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THE PROBLEM OF PRICE ADEQUACY IN FORECLOSURE SALES

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The author's thesis, made more compelling by the phenomena of Canada's recessionary period, is that a majority of provinces subscribe to liquidation processes on the forced sale of mortgageed property which fail to ensure the adequacy of the sale price. Whether a sale is effected in the judicial forum or under a power of sale, the problem of price adequacy, generated principally by the adherence to ineffective marketing techniques, will persist, regardless of the economic climate. The relative acuteness of the problem is revealed in those jurisdictions where the creditors are permitted to purchase their security. While the principal purpose of the article is to expose the problem and its cause, consideration is also given to formulating and applying a proper standard of care to be exercised by a mortgagee in carrying out a sale.

Selon l'auteur, et son assertion est encore plus à propos quand on considère la récession au Canada, la majorité des provinces donne son appui aux mesures de liquidation mises en place pour la vente forcée de propriétés hypothéquées qui ne peuvent assurer un prix de vente suffisant. Que la vente se fasse par une intervention judiciaire ou par un pouvoir de vente, le problème de l'insuffisance du prix, due avant tout à l'emploi de techniques de vente inefficaces, continuera quel que soit le climat économique. La situation apparaît d'autant plus critique dans les provinces où les créiteurs ont le droit d'acheter la propriété hypothéquée. Quoique le but de cet article soit principalement la présentation du problème et de ses causes, l'auteur considère aussi la formulation et l'application de certaines normes à suivre en cas de vente.

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Introduction

The purpose of this article is to expose certain structural weaknesses in the liquidation process generally followed in each province when realizing on debts secured by real property mortgages. Its primary concern is with the manner in which courts and creditors seek to ensure the adequacy of the monetary consideration for which real property is exchanged in a forced sale. Specifically, the article identifies those aspects of the sale process which are flawed and ineffective. The nature and scope of the marketing techniques presently used are found, in most instances, to be utterly incompatible with the objectives of a forced sale, whether pursued in a judicial forum or under a power of sale. An additional goal of the article is to establish the proper standard of care governing marketing and sale techniques and explore its application in a practical manner.

An examination of the marketing techniques employed in the majority of provinces, when coupled with the remedies available to the secured creditor, raises fundamental concerns as to the acceptability of a number of sale processes. The acute nature of the problem may be encapsulated in a simple question: should property be sold to the highest bidder at a public auction if the sole exposure to the market place consists of a few legal advertisements in a local newspaper? This question is posed to stimulate an examination of what otherwise might continue to be regarded as an acceptable and justifiable behaviour. It is of course only a sophistic device since it fails to acknowledge that there are other controls with respect to price prescribed by law or by statute. Their existence does not detract materially from the general thesis of the article. Moreover, the relevance of the central problem and the degree of its severity are strikingly exemplified in those provinces which permit the foreclosing creditor to purchase the property and to maintain an action for the deficiency.

I. The Effect and Relevance of the Recent Recession

While the objectives outlined are those common to traditional legal analyses, it is now trite to emphasize that they are responses to a problem which has its present stimuli in the economic problems of the late seventies and early eighties. But this is only true for those who have experienced the recent recession. Consequently, this phenomenon and its relevance will not be as readily apparent to future generations of readers unless by chance case law acknowledges the recent plight of debtors and creditors. Thus it is thought appropriate to outline the manifestations of economic instability which gave rise to the volume of litigation found over the last ten years. More important, these manifestations underscore the significance of the problem once it is acknowledged that governments did little to alleviate the hardship.

Undoubtedly for many Canadians the dramatic and unprecedented fluctuation in interest rates experienced between 1980-1982 has left an

indelible impression, comparable in impact to the rate of unemployment which has yet to return to a level which can be considered tolerable.¹ Erratic unprecedented high interest rates provoked political predictions as to the numbers of Canadians who upon renewal of their mortgages would ultimately lose their homes. While these predictions were inevitable they could not be substantiated because statistics on mortgage fatalities are not compiled on a national basis.² Nonetheless, from what little statistical data is available, one can say that in the years 1982-1985 the numbers of mortgages in serious default were significant.³

Few would draw an analogy, at least on a national level, between the effects of our "new depression" and those suffered during the 1930s. For example, as of February 1984 barely one per cent of the residential mortgages held by the chartered banks were in serious default.⁴ Moreover, that default rate has been continually declining ever since. Statistics compiled by Mortgage and Housing Corporation with respect to insured mortgages indicate a similar default ratio, although in the case of certain loans the rate is higher.⁵ Ten years ago such a delinquency rate did not give rise to concern.⁶ On the other hand, national percent-

