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COURT OF QUEEN'S BENCH OF ALBERTA IN
BANKRUPTCY AND INSOLVENCY

JUDICIAL CENTRE OF

CALGARY

IN THE MATTER OF THE *BANKRUPTCY AND
INSOLVENCY ACT*, RSC 1985, c B-3, AS
AMENDED, the *JUDICATURE ACT*, RSA 2000, c J-
2 and the *PERSONAL PROPERTY SECURITY ACT*,
RSA 2000, c P-7

AND IN THE MATTER OF METRO PAVING AND
ROADBUILDING LTD., METRO PAVING LTD.,
METRO PARS CORPORATION and GRASSLANDS
OF BEISEKER DEVELOPMENT CORPORATION

APPLICANT

BANK OF MONTREAL

RESPONDENT

METRO PAVING AND ROADBUILDING LTD.,
METRO PAVING LTD., METRO PARS
CORPORATION, and GRASSLANDS OF
BEISEKER DEVELOPMENT CORPORATION

DOCUMENT

**REPLY BRIEF OF BDO CANADA LIMITED IN ITS
CAPACITY AS RECEIVER/TRUSTEE**

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COURT OF QUEEN'S BENCH OF ALBERTA IN
BANKRUPTCY AND INSOLVENCY

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IN THE MATTER OF THE *BANKRUPTCY AND
INSOLVENCY ACT*, RSC 1985, c B-3, AS
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TABLE OF CONTENTS

| | | |
|------|---|----|
| I. | INTRODUCTION & OVERVIEW..... | 4 |
| II. | LAW & ANALYSIS..... | 4 |
| | A. Trevcon and PCL have separate and distinct obligations to pay under the construction contracts and under the bonds | 4 |
| | B. Metro Roadbuilding is also a “Claimant” under the bonds | 6 |
| | C. Trevcon and PCL’s proposed third-party set-off is inappropriate and cannot be maintained within an insolvency proceeding | 7 |
| | 1. Test for equitable set-off has not been met..... | 8 |
| | a. No equitable grounds to protect against receiver/trustee’s demands for payment..... | 8 |
| | b. No clear connection and not manifestly unjust..... | 10 |
| | 2. Set-off in the context of a receivership/bankruptcy should be narrowly applied..... | 11 |
| | D. Construction project funds are not “trust property” under a labour and material bond | 12 |
| | E. Possible strategies to mitigate the quantum of any double payments..... | 12 |
| III. | CONCLUSION | 13 |
| | LIST OF AUTHORITIES..... | 14 |

I. INTRODUCTION & OVERVIEW

1. This reply brief (the “**Reply Brief**”) supplements the Receiver/Trustee’s brief dated June 3, 2021 (the “**Receiver’s Brief**”) filed in support of the Receiver/Trustee’s application for advice and direction, returnable on June 30, 2021.¹ This brief is filed by the Receiver/Trustee in reply to the briefs of Trevcon and PCL, filed June 24, 2021 (respectively, the “**Trevcon Brief**” and the “**PCL Brief**”). Terms not otherwise defined herein shall have the same meaning ascribed to them in the Receiver’s Brief and the Second Report of the Receiver dated May 31, 2021.²
2. The Trevcon Brief and PCL Brief raise several common issues and accordingly, the Receiver/Trustee’s reply is universal, except where so stated.
3. This Reply Brief addresses the following:
 - (a) Each of Trevcon and PCL have two separate and distinct mandatory obligations to pay Metro Roadbuilding under each of (i) their construction subcontracts with Metro Roadbuilding (the “**Construction Subcontracts**”) and (ii) under the Bonds (as Metro Roadbuilding is also a “claimant” under the Bonds). By conflating these distinct obligations, PCL and Trevcon respectfully misinterpret and misapply the relevant case law. Unless Trevcon and PCL are able to establish a valid defence to payment or a valid set-off right, there is no basis upon which to: (i) deny payment to Metro Roadbuilding’s estate under the Construction Subcontracts or the Bonds; and (ii) to treat the mandatory obligation to pay Sub-subcontractors under the Bonds differently than the mandatory obligation to pay Metro Roadbuilding under the Bonds, when both the Sub-subcontractors and Metro Roadbuilding are “claimants” under the Bonds.
 - (b) While “direct” set-off, once it is substantiated, is permissible in an insolvency proceeding, it is unclear whether “third-party” set-off is permissible in an insolvency proceeding. Trevcon and PCL’s proposed “third-party” set-off will have the effect of reducing the amounts owing by Trevcon and PCL to Metro Roadbuilding’s estate at the expense of the general body of Metro Roadbuilding’s creditors. PCL and Trevcon have not clearly established that the test for equitable set-off has been met, particularly in light of the decision in *APM Construction*.³ Furthermore, set-off remains an exception to the general priority regime in insolvency and thus the criteria for set-off should be strictly applied due to the impact on creditors of an insolvent debtor.
 - (c) Contrary to Trevcon’s assertion, labour and material payment bonds guarantee payment, but they do not impress a trust over the construction project funds. This is not a debate about one pool of funds. It is a debate about project funds on the one hand, and the funds available under the security provided by the Bonds. The project funds in the hands of PCL and Trevcon are not trust property of the Bonds.

