

Court of Queen's Bench of Alberta

Citation: Re Titan Investments Limited Partnership, (Judicature Act), 2005 ABQB 637

Date: 20050819
Docket: 0401-19905
Registry: Calgary

In the Matter of Titan Investments Limited Partnership, and Titan Genpar Inc, and Evolution Capital Management Ltd, and The Estate of David Comte, Deceased, and The Comte Family Trust and Predator Holdings Ltd.

In The Matter of the *Judicature Act*, R.S.A. 2000,
c.J-2 and Rules 467 and 468 of the Alberta Rules of Court

CLERK OF THE COURT

AUG 19 2005

CALGARY, ALBERTA

**Reasons for Judgment
of the
Honourable Mr. Justice G.C. Hawco**

INTRODUCTION

[1] This is an application by the Receiver of Titan Investments Limited Partnership ("Titan" or the "Partnership"), and certain of the unpaid investors of the Partnership (the "Investors Committee") (together, "the Applicants") for an Order declaring that redemptions made by Titan to certain of the investors in the Partnership (the "Overpaid Investors") are void as fraudulent preferences. The Applicants further request that the Order direct the Overpaid Investors to repay the full amount of the redemptions to the Receiver, failing which the Applicants shall be entitled to judgment against those parties that have not paid the amount of the redemption. In the alternative, the Applicants request that the Order direct the Overpaid Investors to repay the difference between the amount of their initial investment and the amount they received in redemptions (the "False Profits"), failing which the Applicants shall be entitled to judgment against those parties who have not paid the amount of the False Profits.

FACTS

[2] Titan was formed April 30, 2003, after which the existing partners of Comte Global Partnership became partners in Titan. Effective June 2, 2003, the partners of Prometheus Investments Limited Partnership ("Prometheus") and Tyche Investments Limited Partnership ("Tyche") became partners of Titan as well. Titan was represented as an investment vehicle whereby investor funds were purported to be pooled for the purposes of trading in the futures and

equities markets. Profits earned were to be returned to the investors pro rata. According to its prospectus (the "Prospectus") the goal of Titan was to "provide consistent net returns...in the range of 50% to 100% per year (at page 5)."

[3] Titan's general partner is Titan Genpar Inc. ("Genpar"). Genpar's sole shareholder was David Comte ("Comte"). Comte was also the President, head trader, and majority owner of Evolution Capital Management Ltd ("Evolution"). Evolution, in addition to being the initial limited partner of Titan, provided management services to Titan and acted as its trading advisor. In return, Evolution was to receive an incentive fee based upon a percentage of the increase in the value of Titan's assets. Comte was the directing mind of Titan.

[4] Individuals became investors in Titan by purchasing units of the partnership. Investors were cognizant that their investments were not in the nature of loans to Titan, but were investments in equity. Accordingly, each investor was aware that the net asset value of his or her units in Titan could go up or down depending on Comte's success in trading in the futures and equities markets.

[5] Comte held himself out to the investors as a highly successful trader. In the Prospectus, he claimed to have achieved returns of over 20% per month in his previous partnership operations. Titan, through Evolution and Comte, issued regular statements of account to investors regarding the financial status of the partnership. These statements indicated that Comte was achieving similarly high returns for Titan through continuous trading in futures. For example, a quarterly performance report for the period of July 1 through to September 30, 2004 indicated returns of 7.54% for July, 11.4% for August, and 11.24% for September. As of September 30, 2004, the year to date return was stated to be 77.64%, and the return since inception was reported to be 2,782.77%.

[6] On November 30, 2004, a notice was sent to some or all investors advising that Titan would be wound up. This notice was also placed on Evolution's website. Commensurate with the winding up during the fourth quarter of 2004, Comte paid full or partial redemptions to 87 of the investors at the price of \$29.25 USD per unit. The realization for investors who were paid out at this time ranged from an average of 242% to a maximum of 5,500%. In total, these redemptions aggregated approximately \$3.9 million USD.

[7] All was not as it appeared, however. Save one isolated trade made by Comte in May 2003 on behalf of Prometheus, Comte had not traded securities since February 2001, a full two years prior to the formation of Titan. Freeze orders were issued by the Alberta Securities Commission in December 2004, and shortly after the issuance of the orders, Comte committed suicide. In a suicide note left on his computer (the "Halt note"), he confirmed that he had not made any trades in nearly four years. He also admitted that he had operated Titan as a Ponzi investment scheme, and had stolen millions of dollars from partners investment accounts in order to "live the high life".