¹ By way of illustration, the conventional mortgage interest rate stood at 10.4% in 1977; it rose to 18.2% in 1981, and 17.9% in 1982; fell to 13.3% in 1983; and in March, 1985 it was at 11.5%: Bank of Canada Review and Weekly Financial Statistics; Statistics Canada, Labour Force Survey (72-001) and Canadian Statistical Review (11-003E). In September 1981, institutional lenders were quoting an interest rate of 21.45%, the highest reached during the years 1981 and 1982: Canadian Mortgage and Housing Corporation, Canadian Housing Statistics, 1981-85.

² The writer was advised by officials of Canada Mortgage And Housing Corporation that statistics on foreclosures in Canada are not maintained on a national basis. Up until June 1980, the Mortgage Bankers Association of America undertook a quarterly delinquency survey, but it was discontinued due to declining responses by mortgagees surveyed and a lack of interest in the survey results. Accordingly there are no national statistics available with respect even to those who are experiencing financial difficulty.

³ During the period June, 1982 to March, 1985 the percentage of housing loans held by the chartered banks in arrears by three months or more was 0.66% in June, 1982, rising to a high of 1.02% in February, 1984, and declining to 0.79% in March, 1985. The peak period was late 1983 and early 1984, when over 8,000 loans were in default: Canadian Bankers' Association.

⁴ *Ibid.*

⁵ For example, assisted home ownership mortgages: see Canadian Mortgage and Housing Corporation, Canadian Housing Statistics, 1980-85.

⁶ See J.E. Hatch, *The Canadian Mortgage Market* (1975), Ministry of Treasury, Economics and Intergovernmental Affairs, Ontario, p. 112. While the delinquency rate was considered low the actual default rate was viewed as negligible. The reason for the disparity was based on the strong demand for housing at that time and because prices had been steadily increasing. If the borrower got into financial difficulty he sold his home. See also, J.P. Herzog and J.S. Earley, *Home Mortgage Delinquency and Foreclosure* (1970), National Bureau of Economic Research, New York, p. 24 *et seq.* for American statistics pertaining to foreclosure and delinquency rates between 1950 and

ages fail to convey the raw facts of the problem. With respect to the chartered banks, that one per cent figure represented approximately 8,500 homeowners. As of March 1984 banks held 32.6% of the residential mortgage market.⁷ Thus, if we assume that all lenders had experienced a similar default rate, we can estimate that approximately 25,000 Canadian homeowners were in arrears to such degree that foreclosure proceedings were a distinct possibility. It must also be acknowledged that the recent recession has had a greater impact on debtors in some of the provinces than in others.

While the national default rate hovered around one per cent in February of 1984, Alberta led the country with a figure of over three per cent, followed by British Columbia with one and a half per cent and Saskatchewan with .7 per cent.⁸ While these figures had not declined drastically by March of 1985, they had fallen in other provinces. For example, as of March 1985 Ontario's default rate fell by one half to one quarter per cent. However, the Alberta default rate was twelve times greater.

Politically, numbers alone demanded that some form of relief be found. Accordingly, when interest rates exceeded twenty per cent, both Saskatchewan and Federal governments reacted to the perceived hardship which faced homeowners renewing mortgages. Saskatchewan's Homeowners Protection Act,⁹ which came into effect on December 31, 1981, enlarged the criteria upon which a court could refuse to grant leave to commence foreclosing proceedings under the Land Contracts (Actions) Act¹⁰ where the security constituted the debtor's principal residence. Persons unable to make monthly payments based on the renewed rate were to be granted relief for a period of one year.¹¹

As a temporary measure the Federal government first announced the Canada Mortgage Renewal Plan in November of 1981 for the purpose of assisting homeowners renewing mortgages between September 1981 and November 1982.¹² Eventually, with amendments to the Housing Act in 1984, the Federal Government introduced the Mortgage Rate

1967 which support the observation that the recent recession had not reached a critical point.

⁷ Globe and Mail, September 4, 1984, p. B1 (Tor. & Nat. Editions), "Trust Firms Lose Mortgage Lead to Chartered Banks".

⁸ Source: Canadian Bankers Association.

⁹ S.S. 1981-82, c. H-4.2.

¹⁰ R.S.S. 1978, c. L-3, s.3(1).