II. LAW & ANALYSIS

A. TREVCON AND PCL HAVE SEPARATE AND DISTINCT OBLIGATIONS TO PAY UNDER THE CONSTRUCTION CONTRACTS AND UNDER THE BONDS

4. The Construction Subcontracts and the Bonds create two separate and distinct obligations pursuant to which Trevcon and PCL are liable to make payment to Metro Roadbuilding:
 - (a) PCL and Trevcon each have an obligation to pay Metro Roadbuilding under their Construction Subcontracts with Metro Roadbuilding; and

¹ Brief of BDO Canada Limited in its Capacity as Receiver/Trustee, filed June 3, 2021 [“**Receiver’s Brief**”].

² Second Report of the Receiver dated May 31, 2021 [“**Second Report**”].

³ *APM Construction Services Inc. v Caribou Island Electric Ltd.*, 2013 NSCA 62 [“**APM Construction**”].

- (b) PCL and Trevcon (or the sureties, where PCL and Trevcon have failed to pay) each have an obligation to pay “claimants” who have provided labour and material and who have not been paid for the same pursuant to either: (i) PCL/Trevcon’s obligation to do so; or (ii) a subcontractor’s obligation to do so. Proper “claimants” include both Metro and the Sub-subcontractors.
5. In their respective briefs, Trevcon and PCL appear to conflate their obligation to pay Sub-subcontractors and Metro under the Bonds with their obligation to pay Metro under the separate and distinct Construction Subcontracts. By conflating these obligations, PCL and Trevcon misinterpret and misapply the relevant caselaw in an effort to justify setting off amounts that they wish to pay to third parties against amounts properly owed to Metro.
 6. Trevcon and PCL have a mandatory obligation to pay Metro Roadbuilding for work performed under the Construction Subcontracts.⁴ However, there is no mandatory contractual obligation under the Construction Subcontracts requiring Trevcon and PCL to make payment directly to the Sub-subcontractors. In its brief, PCL suggests that Article 12 of PCL’s Construction Subcontract with Metro Roadbuilding gives PCL the discretion to pay the Sub-subcontractors directly.⁵ However, as correctly noted by Trevcon in its brief, the Alberta Court of Appeal in *Iona Contractors* has stated that “[a]fter bankruptcy, that discretion cannot be exercised in such a way that it disturbs the priorities in the *Bankruptcy and Insolvency Act*.”⁶ Therefore, such clause is unenforceable.
 7. The only instruments that contain mandatory obligations for Trevcon and PCL (and the sureties) to pay the Sub-subcontractors directly are the Bonds — each, a “freestanding contract” with its own obligations that are distinct from the Construction Subcontracts.⁷
 8. At paragraph 70(b) of its brief, in attempting to apply the Alberta Court of Appeal’s decision in *Iona Contractors*, Trevcon says that it has an “obligation to pay claimants” and that the obligation is “just that, an obligation there is no discretion or option and the requirement is clear and unequivocal”. Trevcon is absolutely correct that it has this obligation under the Morrin Bond. However, the Alberta Court of Appeal in *Iona Contractors* is clear that the obligation to pay under a labour and material payment bond cannot be imported and applied as an obligation under the relevant construction contract. The obligations are separate and distinct. The relevant paragraph making this distinction immediately follows the Court’s *obiter* cited by Trevcon at paragraph 69 of the Trevcon Brief:

[16] [...] if the owner had an obligation to pay the subcontractors, and not just a discretion, the result would be different.