[8] Ponzi schemes are fraudulent investment schemes whereby individuals are enticed by a con-man or fraudster to make investments in an operation promising an unreasonably high rate of return. Once the first few investments are made, subsequent investors are enticed to invest partly through reported gains and partly through the high payouts to earlier investors. Ultimately, the con-man either spends or disappears with the remaining money, or the scheme collapses on itself as funds are exhausted by payouts to earlier investors.

[9] As Comte admitted, Titan was operated as a Ponzi scheme. The Partnership was a fraud from its inception. Comte reported to investors that his trading activities were generating extraordinary profits for Titan and its investors. In fact no profits were ever generated. Rather, partnership capital was depleted by Comte through the millions of dollars in fees he charged to the Partnership in his own name and in the names of Evolution and his wife, Janet Comte. The collapse of Titan was precipitated by the inquiries of the Alberta Securities Commission and, ultimately, by Comte's suicide.

[10] Comte has left numerous victims in his wake, including his wife and family. This application, however, concerns the status of the Titan investors. The values Comte ascribed to units in Titan were fictitious and never bore any relationship to the value of the underlying assets in the Partnership. When Comte made redemptions to investors in the Partnership at these fictitious rates, he was doing so with the funds and at the expense of the other investors.

[11] There is no evidence indicating why Comte, on behalf of the Partnership, made distributions of funds to certain investors and not to others in the fourth quarter of 2004. Investors who received these distributions from the Partnership had no knowledge of any fraud upon which the distributions were based, nor did they have any intent to participate in any fraud.

[12] There are more than 40 Titan investors who to date have received either no redemptions from the Partnership, or redemptions that are not sufficient to cover their initial investment in Titan (the "Underpaid Investors"). The receiver calculates that between \$2.3 million USD and \$4.5 million USD is currently available to distribute to these partners, resulting in an average realization of 45% of initial investment per Underpaid Investor, and a low of 33% realization. In contrast, those partners who received redemptions at fictitious unit prices, the Overpaid Investors, particularly in the fourth quarter of 2004, achieved average realizations of 242%, with a high of 5,500%. If, however, previous redemptions to investors are paid back to the receiver, and the funds are then redistributed to all investors *pro rata*, the receiver estimates that the realization per partner will be between 75% and 93%.

ISSUES

1. Are the redemptions made to the Overpaid Investors void as fraudulent preferences pursuant to the *Fraudulent Preferences Act*, R.S.A. 2000, c. F-24 (the "FPA")?
 - (a) Can the payment to the Overpaid creditors be challenged under s. 2 of the FPA?
 - (b) Can the payment to the Overpaid creditors be challenged under s. 3 of the FPA?

(c) How does s. 6 of the *FPA* affect the ability of the Applicants to recover from the Overpaid Investors?

2. Are the redemptions made to the Overpaid Investors void as fraudulent preferences pursuant to the *Statute of Fraudulent Conveyances*, 1571 (U.K.), 13 Eliz., c. 5 (the "*Statute of Elizabeth*")?
3. Are the redemptions made to the Overpaid Investors void as fraudulent preferences pursuant to the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "*BIA*")?
4. In the event that the redemptions are found to be void on any of the above grounds, must the Overpaid Investors repay the full amount of the redemptions, or may they keep amounts equal to the principle they invested in the partnership?
5. Does the defence of equitable change of position apply?

1. **The *Fraudulent Preferences Act*, R.S.A. 2000, c. F-24**

[13] The Applicants submit that they are entitled to recover a judgment against the Overpaid Investors, as the distributions to the Overpaid Investors constituted fraudulent preferences pursuant to the *FPA*. The Applicants rely on the following provisions of the *FPA*:

2. Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made
 - (a) by a person at a time when the person is in insolvent circumstances or is unable to pay the person's debts in full or knows that the person is on the eve of insolvency, and
 - (b) to or for a creditor with intent to give that creditor preference over the other creditors of the debtor or over any one or more of them, is void as against the creditor or creditors injured, delayed, prejudiced or postponed.
3. Subject to sections 6 to 9, every gift, conveyance, assignment, transfer, delivery over or payment of goods, chattels or effects or of bills, bonds, notes or securities or of shares, dividends, premiums or bonus in any bank, company or corporation, or of any other property, real or personal, made
 - (a) by a person at a time when the person is in insolvent circumstances or is unable to pay the person's debts in full or knows that the person is on the eve of insolvency, and

(b) to or for a creditor and having the effect of giving that creditor a preference over the other creditors of the debtor or over any one or more of them, is, in and with respect to any action that within one year after the transaction is brought to impeach or set aside the transaction, void as against the creditor or creditors injured, delayed, prejudiced or postponed.

5. In sections 2 to 4, "creditor" includes

(b) a cestui que trust or other person to whom liability is equitable only.