¹¹ Relief was not granted in *Canada Trustco Mortgage Co. v. Moore* (1982), 22 R.P.R. 13 (Sask. Q.B.) and *Toronto-Dominion Bank v. Butler* (1982), 24 R.P.R. 129 (Sask. Q.B.). In both cases the inability to pay was not related to high interest rates.

¹² Assistance of up to \$3,000 per year, or special guarantees for the deferral of interest payments, should there have been equity in the home, were available. Where there was little or no equity, a non-taxable contribution was provided.

Protection Plan by which homeowners could obtain insurance against extraordinary increases in mortgage rates.¹³ Apparently this plan did not generate the interest anticipated and has been described as bringing too little, too late.¹⁴ However, such expedients were implemented to avoid foreclosure proceedings and do not attack the problem of price inadequacy where a sale does take place. The picture is further complicated by the fact that while defaults were on the increase market values were in decline.

The foreclosure experience suffered by Calgary homeowners in 1984 illustrates poignantly this facet of the market place.¹⁵ Canada Mortgage and Housing Corporation, estimated to have one-third of the foreclosures, came into possession of 1000 homes in that year and expected to obtain title to another 1000 in 1985 plus fifty apartment buildings.¹⁶ Between 1981 and 1985 house prices in this city dropped approximately forty per cent, which caused Canada Mortgage and Housing Corporation to withdraw 150 homes from the market in an effort to stabilize the situation. The immediate source of the problem stemmed from the large exodus of homeowners following the burst of the oil boom. For those who remained, their difficulties are reflected in the unemployment levels in this province, and given the dramatic fall in world oil prices one cannot expect this situation to improve.

The extent to which the numbers of foreclosures and the decline in market value have affected lending institutions is not measureable other than by examples such as the collapse of the Northland and Canadian Commercial Banks.¹⁷ But any concerns as to the financial hardship suffered by creditors will, in many instances, be unwarranted given the fact that insurance against such risk is commonplace and one which had matured to an extent unforeseen at the time when this fiscal arrangement was conceived.¹⁸

¹³ The plan provides for mortgage rate insurance for new or renewed mortgages valued up to \$70,000. The maximum premium is \$1,050 based on 1.5 per cent of the mortgage amount. When the mortgage is renewed the scheme will pay seventy-five per cent of the increased mortgage payment if it is more than two per cent over and ten per cent under the initial rate.

¹⁴ See *Toronto Star*, Saturday, September 1, 1984, p. E.5, "Mortgage Protection Plan Meets With Little Interest".

¹⁵ See *Globe and Mail*, Tuesday, February 5, 1985, p. B2 (Tor. & Nat. Editions), "CMHC Tries to Stabilize Market As Calgary Home Owners Leave".

¹⁶ It was estimated that the remaining two thirds were shared by the Albert Mortgage and Housing Corporation and private insurers.

¹⁷ Report of the Inquiry into the Collapse of the CCB and Northland Banks (August, 1986), Hon. W.Z. Estey, Commissioner.

¹⁸ In 1978, sixty-eight per cent of all mortgage commitments issued were for insured mortgages: G.S. Fields and B. Gershman (ed.), *Canadian Mortgage Practice Reporter*, vol. 1, p. 38-11, 12.

Under the Mortgage Insurance Fund administered by Canada Mortgage and Housing Corporation the total claims paid in 1981 amounted to \$400.7 million dollars, and in 1982 to \$213.7 million dollars.¹⁹ So far as the federal government is concerned, there is one further consequence of mortgage fatalities which is worthy of note and which strengthens the view that despite relatively low percentages of delinquent mortgage accounts there is justification for a renewed interest in this phenomenon. As of December 1982 the Fund was required to "borrow" \$341 million dollars from the government in order to meet obligations with respect to the \$29 billion dollars worth of insurance policies in force.²⁰ Turning to the private sector, we find that within a three year period the Mortgage Insurance Company of Canada lost \$178 million dollars.²¹ These amounts by themselves underline the significance of the problem of mortgage fatalities and price inadequacy.

The unsatisfactory performance of the economy has in recent years made self-evident the structural weaknesses of certain liquidation processes. However, the problem of price adequacy must be addressed through effective marketing techniques impregnable to fluctuations in conditions in the market place. Nevertheless, our recent economic history provides a convenient backdrop against which to examine and criticize judicial responses, or their absence, to the problem.