[17] The appellant argues that even if the Airport Authority merely had a discretion (and not an “obligation”) to pay subcontractors under the contract, it does have such an obligation under the Labour and Material Payment Bond. The appellant argues that when the construction contract and the bond are read together, they disclose an obligation on the part of the Airport Authority to “mitigate” the exposure of the surety, which includes using the holdback funds to pay the subcontractors. Even if the agreements, when read together, disclose some intention to minimize the exposure of the surety, the private arrangements between the owner, the contractor, and the bonding company cannot affect the rights of third parties like the Trustee in bankruptcy and the secured creditor. Whatever rights the appellant may have were not registered at the Personal Property Registry, and cannot displace the rights of the secured party. Further, in Greenview the

⁴ Receiver’s Report at Appendix “K”; Affidavit of Tom Zavediuk sworn June 24, 2021 [**Zavediuk Affidavit**] at clauses D1 and D2; Affidavit of Lawrence Haddow sworn April 8, 2021 at Exhibit “D” (see payment terms of Metro Roadbuilding invoice, accepted February 9, 2019).

⁵ PCL Brief at para 33.

⁶ *Iona Contractors Ltd. v Guarantee Company of North America*, 2015 ABCA 240 at para 15 [**Iona Contractors**]; *Horizon Earthworks Ltd., Re*, 2013 ABCA 302 [**Horizon Earthworks**] at para 41; Trevcon Brief at para 68.

⁷ *APM Construction* at paras 60 and 61.

Court confirmed that the existence of a surety and a bonding arrangement did not change the outcome. [emphasis added]⁸

9. The Alberta Court of Appeal's decision in *Iona Contractors* appears to clarify that, in the current circumstances, payments made to Sub-subcontractors under the Bonds should not impact the rights of the Receiver/Trustee to collect the Trevcon Indebtedness and the PCL Indebtedness under the Construction Subcontracts. The "private arrangements" that PCL and Trevcon (both commercially sophisticated construction companies) made as principals under the Bonds are independent from the equally "private arrangements" that PCL and Trevcon had with Metro Roadbuilding (*i.e.*, the Construction Subcontracts). There is no *obligation* under the Construction Subcontracts for PCL or Trevcon to make payment directly to the Sub-subcontractors. That *obligation* only exists under the Bonds.
10. At best, PCL had a discretion to pay the Sub-subcontractors directly under its Construction Subcontract with Metro Roadbuilding, but the ability to exercise that discretion ended with Metro Roadbuilding's receivership/bankruptcy.
11. Thus, while the Receiver concedes that there is an obligation on PCL, Trevcon, and the sureties to compensate "claimants" (which includes the Sub-subcontractors) under the Bonds, such obligation does not supplant PCL and Trevcon's ongoing and independent obligation to pay Metro Roadbuilding under the Construction Subcontracts. These two mandatory and independent obligations likely mean that PCL and Trevcon will have to pay both the Receiver/Trustee and the Sub-subcontractors. Further, it also suggests that the concerns raised in numerous cases about third party set-off in insolvency proceedings remain legitimate and applicable.

B. METRO ROADBUILDING IS ALSO A "CLAIMANT" UNDER THE BONDS

12. Although Metro Roadbuilding's primary claim is a contractual claim under the Construction Subcontracts, Metro Roadbuilding also has a claim under the Bonds (which operates as a contract of guarantee) for the non-payment of its contractual claim under the Construction Subcontract. As such, in addition to making payment demands on Trevcon and PCL directly pursuant to the Construction Subcontracts, in January 2021 the Receiver/Trustee also submitted notices of claim under the Bonds.⁹
13. As Trevcon and PCL recognize in their briefs,
 - (a) the definition of "claimant" under the Morrin Bond includes a person "who has provided labour and material and who has not been paid for the same by the Principal or a subcontractor, in accordance with the Principal's or subcontractor's obligation to do so...";¹⁰ and
 - (b) the definition of "Claimant" under the Whistlers Bond includes "anyone who has a direct contract with the Principal or any Sub-Contractor of the Principal...".¹¹
14. Metro Roadbuilding has a direct contractual relationship with each of Trevcon and PCL, has provided labour or material under the Construction Subcontracts, and has not been paid (at least in part) for the provision of that labour or material. As such, Metro Roadbuilding clearly falls within the definition of "claimant" under the Bonds.
15. PCL and Trevcon do not appear to dispute that Metro Roadbuilding performed work under the Construction Subcontracts or that there are amounts owing to Metro Roadbuilding thereunder (subject to any available defences or rights of direct set-off). Rather, PCL and Trevcon assert that

⁸ *Iona Contractors* at para 17.

