

Bankruptcy: It's Not the End!

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Under the *Law of Property Act*¹, a mortgagee is limited to recovery of the property unless the mortgage is high ratio, insured by CMHC, or granted by a corporation. If one of these latter circumstances exist, then the mortgagee is entitled to both recovery of the property and a judgment against the mortgagor for the deficiency in the event that the amount owed under the mortgage exceeds the value of the property. The mortgagee can then take steps to collect on the deficiency judgment in order to make itself whole.

Unfortunately for mortgagees, the deficiency judgment is an unsecured debt, and if the mortgagor makes an assignment into bankruptcy, the mortgagee ends up lumped in with all of the other unsecured creditors ranking at the bottom of the distribution list of the bankrupt mortgagor's estate. If bankruptcy occurs, should the mortgagee give up? Is bankruptcy the end of the mortgagee's rights to collect? As with most things, timing (in this case, the timing of the bankruptcy) is everything.

In *CIBC Mortgage Corp. v. Stenerson*², the Donalds granted a mortgage to CIBC that CMHC insured. Subsequently, the Donalds transferred the property to the Stenersons. By operation of the Land Titles Act, the Stenersons became liable for payment of the mortgage. In March 1996, Cherie Stenerson assigned herself into bankruptcy. For seven months after the assignment, she continued to make the mortgage payments. In November 1996, the mortgage went into default, and in December 1996, Ms. Stenerson was discharged from bankruptcy. CIBC started foreclosure proceedings in February 1997. Because the amount owed under the mortgage exceeded the value of the property, CIBC was granted a deficiency judgment against Mr. Stenerson. The issue before the Court was whether CIBC was also entitled to a deficiency judgment against Ms. Stenerson given her bankruptcy.

The Court held that yes, CIBC was entitled to its deficiency judgment because Ms. Stenerson had affirmed the contractual relationship with CIBC by making the required mortgage payments during the bankruptcy.

The mortgagee's right to a deficiency judgment is therefore dependent upon the timing of the date of bankruptcy and the date that payments are made. If the default under the mortgage occurs before the date of bankruptcy and no further payments are made under the mortgage, then the mortgagee will be limited to recovery of the property and a declaration of the deficiency. The mortgagee will then be able to register a proof of claim in the bankruptcy for the amount of the deficiency, but will rank alongside the other unsecured creditors. However, if even one payment is made under the mortgage after the date of bankruptcy, the mortgage is affirmed and the mortgagee will be entitled to claim for both the property and any deficiency judgment against the bankrupt mortgagor. Bankruptcy is not always the end to the rights of creditors!

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1 R.S.A. 2000, c. L-7

2 1998 CarswellAlta 388 (Alta. Q.B.)