discretion not to allow the appellants to tender new evidence, which, as noted above, the motion judge viewed as seeking to contradict the deemed admissions. The procedural history of enforcement efforts by the respondent subsequent to the default judgment, and the appellants' non-compliance with those efforts, was included in the record before the motion judge. He was entitled to rely on the procedural history as a factor in exercising his discretion regarding admissibility of evidence.

[13] Further, we do not accept the appellants' argument that the motion judge relied on the procedural history of the subsequent attempts to enforce the default judgment in coming to the conclusion that the individual appellant failed to account for the trust funds under the *CA*. The reasons of the motion judge demonstrate that

he drew this conclusion from the deemed admissions that were available from reading the Statement of Claim as a whole.

[14] Finally, the appellants argue that the motion judge erred in finding, on the record before the court, that the judgment debt arose from misappropriation or defalcation in relation to the trust funds.

[15] The appellants acknowledge that the motion judge correctly stated the law in relation to the nature of the factual findings required to engage s. 178(1)(d) of the *BIA*. We agree. In particular, the motion judge recognized that, as a result of the default judgment, the appellants were deemed to admit the facts pleaded in the Statement of Claim. He recognized that he was required to make a factual assessment of whether the breach of trust, in the context of the deemed admissions from the pleading, engaged s. 178(1)(d) of the *BIA*. He also recognized that, in order for a judgment debt to trigger s. 178(1)(d) as arising from “fraud, embezzlement, misappropriation or defalcation while acting in a fiduciary capacity”, the debt must arise from conduct that displays at least some element of wrongdoing or improper conduct that would be unacceptable to society because of its “moral turpitude or dishonesty”: *Simone v. Daley* (1999), 43 O.R. (3d) 511 (C.A.).

[16] However, the appellants contend that the motion judge did not apply the law correctly to the facts before him. The appellants’ argument has two branches. First,

they argue that the motion judge found that *any* finding that trust funds were directed for a purpose inconsistent with the trust is morally dishonest and will constitute “misappropriation or defalcation” for the purposes of s. 178(1)(d) of the *BIA*. Second, they argue that the deemed admissions in the Statement of Claim, on which the default judgment rests, are insufficient to establish the type of wrongdoing or improper conduct in relation to trust funds required to engage s. 178(1)(d) of the *BIA*.

[17] We disagree with both branches of this submission.

[18] Regarding the first branch, we do not agree with the appellants’ characterization of the motion judge’s decision. The motion judge did not find that *any* finding that trust funds were directed for a purpose inconsistent with a trust will constitute misappropriation or defalcation for the purposes of s. 178(1)(d) of the *BIA*. Rather, he considered, on the record before him and with particular regard to the deemed admissions, whether the specific breach of trust by the appellants displayed an element of wrongdoing or improper conduct as required to engage s. 178(1)(d) of the *BIA*. That the motion judge made a case-specific finding and did not rely on a categorical rule is clear from the fact that his reasons expressly considered whether the deemed admissions were of conduct which could have been done negligently or incompetently (which would not have triggered

s. 178(1)(d) of the *BIA*), or were of conduct done intentionally and with an element of misconduct.

[19] Regarding the second branch of the appellants' argument, we see no basis for appellate intervention in the motion judge's findings that the record was sufficient to establish that the judgment debt arose from misappropriation or defalcation.

[20] As we have noted above, there is no error in the motion judge's statement of the applicable law. In applying the law to the record before him, the motion judge considered a number of factors in coming to the conclusion that the deemed admissions regarding the appellants' conduct in relation to the trust funds satisfied the element of wrongdoing or improper conduct required to trigger s. 178(1)(d) of the *BIA*, including:

- That the deemed admissions were not allegations of negligent or incompetent conduct, but rather, were acts of the individual appellant converting or appropriating trust funds for his own use or a use inconsistent with the trust;
- That the acts deemed admitted were intentional, in that the individual appellant "assented to and acquiesced" in the diversion of trust funds established under the *CA* for purposes inconsistent with the trust; and
- That the default judgment included an award of punitive damages, which, as the motion judge noted in his review of the deemed admissions, was based on a pleading (deemed admitted) that the conduct of the appellants was "misconduct that markedly departs from ordinary standards of decent behaviour".

[21] The motion judge also considered relevant authorities of this court and the Superior Court in order to assess the types of conduct that have been found to be sufficient to meet the threshold of wrongdoing or improper conduct necessary to constitute misappropriation or defalcation under s. 178(1)(d) of the *BIA: Bibico Electric Inc v. Battlefield Electrical Services Inc.*, 2012 ONCA 676, aff'g, [2011] O.J. No. 6557 (S.C.); *Yanic Dufresne Excavation Inc. v. Saint Joseph Developments Ltd.*, 2022 ONCA 556, 22 C.L.R. (5th) 185; *Re: Ieluzzi (#2)*, 2012 ONSC 1474, 88 C.B.R. (5th) 215. This aspect of the motion judge's reasons underlines the fact-specific analysis he engaged in.

[22] The conclusion that the appellants' actions in relation to the statutory trust funds had the element of wrongful or improper conduct necessary to constitute misappropriation or defalcation was open on the record before the motion judge. We see no palpable and overriding error in his conclusions.

Disposition

[23] The appeal is dismissed. In accordance with the agreement of the parties, the appellants shall pay costs of the appeal to the respondent in the amount of \$14,000, inclusive of disbursements and applicable taxes.

"Gary Trotter J.A."

"L. Sossin J.A."

"J. Copeland J.A."