⁹ Receiver's Report at para 17.

¹⁰ Trevcon Brief at para 36.

¹¹ PCL Brief at para 17.

they are entitled to indirectly set-off the amounts paid to Sub-subcontractors under the Bonds against the Indebtedness owing to Metro Roadbuilding under the Construction Subcontracts.

16. While each of PCL and Trevcon also assert (or reserve the right to assert) an entitlement to claim “direct” set-off against Metro Roadbuilding’s estate on the basis of deficient work and warranty issues (among other things),¹² this “direct” form of set-off is not at issue on this application for advice and direction.
17. What is at issue is PCL and Trevcon’s entitlement to use the doctrine of equitable set-off to seek “third-party” set-off in the context of an insolvency, by trying to set-off amounts owing by them to Metro Roadbuilding’s estate against amounts paid by Trevcon/PCL to Sub-subcontractors.
18. While case law and subsection 97(3) of the *BIA* support the proposition that “direct” set-off is permissible in an insolvency (once substantiated), it does not support the proposition that “third-party” set-off is permissible.

C. TREVCON AND PCL’S PROPOSED THIRD-PARTY SET-OFF IS INAPPROPRIATE AND CANNOT BE MAINTAINED WITHIN AN INSOLVENCY PROCEEDING

19. As set out in the Receiver’s Brief¹³, the Supreme Court of Canada in *Husky Oil* stated that in the bankruptcy context:

the law of set-off allows a debtor of a bankrupt who is also a creditor of the bankrupt to refrain from paying the full debt owing to the estate, since it may be that the estate will only fulfil a portion, if that, of the bankrupt’s debt. [emphasis added].¹⁴
20. Additionally, the Alberta Court of Queen’s Bench has stated that in the insolvency context, “[b]ecause the effect of the set-off is to prefer one creditor over the general body of creditors, it is confined within narrow limits and the requirement of mutuality is rigorously enforced.”¹⁵
21. In the present case, Trevcon and PCL, who are not creditors of Metro Roadbuilding, are attempting to obtain a reduction of Metro Roadbuilding’s claims against them for amounts that Trevcon and PCL pay to Sub-subcontractors. In other words, Trevcon and PCL wish to claim set-off in a way that will reduce Trevcon and PCL’s obligations to Metro Roadbuilding at the expense of the general body of creditors of Metro Roadbuilding.
22. While PCL’s Construction Subcontract does contain a set-off clause¹⁶, that clause does not appear to cover the “third-party” set-off being contemplated here. PCL’s contractual set-off clause states that “... the Contractor’s obligation to pay the Subcontractor shall be reduced by, any claim of any nature or kind by the Contractor against the Subcontractor ...”.¹⁷ It is the Receiver/Trustee’s view that payments made by PCL to the Sub-subcontractors do not constitute a claim by PCL against Metro Roadbuilding.
23. Based on the foregoing, and because Trevcon’s Construction Subcontract did not contain contractual set-off language, in order to substantiate a valid set-off claim in these circumstances, both PCL and Trevcon must show that: (i) they meet the legal test for equitable set-off; and (ii) that “third-party” equitable set-off is applicable and appropriate in the context of a receivership/bankruptcy.

¹² PCL Brief at paras 12, 13 and 15; Trevcon Brief at para 17.

¹³ Receiver’s Brief at para 67.

¹⁴ *Husky Oil Operations Ltd. v Minister of National Revenue*, [1995] 3 SCR 453 (SCC) [*Husky*].

¹⁵ *FAST Industries Ltd. v Sparta Engineering Ltd.*, 2017 ABQB 240 [*FAST Industries Ltd.*] at para 21.

¹⁶ Receiver’s Brief at para 57; PCL Brief at para 56.

¹⁷ Report at Appendix “K”; *Zavediuk Affidavit* at Exhibit “B”.