6. Nothing in sections 1-5 applies to

(a) a bona fide sale or payment made in the ordinary course of trade or calling to innocent purchasers or parties, or

(b) a payment of money to a creditor, or a bona fide conveyance, assignment, transfer or delivery over of any goods, securities or property, of any kind as above mentioned, that is made in consideration of a present actual bona fide sale or delivery of goods or other property or of a present actual bona fide payment in money, or by way of security for a present actual bona fide advance of money, if the money paid or the goods or other property sold or delivered bear a fair and reasonable relative value to the consideration for it.

10(1) One or more creditors may, for the benefit of creditors generally or for the benefit of those creditors who have been injured, delayed, prejudiced or postponed by the impeached transaction, sue for the rescission of, or to have declared void, agreements, deeds, instruments or other transactions made or entered into in fraud of creditors or in non-compliance with this Act or by this Act declared void.

(2) If, in an action under subsection (1), an amendment is made to the statement of claim, the amendment relates back to the commencement of the action for the purpose of the time limited by section 3.

11(1) If a gift, conveyance, assignment or transfer of any property, real or personal, that in law is invalid against creditors, was made to a person, and that person has sold or disposed of, realized or collected the property or a part of it, the money or other proceeds or that amount, whether further disposed of or not, may be seized or recovered in an action by a person who would be entitled to seize and recover the property if it had remained in the possession or control of the debtor or of the person to whom the gift, conveyance, assignment, transfer, delivery or payment was made.

(2) The right of seizure and recovery exists in favour of all creditors of the debtor.

(3) When the proceeds are of such a character as to be seizable under writ proceedings, they may be seized under the writ of any creditor and shall be distributed among creditors under the Civil Enforcement Act.

(4) Whether the proceeds are or are not of such a character as to be seizable under writ proceedings, an action may be brought for them or to recover the amount of them by a creditor, whether a judgment creditor or not, on behalf of that creditor and all other creditors, or any other proceedings may be taken that are necessary to render the proceeds or the amount of them available for the general benefit of the creditors.

(5) This section does not apply as against innocent purchasers of any of the property.

(a) Can the payment to the Overpaid creditors be challenged under s. 2 of the FPA?

In order to successfully impeach the payment to the Overpaid Investors under s. 2 of the FPA, the applicant must show (1) that there was a transfer of property, (2) by an insolvent person or a person who is on the eve of insolvency, (3) to a creditor, (4) with the intent of giving that creditor a preference.

Was there a transfer of property?

[14] The payment of the investment funds by Comte to the Overpaid Investors qualifies as a transfer of property for the purposes of the s. 2 of the FPA.

Was Comte insolvent or on the eve of insolvency?

[15] In order for a transaction to be impeached under the FPA, the debtor must have been either insolvent, on the eve of insolvency, or unable to pay the person's debts in full at the time that the transfer was made (*FPA s. 2(a); Alberta (Attorney General) v. Samuel Doz Professional Corp.* (1993), 9 Alta. L.R. (3d) 201 (Q.B) at para. 19). In interpreting the parallel provision under s. 3 of the FPA, Master Fundunk held that the section was to be read disjunctively, such that an applicant would only be required to prove one of either insolvency, eve of insolvency, or inability to pay debts in full (*Stihl Ltd. v. Motion Engine Services Ltd.* (1990), 106 A.R. 118 (Q.B.) at paras. 14 and 16). While the burden of proving this rests with the applicant, in *Clarke v. Sutherland* (1917), 37 D.L.R. 368, the Alberta Supreme Court, Appellate Division, held that "the same strictness ought naturally not to be required that would be demanded under other conditions (at 369)." Instead, an applicant need only prove facts that will warrant a reasonable inference of insolvency (at 369).

[16] There is a body of American case law holding that Ponzi schemes are insolvent from the moment that the first investment contract is entered into (see *Merrill v. Abbott (In re Independent*

Clearing House Co.), 77 B.R. 843, 871 (D. Utah 1987); *Martino v. Edison Worldwide Capital (In re Randy)*, 189 B.R. 425, 441 (Bankr. N.D. Ill. 1995); *Scholes v. Lehmann*, 56 F.3d 750 (7th Cir. 1995). Counsel for the Applicants submits that the operation of a Ponzi scheme will necessarily leave the debtor without sufficient capital from the inception of the scheme, and unable to pay its debts as they become due. There does not appear to be any Canadian authority on this point, and the Applicants submit that it is therefore open to this Court to adopt this approach. I find the American approach to be reasonable. It is apparent that there were never sufficient funds in the Partnership to enable Titan to pay out its partners at the alleged unit values of the partnership, and the scheme would have collapsed at any time that a sufficient number of investors demanded redemptions. I therefore adopt the American authorities and find that Titan, which was run as a Ponzi scheme by Comte, was insolvent from its inception.