II. *The Immediate Source of the Problem—Marketing Techniques*

Any attempt to lay down the co-ordinates of an acceptable sale price requires an examination of the marketing and sale techniques whether prescribed by law or followed by custom. But even if one were to describe the paradigm process some would argue, correctly, that the problem cannot be resolved properly unless market failure is a recognized part of the equation. That particular concern will be addressed in due course,²² but for the moment it is necessary to isolate the immediate source of the problem, marketing techniques.

¹⁹ See Canada Mortgage and Housing Corporation Annual Report, 1982. These amounts do not reflect the fact that if the foreclosing creditor obtains title to the property it is reconveyed to the Corporation upon settling the claim. It should also be noted that between 1979 and 1984 the Federal Business Development Bank lost nearly \$300 million dollars on bad loans; see McLean's, August 19, 1985, p. 37.

²⁰ This deficit is attributed mainly to the charging of inadequate premiums in prior years with respect to the Assisted Home Ownership and Assisted Rental Programs; see Canada Mortgage and Housing Corporation Annual Report, 1982.

²¹ See Globe and Mail, Saturday, June 29, 1985, p. B10 (Tor. & Nat. Editions) and The Financial Post, October 12, 1985, p. 29, "MICC Coming Out of Its Slump". Much of the loss is attributed to the large number of defaults by Alberta homeowners.

²² *Infra*, the text commencing at footnote 188.

While foreclosure sales in Canada are effected by one of two procedures, the use of the American classification of foreclosure by judicial sale or by power of sale is convenient and minimizes misunderstandings. The former term connotes a sale pursuant to an order of the court or one which is conducted under its supervision. The latter refers simply to the situation where the secured creditor pursues a sale either privately or by way of public auction, but without resort to the courts.

The very nature of the power of sale itself dictates that there are endless possibilities as to how a sale may be achieved. Similarly, in the majority of provinces where the judicial process is followed, there is no assurance of uniformity in the directions of the courts. The discretionary powers granted ensure that variations will exist in the application of rules of procedure from one judicial district to the next. Nonetheless there is one facet common to all liquidation processes which is clearly identifiable. In each province it is evident that there has been a conscious effort to standardize and to adhere to unchallenged practices entrenched by custom and occasionally by statute.²³ Together they provide the basis upon which each sale process is to be judged.

A. The Judicial Sale

Six of the ten provinces use the judicial sale as either the primary or sole vehicle for disposing of real property: they are British Columbia, Alberta, Saskatchewan, Manitoba, Quebec and Nova Scotia.²⁴ The situ-

²³ Under Quebec's Civil Code, art. 2077, and Code of Civil Procedure, art. 670 and 683, the marketing requirements are rigid. Pursuant to ss. 126(3) and s. 129(7) of Manitoba's Real Property Act, R.S.M. 1970, c.R-30, the sale may be by auction or private contract, while the Registrar of Land Titles is empowered to require that notice be published once a week for three consecutive weeks. Subject to the direction that an upset price or reserve bid be set, Saskatchewan courts are free to direct a sale in any manner: The Limitation of Civil Rights Act, R.S.S. 1978, c.L-16, s. 5. Rule 689 of the Alberta Rules of Court dictates that notice must be published once a week for two consecutive weeks. Rule 47.08(1) of the Rules of Practice of Nova Scotia states that the property shall be sold in accordance with the advertisements of sale by the Sheriff or persons authorized by the Court to conduct the sale. Ontario's Rule 64.04(12) of the Rules of Civil Procedure merely states that the property is to be sold under the referee's direction.

²⁴ It is said that the contractual power of sale in British Columbia is seldom invoked—Law Reform Commission of British Columbia, Report No. 24: Report on Security Interests in Real Property (1974). But in those instances where the credit or has resorted to this extra-curial remedy both he and the courts have experienced difficulties; e.g., *South West Marine Estates Ltd. v. Bank of British Columbia* (1985), 65 B.C.L.R. 328 (B.C.C.A.). In recent years this remedy has been pursued in Alberta but not without difficulty: see *Femco Financial Corp. Ltd. v. Femco Ventures Ltd.* (1983), 27 R.P.R. 244 (Alta. Q.B.) and cf. *Province of Alberta Treasury Branches and Coopers & Lybrand v. Ryan Construction Ltd.* (1983), 43 A.R. 98 (Alta. Q.B.). In Manitoba there are two systems of land registration in operation. One provides for the registration of deeds under the

ation in Ontario is problematic for in recent years creditors have resorted to the power of sale as the dominant means by which to liquidate their debts because of delays met in processing foreclosure applications in the judicial forum.²⁵ However, since conversion to the extra-curial process is a phenomenon of the last five years and as the judicial sale remains in use, consideration of both sale processes is instructive.