1. TEST FOR EQUITABLE SET-OFF HAS NOT BEEN MET

24. The test for equitable set-off requires the following elements:¹⁸
- (a) The party relying on set-off must show some equitable ground for being protected against his adversary's demands;
 - (b) The equitable ground must go to the very root of the plaintiff's claim before a set-off will be allowed;
 - (c) A cross-claim must be so clearly connected with the demand of the plaintiff that it would be manifestly unjust to allow the plaintiff to enforce payment without taking into consideration the cross claim;
 - (d) The plaintiff's claim and the cross-claim need not arise out of the same contract; and
 - (e) Unliquidated claims are on the same footing as liquidated claims.
25. The PCL and Trevcon Briefs have not clearly established that
- (a) there are equitable grounds to protect PCL and Trevcon against the Receiver/Trustee's demands for payment; and
 - (b) the Receiver/Trustee's claim for payment under the Construction Subcontract and/or Bond are so clearly connected to PCL and Trevcon's obligations to pay the Sub-subcontractors under the Bonds that it would be manifestly unjust to allow the Receiver/Trustee to enforce payment without taking the payment to Sub-subcontractors into consideration.

A. NO EQUITABLE GROUNDS TO PROTECT AGAINST RECEIVER/TRUSTEE'S DEMANDS FOR PAYMENT

26. As described in paragraph 4 above, Trevcon and PCL have distinct legal obligations to (i) Metro Roadbuilding, under the relevant Construction Subcontracts; and (ii) "claimants" under the Bonds.
27. PCL and Trevcon assert that not allowing their "third-party" set-off claim would require them to pay the same amount twice "simply because of Metro's insolvency", which would be inequitable.¹⁹
28. PCL and Trevcon are not exposed to potential double paying "simply because of Metro's insolvency," but rather they and the sureties (who are all sophisticated parties) knowingly caused the Bonds to be issued with a broad definition of "claimant". The risk of a double payment exists both within and outside of an insolvency. For example, under any form of bond with such a broad definition of "claimant", there is a risk of double payment where a subcontractor takes money from the contractor and does not use it to pay Sub-subcontractors. While double payment is never ideal, it is not inherently commercially unreasonable or manifestly unjust, particularly where (as is the case here) the purpose of the bond is to entice subcontractors and sub-subcontractors to provide labour and materials to public projects on which no lien rights are available. In fact, double payment is the exact result that occurred in the Nova Scotia Court of Appeal decision in *APM Construction*.²⁰
29. In *APM Construction*, the successful bidder, APM Construction ("**APM**"), was required to obtain a labour and material bond that included a broad definition of "claimant", including "lower-tiered claimants". APM subcontracted parts of the work to Caribou Island Electrical Limited ("**Caribou**"), which, in turn, sub-subcontracted part of its work to Advanced Cabling Systems ("**ACS**"). Caribou

¹⁸ Trevcon Brief at para 95; PCL Brief at para 59.

¹⁹ Trevcon Brief at para 101; PCL Brief at para 54 and 58.

²⁰ See paras 35-39 of this brief for further detailed analysis of the commercial reality of paying twice.

became indebted to ACS, which gave notice to the surety of the labour and material bond that it would advance a claim for the amounts that Caribou had failed to pay.

30. Around the same time, the Canada Revenue Agency (“**CRA**”) served a Requirement to Pay on APM, seeking to garnish amounts that APM would otherwise have paid to Caribou for its subcontract work. APM paid a certain amount to the CRA in partial satisfaction of its claim, rather than paying Caribou.
31. Subsequently, APM applied to the court to permit the remaining amounts that it owed to Caribou to be paid into court and sought a declaration that its obligations to ACS had been discharged. At the same time, the surety sought a declaration discharging its obligations under the labour and material bond.
32. The Nova Scotia Supreme Court
 - (a) dismissed APM’s motion for an interpleader order;
 - (b) declared that ACS was entitled to payment from the surety under the bond;
 - (c) upon payment of such amount to ACS, released the surety from further liability to ACS; and
 - (d) determined that upon the payment to CRA of the money that APM otherwise would have paid to Caribou, APM had no further liability to CRA.
33. Since the surety then had the ability to seek indemnification from APM for the amounts that the surety paid to ACS under the bond, APM was put into the position that it had to pay twice for the same work because APM was liable to
 - (a) remit to CRA the money that otherwise would have gone to Caribou for its work; and
 - (b) indemnify the surety for the surety’s payment to ACS that resulted from Caribou’s failure to pay ACS.
34. The Nova Scotia Court of Appeal affirmed the Nova Scotia Supreme Court decision. While *Trevcon* refers to paragraphs 69 and 70 of *APM Construction* in its brief, it does not provide the full analysis and conclusion that includes paragraph 71 as well:

[69] While this is a very broad obligation, it is clear and unambiguous. When read in light of the rest of the contract, no ambiguities arise. “Claimant” is a defined term in the bond, as is “Contract”. Neither of these defined terms presents any difficulties when interpreting the wording of paragraph 4. In the absence of ambiguity, there is no need to apply *contra proferentem*. APM’s position that by making payment to its own subcontractor its obligation is null and void is simply not supported by the wording of the Bond.