[17] Additionally, I would find, based on the principles of equitable liability, that Titan was on the eve of insolvency during the fourth quarter of 2004. During the fourth quarter of 2004, the Alberta Securities Commission had issued freeze trading orders against Titan, and it was apparent to Comte, as the directing mind of Titan, that the Partnership was on the verge of collapse. Investors had been induced through Comte's fraud to invest in the Partnership. In equity, a transaction induced by fraud is voidable (John McGhee, ed. *Snell's Equity*, 31st ed. (London: Sweet & Maxwell, 2005), at 94). Had each of the investment transactions been voided, there would have been insufficient funds in the partnership to return each investor's principle, thus rendering Titan insolvent.

Was the transfer made to a creditor?

[18] Romaine J. held in *Krumm v. McKay et al.* (2003), 342 A.R. 169, 2003 ABQB 437 that "[u]nless specifically defined in a particular statute, the term 'creditor' bears the meaning ascribed to it in every day usage (at para. 29)." "Creditor" is not generally defined in the *FPA*. In *First Edmonton Place Ltd. v. 315888 Alberta Ltd.* (1988), 60 Alta. L.R. (2d) 122 (Q.B.), appeal adjourned 71 Alta. L.R. (2d) 122 (C.A.), McDonald J. held that the common law defines a creditor as "a person to whom a debt is owing (at p. 163)." I concur that this definition represents the everyday meaning of the word. The Applicants have acknowledged that the Underpaid Investors are not creditors in this everyday sense. The Underpaid Investors were aware that their investments were in the nature of equity rather than debt, and as such Titan does not strictly owe any debts to the Underpaid Investors.

[19] Section 5 of the *FPA*, however, stipulates that for the purposes of ss. 2-4 of the *FPA*, a "creditor" will also include "a cestui que trust or other person to whom liability is equitable only." Springman *et al.* write in *Fraudulent Conveyances and Preferences* (Toronto: Carswell, 2004) at 17-3 that in Alberta "other equitable obligees of the debtor are creditors who have status to commence actions to set aside preferences." Sections 2-4 of the *FPA* create the rights available to creditors under the *Act*, while ss. 10 and 11 give effect to those rights. As the Legislature did not stipulate that the expanded definition of "creditor" applied to the remedy granting provisions of ss. 10 and 11 of the *FPA*, counsel for the Respondents argued that the Legislature only intended to make the remedies under ss. 10 and 11 of the *FPA* available to creditors in the non-expanded

sense of the word. The Respondents submit that the Applicants therefore have no cause of action or remedy pursuant to the *FPA*, and their application under the *FPA* must be dismissed. In essence, the Respondents submission is that even if the distributions of funds made by Titan to the Overpaid Investors are found to be void as against the Underpaid Investors pursuant to ss. 2 and 3 of the *FPA*, the Underpaid Investors have no ability to seek a declaration that the distribution of those funds is void.

[20] I find that it cannot have been the intention of the Legislature to restrict the remedies under ss. 10 and 11 of the *FPA* to the unexpanded definition of "creditor." This would lead to an absurd result. The Respondents' suggested interpretation of the *FPA* must be rejected in favour of an interpretation that extends the remedies available under ss. 10 and 11 of the *FPA* to the expanded definition of "creditor" set out in s. 5. The purpose of ss. 10 and 11 of the *FPA* is to give effect to creditors' rights under ss. 2-4. It is difficult to see why the Legislature would expand the definition of a "creditor" if it did not intend to give those who fall within the expanded definition a remedy. The expanded definition would give those within it a mere illusory right. As Holt C.J. wrote in *Ashby v. White* (1703), 2 Ld. Raym. 938, 92 E.R. 126 "if the plaintiff has a right, he must of necessity have a means to vindicate and maintain it...indeed, it is a vain thing to imagine a right without a remedy (at 136)." I find, therefore, that the remedies available under ss. 10 and 11 of the *FPA* are available to Applicants who fit within the expanded definition of "creditor" set out in s. 5 of the *FPA*.

Do the applicants qualify?

[21] Having found that the remedies available under ss. 10 and 11 of the *FPA* are available to Applicants who fit within the expanded definition of "creditor" set out in s. 5 of the *FPA*, I now turn my mind to whether these Applicants are creditors within the expanded meaning of the word. Put differently, are the Underpaid Investors persons to whom Titan owed a liability in equity?

