



Joint Debts, Joint Tenants - Insolvency Law Meets Real Estate Property Law

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The decision of the Court of Appeal in *TD Bank v. Phillips* [2014 ONCA 613] involves a separated couple, their joint asset, a joint debt, and an outcome that is anything but, thanks to creditor protection afforded by the *Bankruptcy and Insolvency Act* (“*BLA*”). This decision highlights some of the intricacies of these legal areas, and a reminder that the consequences of legal decisions may not always be apparent.

The Facts

The Bank of Montreal (“BMO”) granted a line of credit to Mr. Phillips, guaranteed by Mrs. Phillips. After default, BMO obtained judgment and filed a writ of seizure and sale in late 2012 to enforce the judgment. Mr. and Mrs. Phillips subsequently separated. Mrs. Phillips then filed a proposal to her creditors under the *BLA* to compromise her debts, which proposal was accepted by her creditors on March 18, 2013. BMO received partial payment under its judgment and writ as a dividend, but was not made whole under the accepted *BLA* proposal.

This settled state of affairs was upended when the Phillips’ home was sold under power of sale by TD Bank, resulting in an unanticipated surplus (\$52,295.14). The question before the Court in this case was simple: was that surplus to be paid to Mr. Phillips, Mrs. Phillips, or BMO pursuant to its judgment and writ? TD paid the surplus into court and exited, stage left.

Mr. and Mrs. Phillips settled BMO’s claim for an additional payment of \$19,327.50 out of the surplus proceeds of sale of the home, leaving them to fight over the remaining \$32,217.64. Mr. Phillips argued that the remaining funds should be split equally, being payment of a joint debt, out of a joint asset. Mrs. Phillips argued that the *initial* surplus of \$52,295.14 was to be divided equally, and that the BMO payment should come out of Mr. Phillips’ share alone (resulting in most of the funds being payable to her). They had agreed that the payment to BMO was “without prejudice” to these positions.

The Court's Reasoning

The Court of Appeal sided with Mrs. Phillips, applying the *BLA*, the *Mortgages Act* and common law rules surrounding real property.

Mrs. Phillip’s proposal under the *BLA* had a similar effect to an assignment into bankruptcy: pursuant to section 69.1 of the *BLA*, all claims, actions and enforcement proceedings against her were forever stayed (stopped). This included BMO’s judgement and writ.

BMO could not execute on its judgment and writ against Mrs. Phillips; but it could still execute against Mr. Phillips, and the writ still attached to *his* interest in the property. This made BMO a “subsequent encumbrancer” within the meaning of under the *Mortgages Act*, which requires payment of “amounts due to the subsequent encumbrancers according to their priorities” (s.27).

But enforcement against Mr. Phillips’ interest alone still did not settle the issue.

He correctly argued that an enforcement of his debt alone would still result in an equal division, *if the execution was taken against real property held in "joint tenancy."* At common law, a joint tenant has a right to the entire property, or possibly none of the property - since the *other* joint tenant *also* has a right to the entire property. To quote the obligatory latin, *totem tenet et nihil tenet*: a joint tenant holds everything and nothing. A tenant in common, on the other hand, has a fixed share of the property. If BMO's execution was made against one *joint tenant*, it would be taken against the *undivided property of both tenants* (despite the stay against Mrs. Phillips). The joint tenants would share the residue equally. BMO's execution against a *tenant in common*, on the other hand, would only be taken from Mr. Phillips' fixed share, leaving Mrs. Phillips' residue intact (because her proposal had resulted in her debt to BMO being discharged).

The issue became: "Was there a joint tenancy or was it severed?" Joint tenancies require unity of title, time and possession and interest. Should any of these unities be broken (intentionally or otherwise), the joint tenancy will be severed and a tenancy in common created.

Did the *BLA* proposal sever the joint tenancy? No. An assignment in bankruptcy can have this effect, since the debtor's property is assigned to the Trustee (breaking unity of title). In a proposal under the *BLA*, on the other hand, Mrs. Phillips' assets remained vested in her.

Did BMO's execution sever the joint tenancy? Yes. An execution can have this effect, if the creditor goes further than just filing a writ and takes a step to enforce the writ (breaking unity of interest). The Court found that BMO's actions, appearing in court to contest the matter and receiving a payment pursuant to a "without prejudice" settlement with Mr. and Mrs. Phillips, were sufficient to constitute an execution of the writ.

What is curious is that the court did not consider the *timing* of BMO's "action." In real property law, emphasis is placed on timing (prior registration governs and trumps a later interest - including payment of surpluses under s. 27 of the *Mortgage Act*). Had the Court considered the existence of a joint tenancy *at the time of the sale*, which was prior to BMO's enforcement "action," the result would have been different.

In the end, however, the joint tenancy was severed and BMO's payment was taken from Mr. Phillips' fixed share of the tenancy in common. Mrs. Phillips received her share in full.

The Lessons to be Learned

What lessons can we learn from this decision?

- This decision emphasizes that joint debtors may be treated differently. A joint and several debt is payable by *any* of the debtors, and each can be liable for the full amount. Thus, where one invokes the protection of the *BLA* (or similar insolvency statute), the remaining debtor(s) could be left with the entire liability, as happened in this case.
- The Court did not address the agreement between Mr. and Mrs. Phillips that payment to BMO was "without prejudice" to their positions. Although unstated, this is consistent with the rule that parties cannot contract out of the *BLA*, which is for the benefit of *all* creditors.
- The "unfairness" from this decision appears to be that while Mrs. Phillips keeps *her* share of the joint asset, Mr. Phillips' share was taken. Which raises the question: was "equity" considered? While the courts have broad powers to apply equity as well as law, the Court correctly notes that equity cannot override the statutory scheme in the *BLA*. On the other hand, the initial debt was Mr. Phillips' debt - maybe the decision was intended to be "fair" after all.
- Finally, "joint tenancies" and "tenancies in common" are different. On the death of a joint tenant, the property passes to the surviving tenant without falling into the estate (avoiding attachment by creditors and estate taxes). Not so in the case of a tenant in common. Should a joint tenancy be severed unintentionally during legal manoeuvres, as happened to Mr. and Mrs. Phillips, the surviving spouse's interest can be compromised if the spouses were counting on joint tenancy rules to protect the surviving spouse. ■