[70] It is clear that paragraph 4 creates a freestanding obligation to pay third parties that are not a party to the Bond and have no contractual privity with APM. It does so by incorporating the broad definition of “Claimant” into the obligation in paragraph 4. This obligation is owed by the principal (and thus by the surety) to the obligee. It is extended to all claimants by the wording of the Bond.

[71] I recognize that this result creates a hardship for APM. Having paid Revenue Canada, it now must respond to ACS’s claim, essentially paying twice for the same work. However, the Province required APM to secure a labour and material payment bond as a precondition to it being awarded the construction contract. It intended that the protections contained within the Bond would be effective. Travelers knew that it could be called upon to pay under the bond, and APM knew it would have to indemnify the surety if a claimant was successful. Since ICI, the law of Nova Scotia, governing this Bond, has

included the risk of double payment. It is up to a bidder, if it so chooses, to include a contingency for that risk in the calculation of its bid price for a job with the wording of this Bond.²¹

[emphasis added]

35. In *APM Construction*, the Nova Scotia Court of Appeal recognized the potential double payment as an acceptable commercial result. There was no question that there was an obligation to pay the CRA. Since, because of the Requirement to Pay, Caribou did not receive the full amount of funds that it expected from APM and thus did not pay its debt to ACS, the labour and material bond could be called upon.
36. As noted in paragraph 34 above, the Court in *APM Construction* referred to the Nova Scotia Court of Appeal decision in *ICI Paints (Can.) Inc. v. J.M. Breton Plastering (1984) Co* ("**ICI Paints**") for the proposition that the law of Nova Scotia governing bonds with a broad definition of claimant include the risk of double payment.²² In *ICI Paints*, the Nova Scotia Court of Appeal held the surety under a labour and material bond separately liable to pay sub-subcontractors, who had not been paid by the subcontractors.²³ In that case, the Court noted that under the terms of such bond the surety guaranteed that all claimants shall be paid, which creates the possibility of double payment where the principal has paid the subcontractor who fails to pay its sub-subcontractor.²⁴ While recognizing this possibility, the Nova Scotia Court of Appeal highlighted the fact that "the parties are all experienced persons in the field."²⁵
37. It should also be noted that potential double payment by an "owner" is a legislated reality in Alberta under the *Builders' Lien Act*.²⁶ If the "owner" on a construction project in Alberta fails to retain the 10% Major Lien Funds prescribed by the legislation, the "owner" could be liable to pay that same amount twice.²⁷
38. To avoid possible double liability, the principals in *APM Construction*, and in this case Trevcon and PCL, could have negotiated carve-outs in the bonds, the underlying indemnity agreements, or built this risk into their price. Strangers to the labour and material payment bond (*i.e.*, the creditors of the insolvent estate) should not bear the consequences resulting from a principal either (i) failing to adequately account for a transactional risk, or (ii) knowingly assuming that risk but then attempting to avoid liability. Counterparties, lenders and other creditors rely upon the broad language of the bond in a variety of decisions, including decisions to extend credit.
39. The Receiver/Trustee is not aware of any equitable ground that permits a contracting party to simply escape the contractual obligations that it has bargained for because it does not wish to comply with them. A finding that PCL and Trevcon can set-off amounts paid to Sub-subcontractors under the Bonds, notwithstanding their distinct obligation to pay Metro Roadbuilding under the Construction Subcontracts, would be a more inequitable result than potentially forcing PCL and Trevcon pay twice for the same work. Such risk was both predictable and avoidable.

B. NO CLEAR CONNECTION AND NOT MANIFESTLY UNJUST

40. Another part of the test for equitable set-off requires that the cross-claim be so clearly connected with the demand of the plaintiff that it would be manifestly unjust to allow the plaintiff to enforce payment without considering the cross-claim.²⁸

²¹ *APM Construction* at paras 69-71.

²² *APM Construction* at para 71.

²³ *ICI Paints (Can.) Inc. v. J.M. Breton Plastering (1984) Co.*, 1992 NSCA 12 [**ICI Paints**] at para 11.

²⁴ *ICI Paints* at para 12 and 22.

²⁵ *ICI Paints* at para 12.

²⁶ RSA 2000, c B-7.