[22] I find that the Underpaid Investors are persons to whom Titan owed a liability in equity. Generally speaking, persons who make equity investments assume the risk that their investment may turn sour, and they may lose all or a portion of their principle without remedy. The Prospectus itself stated that risks "were many and great," and the parties to this action acknowledged that investors were fully aware that their investments in Titan were not loans, but were in the nature of an investment in equity. If this had been a simple case of an investment performing poorly, it is unlikely that the Underpaid Investors' would have had a remedy.

[23] This action is not, however, a case about a poorly performing investment. Rather, it is a case of innocent investors being induced by a fraudster to purchase units in a partnership that was fraudulent from its inception. There was never any intention on the part of Comte to operate Titan as a legitimate business enterprise. Rather, his intent was to "live the high life", by stealing from the monies investors had invested in the Partnership. It is a maxim of equity that "equity will not suffer a wrong to be without a remedy" (*Snell* at 94). At equity, fraud vitiates the consent of a party to a transaction, thereby rendering the transaction voidable (*Snell*, at 198). Since the

Underpaid Investors were induced by fraud to invest in the Partnership, the contracts they entered into with the Partnership are voidable, and Titan is liable in equity to the Underpaid Investors to the extent of the investor's investment of principle in the Titan.

[24] During this application there was some discussion regarding what the position of the Underpaid Investors would be *vis a vis* trade creditors if the Underpaid Investors were found to be creditors under the *FPA*. As Titan has no trade creditors, I do not need to consider this issue. It is best left to be decided on another day.

If so, did Comte intend to give that creditor a preference?

[25] In *Christensen (Bankrupt) v. Christensen* (1994), 166 A.R. 161 (Q.B.), rev'd on other grounds (1996), 184 A.R. 202 (C.A.), leave to appeal to S.C.C. refused, [1996] S.C.C.A. No. 394, Montgomery J. held that:

After reviewing the analysis of the Supreme Court of Canada in Part VII of the decision in *Hudson v. Benallack*, [1976] 2 S.C.R. 168; 71 N.R. 119; 21 C.B.R.(N.S.) 111, commencing at page 118, I am satisfied that s. 2 does not require a consideration of the intention of the creditors (at para. 18).

[26] Thus, I need only consider whether Titan intended to prefer the Overpaid Investors through the redemptions paid to them. The intent of Titan is to be ascertained by determining the intent of its governing mind, which is in this case is Comte (*Canadian Imperial Bank of Commerce v. Grande Cache Motor Inn Ltd.* (1977), 4 Alta. L.R. (2d) 319, (*sub nom. Hobbema Farms Ltd. v. Fowlis*) (S.C. (T.D.)) at 329) Furthermore, as Miller J. held in *Grand Cache*, "any allegation of fraudulent intent is a serious one and should not be found as a fact without the presence of substantial evidence on which to base such a finding (at 330)."

[27] There is no evidence to indicate why Comte chose to distribute funds to certain investors in Titan and not to other investors. The doctrine of pressure is not applicable, as there is evidence that in the last quarter of 2004 Comte ignored the requests of certain of the Underpaid Investors for redemption of their partnership funds, while redeeming the units of certain of the Overpaid Investors who had made no such requests. While it is impossible to determine why Comte chose to pay certain investors, I find that he did intend to prefer those investors that he paid out. His deliberate decision to ignore the requests of certain investors for redemption of their funds and to instead pay full redemptions to investors who had no made such requests is evidence of his decision to prefer the Overpaid Investors.

(b) *Can the payment to the Overpaid creditors be challenged under s. 3 of the FPA?*

[28] An applicant attempting to impeach a transaction under s. 2 of the *FPA* is not subject to a specific statutory time limit under the *FPA*. By contrast, an applicant seeking to impeach a transaction under s. 3 of the *FPA* must bring the action to impeach the transaction within one year of the date that the transfer occurred. However, an applicant seeking to impeach a

transaction under s. 3 of the *FPA* need not prove an intent to prefer. Rather, it is sufficient that the payment to the creditor had a preferential effect. In other respects, the requirements under s. 3 of the *FPA* are the same as the requirements under s. 2: there must have been (1) a transfer of property, (2) by an insolvent person or a person who is on the eve of insolvency, (3) to a creditor. Having already found a transfer of property by an insolvent person to a creditor, I do not need to repeat this analysis. If I am wrong, however, that Comte intended to prefer the Overpaid Investors, then I find that the redemptions to the Underpaid Investors made within one year of this action having been brought are void pursuant to s. 3 of the *FPA*.

(c) How does s. 6 of the FPA affect the ability of the Applicants to recover from the Overpaid Investors?