Apart from British Columbia and Ontario, all of the provinces using the judicial sale ignore the reality that exposing property improperly to the market place and over an insufficient period of time fails to meet the primary objective of a forced sale. In practice, the time allocated for effecting a sale is that which is necessary for inserting legal notices of sale in a local newspaper. Generally, the notices are brief and are distinctively legal both in format and content. Rarely do they contain references to the marketable features of the property, although some efforts are made to replace the metes and bounds description with a civic address.²⁶ With one exception the sale is by public auction. The summary in Table I attests to sale processes which are as efficient as they are ineffective.

The practice in Alberta has been affected by the decision in 1984 of the Alberta Court of Appeal in *Canada Permanent Trust Co. v. King Art Development Ltd.*²⁷ That case left open the possibility of using sale methods other than the tendering process. As a result changes in foreclosure practices have been occurring which are neither to be found in statute nor readily identified by examination of case law. Accordingly, it should be understood that criticisms that are offered of Alberta practice are based solely on the tendering process. By comparison the judicial sale in Ontario and British Columbia is quite different with respect to the marketing and sale techniques adopted. Before 1974 the practice in Ontario was to proceed by public auction, preceded by the publication of a notice of sale once a week for three consecutive weeks in an appropriate newspaper. Although one text writer maintains that these

Registry Act, R.S.M. 1980, c.R-30, and is designated the "old system". The other provides for registration of title under the Real Property Act, *supra*, footnote 23, and is designated the "new system". Since most of the land in this province falls within the latter the practices surrounding foreclosure sales are restricted to debts secured by property within this system. Hence the quasi-judicial sale under the direction of the registrar of land titles provides the basis for analysis.

²⁵ It is estimated that between ninety to ninety-nine per cent of foreclosures are effected by resorting to the power of sale; see Ontario Law Reform Commission, (Law of Mortgages Project), Directors Report on Issues and Agenda (1982), p. 51.

²⁶ A typical notice of sale in Alberta, while concise, does make reference to a limited number of marketable features. Pursuant to Nova Scotia's Practice Memorandum #16, see Canadian Mortgage Practice Report, *supra*, footnote 18, pp. 74-401 *et seq.*, the advertisement must be concise and provide informative description so that the property can be readily identified. Aside from allegedly being informative, a concise advertisement is recommended because it reduces costs.

²⁷ [1984] 4 W.W.R. 587 (Alta. C.A.).

TABLE I

Province	Sale Mode	Marketing Precautions	Estimated Time In Which To Effect An Undefended Sale
Alberta	tender (1)	once a week for two consecutive weeks in a local newspaper (2)	two weeks to a month from receipt of tenders. A minimum of six weeks from date clerk fills out judicial sale notice is allowed for receipt of tenders.
Saskatchewan	public auction conducted by licensed auctioneer	one notice in local newspaper and five notices in "conspicuous places" (3)	one month
Manitoba	public auction conducted by licensed auctioneer	one publication in Saturday edition of Winnipeg newspaper and if land is outside this city one publication in an area newspaper (4)	one month
Quebec	public auction conducted by Sheriff	one publication in French newspaper (5) and one in Quebec Official Gazette	one month
Nova Scotia	public auction conducted by Sheriff	three publications in local newspaper (6)	six to seven weeks

(1) This sale mode simply encompasses the solicitation of offers which can be withdrawn prior to acceptance by the court; see *Allen v. Greaves* (1983), 44 A.R. 300 (M.C.).

(2) Rule 689(2) of the Rules of Court.

(3) *E.g.*; the Office of the Sheriff, Registrar of Court, Registrar of Land Titles.

(4) The sale documents do, however, provide for publication of more than one advertisement.

(5) Apparently, even if the property is in Montreal no advertisement is inserted in an English newspaper because of Quebec's language laws.

(6) The procedures set out in the Rules of Court are supplemented by practice memorandums which have been approved by a special committee of lawyers and judges of the Queen's Bench—see Practice Memorandums Nos. 16 and 20, set out in Canadian Mortgage Practice Reporter, Vol. 1, pp. 74-401 *et seq.*

procedures produced sales at "maximum expectation", in 1974 creditors began listing with real estate agents for reasons unconnected with the issue of price adequacy.²⁸ However, that fortuitous decision to list the property for sale is appropriate regardless of the reason for the change in practice. Claims that auction sales maximized price are of questionable validity.²⁹

²⁸ See G.W. Dunn, E.J. Freyseng, Marriott and Dunn—Practice In Mortgage Actions in Ontario (4th ed., 1982), pp. 193-194. The change in sale mode is attributed to the passage of the Land Speculation Tax Act, S.O. 1974, c. 17.