²⁷ See ss 18 and 25 of the *Builders' Lien Act*, RSA 200, c B-7.

²⁸ *Telford v Holt*, [1987] 2 SCR 193 (SCC) at para 35.

41. The claim that Trevcon and PCL are seeking to set-off against the amounts owing by Trevcon and PCL to Metro Roadbuilding's estate are not typical "cross claims". The proposed "third-party" set-off claim does not involve a debtor and creditor setting-off amounts mutually owed to one another. Rather, Trevcon and PCL are suggesting that by paying amounts that Metro Roadbuilding's estate owes to Sub-subcontractors, they are able to reduce their payments to Metro Roadbuilding under the Construction Subcontracts and the Bonds by a corresponding amount.
42. It is not clear to the Receiver/Trustee that "third-party" set-off constitutes a permissible basis for a claim of equitable set-off at all, particularly in the insolvency context. The Receiver/Trustee questions whether equitable set-off should be used as a mechanism to "rescue" sophisticated contracting parties from a bad commercial bargain. It seems unjust that the responsibility for any damages suffered by Trevcon and PCL as a result of payments made under the Bonds would be borne by the estate of Metro Roadbuilding.
43. The relief being sought by Trevcon and PCL is exactly what the court guarded against in decisions such as *A.N. Bail*²⁹ and *Horizon Earthworks*. As the Supreme Court of Canada stated in *A.N. Bail*, bankruptcy legislation would be disregarded and deprived of all meaning if a debtor of a bankrupt, instead of paying the trustee, were authorized by contract or other means to pay another creditor of the bankrupt as it saw fit.³⁰ This negative outcome would be realized if Trevcon and PCL could set off amounts payable under the Bonds against the separate and distinct obligations owed to Metro Roadbuilding under the Construction Subcontracts. Meanwhile, the important policy rationale behind the *A.N. Bail* and *Horizon Earthworks* decisions would be fulfilled by holding Trevcon and PCL to their bargains under each of these distinct obligations and rejecting their requested equitable set-off.

2. SET-OFF IN THE CONTEXT OF A RECEIVERSHIP/BANKRUPTCY SHOULD BE NARROWLY APPLIED

44. Set-off is an exception to the general priority regime in insolvency. Within the insolvency context, set-off should be strictly applied due to the impact on the secured and other unsecured creditors.³¹
45. The Trevcon Brief spends significant time discounting the decision in *FAST Industries Ltd.* simply because the type of set-off at issue was legal as opposed to equitable set-off.³² While the Receiver/Trustee acknowledges that *FAST Industries Ltd.* involved legal set-off, the following statements of the court at the outset of the decision were clearly made with reference to set-off generally and were not specific to legal set-off:
- (a) Because the effect of set-off is to prefer one creditor over the general body of creditors, it is confined within narrow limits and the requirement of mutuality is rigorously enforced;
 - (b) The longstanding policy reason for this limitation is that, notwithstanding section 97(3) of the *BIA*, the equitable rights of creditors cannot be undermined; and
 - (c) The competing policy objective of fostering continued relationships between restructuring entities or persons and their trading partners is trumped by the need to protect the integrity of the bankruptcy system.³³
46. The narrow limits on the use of set-off are also evidenced by the suspension of all set-off rights in the model form of Receivership Order³⁴ and its codification in section 97(3) of the *BIA*.

²⁹ *A.N. Bail Co. v Gringas*, [1982] 2 SCR 475 (SCC) [*A.N. Bail*].

³⁰ *A.N. Bail* at para 41.

³¹ *FAST Industries Ltd. v Sparta Engineering Ltd.*, 2017 ABQB 240 [*Fast Industries Ltd.*] at para 21.

³² Trevcon Brief at paras 98-100.

³³ *FAST Industries Ltd.* at paras 21 and 22.

³⁴ Alberta Model Receivership Order Template at para 9.

47. Another limitation on the exercise of set-off in a bankruptcy is that section 97(3) of the *BIA* is intended to apply only to set-off claims (including equitable set-off) that existed on or before the date of bankruptcy.³⁵ In this case, no amounts were paid by Trevcon or PCL to the Sub-subcontractors under the applicable bonds as of the May 12, 2021 date of bankruptcy, therefore no claim for equitable set-off existed as of the date of bankruptcy. Trevcon and PCL's requested equitable set-off relates to an obligation that arose post-bankruptcy, and is thus impermissible.