[29] In *Christensen (Bankrupt) v. Christensen* (1996), 184 A.R. 202 (C.A.), leave to appeal to S.C.C. refused, [1996] S.C.C.A. No. 394, the Alberta Court of Appeal held that s. 6(b) of the *FPA* was to be interpreted such that a payment of money would be exempt from the application of the *FPA* if the payment bore a fair and reasonable value to the consideration which gave rise to the obligation to pay (at para. 26). Thus, in *Christensen*, payments made by a bankrupt to his two brothers to fully discharge loans they had made to him were not fraudulent preferences under the *FPA*. While the debtor was insolvent at the time the payments were made, and the payments had a prejudicial effect on the ability of the other creditors to recover in the bankruptcy, the payments were exempt from the application of the *FPA* because they were substantially similar to the amounts they had loaned the debtor, and therefore the Court found that they bore a fair and reasonable value relative to the consideration.

[30] In *Stihl*, Master Funduk held that s. 6 of the *FPA* did not require “a penny for penny match in value between what each party gives to the other (at para. 62).” Rather, there must be a reasonable fit between the two. The burden of demonstrating that the payment bears a fair and reasonable value relative to the consideration lies with the party seeking to uphold the transaction (at para. 62).

[31] I find that the redemptions made by Titan to the Overpaid Investors do not bear a fair and reasonable value relative to the consideration. Section 6 does not exempt the redemptions from the application of the *FPA*. The Overpaid Investors achieved average realizations of 242% on their principle. Some Overpaid Investors achieved realizations of as high as 5,500% on their principle. The redemptions were calculated by Comte based on fictitious values he ascribed to units in Titan. In September 2004, shortly before the majority of redemptions occurred, Titan reported that the US dollar value per unit was \$28.04. In fact, a spreadsheet found on Evolution’s computer confirms that Comte was aware that the actual unit value of Titan at that time was approximately \$5.92 USD. In the fourth quarter of 2004, when the majority of redemptions occurred, Comte had fictitiously valued units in the partnership at \$29.25 USD. Realizations of between 242% and 5,550% based on units fraudulently valued at more than five times their actual value do not constitute fair and reasonable payments relative to the amounts the Overpaid Investors invested in the Partnership.

2. The *Statute of Elizabeth*

[32] In the alternative, the Applicants submit that the payments made to the Overpaid Investors are void as fraudulent conveyances pursuant to the *Statute of Elizabeth*. In *Goyan v. Kinash*, [1945] 2 D.L.R. 749 (Alta. S.C.), Macdonald J. confirmed that the *Statute of Elizabeth* was in force in Alberta (at 753).

[33] The basic principles respecting the application of the *Statute of Elizabeth* were set out by Clackson J. in *Proulx v. Proulx* (2002), 316 A.R. 150, 2002 ABQB 151. In order for the *Statute of Elizabeth* to apply, there must have been a conveyance of either real or personal property, and the conveyance must have had the effect of defrauding, hindering or delaying the settlor's creditors. It must also have been the intent of the settlor to defraud, hinder, or delay his creditors through the conveyance. Intent is inferred if there is little or no consideration for the conveyance, although this inference may be rebutted by evidence to the contrary. The inference of intent is strengthened if the settlor was insolvent at the time of the settlement, or if the settlement effectively rendered the settlor insolvent (at para. 14).

[34] Unlike the *FPA*, an applicant seeking to attack a conveyance under the *Statute of Elizabeth* does not need to be a creditor or other person to whom an equitable liability is owed. Rather, the *Statute of Elizabeth* "applies to conveyances made against 'creditors and others' (*Krumm* at para. 29)." In *Murdoch v. Murdoch et al.* (1976), [1977] 1 W.W.R. 16 (Alta. S.C.), Bowen J. held that the words "creditors and others" in the *Statute of Elizabeth* were "wide enough to include any person who has a legal or equitable right...by virtue of which he is, or may become, entitled to rank as a creditor (at 20)." In addition, there is no requirement under the *Statute of Elizabeth* that the debtor be insolvent, on the eve of insolvency, or unable to meet its debts as they become due (*Krumm*, at para. 35).

[35] *Bona fide* transfers for consideration are exempted from the application of the *Statute of Elizabeth*, provided that the transferees did not have knowledge of the fraud. An applicant attempting to use the *Statute of Elizabeth* to attack a transfer for value must show both that the transferor had the necessary fraudulent intent and that the transferee was privy to the fraud. (*Krumm*, at para. 15).

[36] The *Statute of Elizabeth* has broader application than the *FPA* in the sense that the *Statute of Elizabeth* does not require the transfer to be made to a creditor, nor does it require the transferor to have been insolvent at the time the transfer was made. Despite this, I find that the *Statute of Elizabeth* does not apply to the present case since Comte reserved no benefit to himself by paying out the Overpaid Investors.