D. CONSTRUCTION PROJECT FUNDS ARE NOT "TRUST PROPERTY" UNDER A LABOUR AND MATERIAL BOND

48. In its brief, Trevcon indicates that labour and material payment bonds use "trust" language and that the Supreme Court of Canada in *Valard Construction* commented that such trust language creates an "express trust" for the benefit of a claimant under a Bond.³⁶ As such, Trevcon argues, payments made by Trevcon to the Sub-subcontractors are separate and distinct from the insolvency proceedings and are not "property" of Metro Roadbuilding.³⁷
49. Trevcon and PCL misinterpret the nature of the trust property under the Bonds. Labour and material payment bonds guarantee payment, but they do not impress a trust over the construction project funds. The labour and material payment bond is separate security, which provides the beneficiaries with the opportunity to receive payment up to the penal sum of the bond.
50. In *Valard Construction*, the Supreme Court of Canada confirmed that the trust property is "the beneficiaries' ability to claim and recover from" the surety any outstanding amounts owed where the principal fails to pay pursuant to the construction contract. Despite Trevcon and PCL's framing of the issue, this is not a debate about one pool of funds. It is a debate about project funds on the one hand, and the funds available under the security provided by the Bonds. The project funds in the hands of PCL and Trevcon are not trust property of the Bonds.
51. This is similar to seeking indemnity from an insurer. In this case, the sureties (and by reason of the joint and several language and the underlying indemnity agreements, Trevcon and PCL) act as indemnifiers to the Sub-subcontractors. As stated in *ICI Paints*, the surety guarantees payment to the Sub-subcontractors.³⁸ The funds held by the surety are not the funds used to pay for the construction project. They are two distinct pools of funds, with no connection to each other. The Sub-subcontractors have access to the surety's pool of funds where they have been left unpaid. The exposure to the Sub-subcontractors was a known risk that Trevcon and PCL, as sophisticated parties with substantial experience in the construction industry, were aware of when they entered into their respective construction projects.

E. POSSIBLE STRATEGIES TO MITIGATE THE QUANTUM OF ANY DOUBLE PAYMENTS

52. In order to mitigate the quantum of any double payment on the part of Trevcon or PCL, the claims of the Receiver (on behalf of Metro Roadbuilding) and the claims of the Sub-subcontractors should be considered contemporaneously so that the quantum of any accepted overlapping claims is consistent. Both the Sub-subcontractors and Metro Roadbuilding should be paid the same amount for the same work. If Trevcon or PCL wish to assert direct set-off claims for deficient work, Trevcon or PCL must meaningfully consult with both the relevant Sub-subcontractor and the Receiver on such matter, as the economic interests of both parties are engaged. If no mutual agreement between such parties can be reached, the matter can be brought before the Courts through a future

³⁵ *McKenzie (Trustee of) v McKenzie*, 2005 MBCA 35, paras 29-32.

³⁶ Trevcon's Brief at paras 30, 31, 43 and 54-57; *Valard Construction Ltd., v Bird Construction Co.*, 2018 SCC 8 at para 16.

³⁷ Trevcon Brief at paras 43 and 44.

³⁸ *ICI Paints* at para 75.

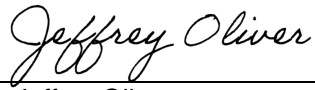
application. This process will ensure that Trevcon and PCL will only treat parties fairly in accordance with their contractual obligations, while not paying for proven deficiencies.

III. CONCLUSION

53. Based on the foregoing, the Receiver/Trustee requests this Court's advice and direction.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 29th day of June, 2021.

Cassels Brock & Blackwell LLP

Per: 

Jeffrey Oliver
Counsel for the Applicant, BDO Canada
Limited, in its capacity as Receiver/Trustee

LIST OF AUTHORITIES

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| 11. | <i>Valard Construction Ltd. v Bird Construction Co.</i> , 2018 SCC 8 | https://www.canlii.org/en/ca/scc/doc/2018/2018scc8/2018scc8.html |

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| 13. | Court of Queen's Bench of Alberta File Number 2101 00809, <i>Bank of Montreal v Metro Paving and Roadbuilding Ltd., Metro Paving Ltd., Metro Pars Corporation and Grasslands of Beiseker Development Corporation</i> , Consent Receivership Order dated January 20, 2021 | https://www.bdo.ca/BDO/media/Extranets/MetroGroupOfCompanies/Consent-Receivership-Order-filed-Feb-2,-2021-PDF.pdf |
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