[37] In *Mulcahy v. Archibald* (1898), 28 S.C.R. 523, Sedgewick J., writing for the unanimous court, held that "the meaning of the statute is that the debtor must not retain a benefit for himself (at page 529)." Similarly, in *Glegg v. Bromley* (1912), 3 K.B. 474 (C.A.), cited with approval by the Alberta Supreme Court, Appellate Division in *Anderson Lumber Co. Ltd. v. Canadian Conifer Ltd.* (1977), 77 D.L.R. (3d) 126, Fletcher-Moulton, L.J. wrote that "[t]he covenous

assignments referred to in the 13 Elizabeth are mock assignments whereby in some form or other the assignor reserves some benefit to himself...(at 485)." In *Anderson*, Prowse J.A. wrote for the Court that:

(as) there was no evidence to support the conclusion that the transaction was 'a mere cloak to secure a benefit to' (the debtor)...I am therefore of the opinion that the transaction is not caught by the *Statute of Elizabeth*. If it had the effect of preferring Anderson Lumber to other creditors, that by itself does not bring it within that statute as the statute is not directed against a debtor preferring one creditor over others (at 134).

[38] Counsel for the Applicants referred me to *Proulx* as an example of a case where a transaction was held to be invalid under the *Statute of Elizabeth* despite the fact that the debtor had not retained a benefit for himself. With respect, I disagree with counsel that the debtor in *Proulx* did not retain a benefit for himself. The debtor in *Proulx* transferred the land in question to his common-law wife and himself as joint tenants. He was able to continue to use the property as his own, thus retaining a benefit in it. Further, the transfer was done with the intent of putting his equity in the property beyond the reach of his existing and prospective creditors (at para. 5). I find that this is an additional benefit. As Comte retained no benefit by making the payments to the Overpaid Investors, the *Statute of Elizabeth* does not apply.

3. *The Bankruptcy and Insolvency Act*

[39] Counsel made submissions regarding the application of s. 95 of the *BIA*. The relevant sections of the *BIA* are:

- 2(1) "date of the initial bankruptcy event", in respect of a person, means the earliest of the date of filing of or making of
- (a) an assignment by or in respect of the person,
 - (b) a proposal by or in respect of the person,
 - (c) a notice of intention by the person,
 - (d) the first petition for a receiving order against the person, in any case
 - (I) referred to in paragraph 50.4(8)(a) or 57(a) or subsection 61(2), or
 - (ii) where a notice of intention to make a proposal has been filed under section 50.4 or a proposal has been filed under section 62 in respect of the person and the person files an assignment before the court has approved the proposal, or
 - (e) the petition in respect of which a receiving order is made, in the case of a petition other than one referred to in paragraph (d);

95.(1) Every transfer of property, every charge made on property, every payment made, every obligation incurred and every judicial proceeding taken or suffered by any insolvent person in favour of any creditor or of any person in trust for any creditor with a view to giving that creditor a preference over the other creditors is,

when it is made, given, incurred, taken or suffered within the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date the insolvent person became bankrupt, both dates included, deemed fraudulent and void as against, or in the Province of Quebec, may not be set up against, the trustee in bankruptcy.

(2) Where any conveyance, transfer, charge, payment, obligation or judicial proceeding mentioned in subsection (1) has the effect of giving any creditor a preference over other creditors, or over any one or more of them, it shall be presumed, in the absence of evidence to the contrary, to have been made, incurred, taken, paid or suffered with a view to giving the creditor a preference over other creditors, whether or not it was made voluntarily or under pressure and evidence of pressure shall not be admissible to support the transaction.

[40] In these circumstances, the initial bankruptcy event occurred on January 28th, 2005, when the Applicants filed a Petition for a Receiving Order against Titan. Thus, if s. 95 of the *BIA* is used, only those payments made after October 28th, 2004 can be attacked. A levy is also imposed when the *BIA* is used, and this further diminishes the funds available to the investors. Finally, s. 95 confers the right to attack a transaction using s. 95 of the *BIA* on the trustee alone. In *Canadian National Railway Company v. Harnett* (1979), 31 C.B.R. (N.S.) 203, the Newfoundland Court of Appeal held that

...if there were voidable or fraudulent transactions made...then the provisions of the Bankruptcy Act relative to such transactions operate only to the benefit of a trustee in bankruptcy. It is he only who can question the legality or propriety of these transactions for the benefit of creditors (at 204).

[41] A receiving order has not yet been granted against Titan, and thus no trustee has been appointed, and there is no one with standing to make a claim under s. 95 of the *BIA*. For these reasons, I decline to decide whether the redemptions made to the Overpaid Investors constitute fraudulent preferences within the meaning of s. 95 of the *BIA*.

4. Amount of Redemptions

[42] The Respondents submit that in the event that I find that the that the redemptions paid to the Overpaid Investors are void as fraudulent preferences, that the Overpaid Investors should only be required to repay the False Profits to the receiver. The Respondents make this argument on several grounds. First, they rely on *Carson (Re)* (1924), 55 O.L.R. 649 (S.C. (A.D.)), which they submit supports the proposition that the Respondents must only pay back the False Profits. With respect, I find that *Carson* does not support the principle that the Respondents must only pay back False Profits. *Carson* involved a debtor who misappropriated money from a trust fund, and then replaced the money shortly before he was declared bankrupt. The trustee attacked the repayment of the money to the trust fund as a fraudulent preference. The Ontario Supreme Court, Appellate Division, held that the restoration of the money to the trust fund was not a fraudulent

preference under the Bankruptcy Act because the intention of the debtor to yield to the dictates of his conscience negated his intention to prefer, and there was no intent to prefer on the part of the estate. The estate was entitled to keep the payments. The debtor in *Carson* misappropriated \$970 from the trust, and repaid \$970 to it. There was no false profit. Thus, I fail to see how *Carson* supports the Respondents' position, as no fraudulent preference was found and no false profits existed.

[43] The Respondents also rely on Mark A. McDermott's article "Ponzi Schemes and the Law of Fraudulent and Preferential Transfers" (1998) 72 Am. Bankr. L.J. 157, which addresses the law on this topic in the United States. McDermott writes that a "trustee pursuing an investor under this theory (fraudulent transfer law) generally will be limited to recovering the fictitious profits earned by the investor and will not be able to recover amounts representing a return of the investor's principle (at 160)." Unfortunately McDermott does not cite any authority for this proposition. Accordingly, without more, I am not prepared to adopt this position.

[44] While I am sympathetic to the position of the Respondents, neither the *FPA* nor the case law supports a finding that the Overpaid Investors should be entitled to keep their principle. The *FPA* states that transactions that are found to be fraudulent preferences are void. It does not provide that the preference will only be void to the extent of the excess paid to the creditor. It is open to the Legislature to enact such statutory reform.

5. Does the Defence of Equitable Change of Position Apply?

[45] The Respondents submit that in the event that I find that the redemptions to the Respondents were fraudulent preferences, then the equitable defence of change of position or estoppel should apply. In *Principal Group Ltd. (Bankrupt) v. Anderson et al.* (1994), 164 A.R. 81 (Q.B.), aff'd (1997), 200 A.R. 169 (C.A.), a case considering the applicability of the defence to s. 95 of the *BIA*, at the trial level Cairns J. cited the American definition of change of position set out in The Restatement of Restitution:

The right of a person to restitution from another because of a benefit received is terminated or diminished if, after the receipt of the benefit, circumstances have so changed that it would be inequitable to require the other to make full restitution (*Anderson*, at para. 178).

[46] In *Anderson*, Cairns J. found that the defence of change of position failed for a number of reasons:

I found that within the context of the *Bankruptcy and Insolvency Act*, and certainly with no knowledge or acquiescence by the recipients (at least those before me on this application), the payment was motivated by fraud, the result of which has been receipt of a wrongful payment by the beneficiaries and it would

therefore, in my view, be against public policy to allow the defence of change of position to succeed... (at para. 180)

[47] Counsel was unable to direct me to any authority that considered whether the equitable defence of change of position was applicable in the context of the *FPA* or the *Statute of Elizabeth*. Without deciding conclusively whether the defence of change of position applies to the *FPA* or the *Statute of Elizabeth*, I find that the defence is not available to the Respondents in these circumstances. First, as in *Anderson*, the Respondents received the payments as a result of a fraud, and therefore, on the authority of *Anderson*, it would be against public policy to allow the defence to apply. Second, any consideration of equity with respect to the Respondents would also have to include a consideration of equity with respect to the Underpaid Investors. It is a maxim of equity that "equality is equity" (*Snell*, at 102). The Overpaid Investors cannot therefore rely on the equitable defence of change of position to retain more than their equal share of redemptions from Titan.


Result

[48] The Applicants shall have an Order declaring that redemptions made by Titan to the Overpaid Investors are void pursuant to s. 2 of the *FPA*, and directing the Overpaid Investors to repay the full amount of the redemptions to the Receiver, failing which the Applicants shall be entitled to judgment against those parties that have not paid for the amount of the redemption.

Costs

[49] If necessary, counsel may speak to costs.

Dated at the City of Calgary, Alberta this 19th day of August, 2005.



G.C. Hawco
J.C.Q.B.A.

Appearances:

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Lisa J.P. Gaunt of Field LLP
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