²⁹ See M. Stambler, Selling the Property, Law Society of Upper Canada, Department of Continuing Education, Mortgage Rights and Remedies—Power of Sale and Conveyancing Under Power of Sale (1981), p. I-23.

Today, only British Columbia adheres to a process which attempts to meet head on the issue of price adequacy. The Rules of Court in that province have been drafted in the widest of terms so as to enable the court to order a sale in any manner which is appropriate.³⁰ An examination of a typical order for sale reveals clearly an appreciation of the inherent problems associated with a defective sale process and a desire to avoid them.

The order permits the listing of property for private sale with a licensed real estate agent pursuant to an exclusive or multiple listing agreement. The price at which the property is to be sold and any terms of the sale (the offer to purchase) are subject to prior approval of the court. Provision is also made for the amount of the commission to which the agent will be entitled. The order further directs that any person in possession shall allow the foreclosing creditor to show the property to any prospective purchaser between specified hours and permits the posting of "for sale" signs.

There is one other facet of British Columbia practice which seeks to minimize the possibility of a sale at an undervalue. Where there is more than one secured creditor, the party having conduct of the sale will normally be the one with the least priority.³¹ For example, the third mortgagee will generally have conduct before the second and the second before the first. However, if it is felt that any sale is unlikely to generate surplus proceeds which could be applied against the debts of subsequent encumbrancers, then conduct will remain in the hands of the creditor with the most to gain. As might be expected, whether or not there is any equity in the property is sometimes in dispute and becomes an issue in

³⁰ Rule 43(4) provides that a sale can be effected by conditional contract, private negotiation, public auction, Sheriff's sale, tender or in any other manner. It should, however, be noted that since the decision in *Canada Permanent Trust Co. v. King Art Developments Ltd.*, *supra*, footnote 27, the masters in Alberta have a wide discretion as to the mode of sale.

³¹ *E.g.*, *First Western Capital Ltd. v. Taylor* (1980), 20 B.C.L.R. 149 (B.C.S.C.); *Commerce Capital Trust Co. v. Magna Investments Number One Limited* (1980), 21 B.C.L.R. 394 (B.C.S.C.), *aff'd, sub nom. Commerce Capital Trust Company v. Zimmerle* (1980), 23 B.C.L.R. 50 (B.C.C.A.). While Rule 48(4) provides that the court may appoint the person who is to have conduct of the sale, a subsequent encumbrancer may obtain conduct by other means. The first mortgagee may simply seek an order for foreclosure without indicating whether an order absolute or an order for sale will be sought. In such circumstances a second mortgagee may have commenced his own action and sought an order for sale, which is granted. This practice is discouraged and it is advised that the second mortgagee should make the application for sale in the first mortgagee's foreclosure proceeding; see *Canlan Investment Corporation v. Gibbons, Gibbons and Lengara Homecraft Incorporated* (1983), 42 B.C.L.R. 199, at p. 203 (B.C.S.C.).

Whether or not there is any equity in the property is sometimes in dispute and becomes an issue in the application for conduct of sale.

the application for conduct of sale. Even if a subsequent encumbrancer were given conduct of the sale it would not be unusual for the creditor who initiated the foreclosure proceedings to seek out potential purchasers.³² While this aspect of British Columbia practice is unique in Canada, it must not be forgotten that the possibility of another secured creditor having conduct of the sale is one which had been originally adopted in England. The practice differed, however, in that English courts looked upon the party with the least priority as the owner of the equity of redemption.³³

When compared to a judicial sale as pursued in the other provinces, it would be unwarranted to criticize British Columbia practice for it is quite evident that the foreclosure process is primarily concerned with protection of debtors when dealing with sale procedures and sale price.³⁴

B. The Power of Sale

The alternative to invoking the jurisdiction of the courts when liquidating a secured debt is to pursue a contractual or statutory power of sale. It is by this means that debts in Ontario, New Brunswick, Prince Edward Island and Newfoundland are liquidated. Dissatisfaction in Ontario with the judicial sale has increased the use of the private remedial process.³⁵ In comparison, when in 1919 the New Brunswick Court of Appeal held that the foreclosing creditor was permitted to buy in at his own sale, as though he were an independent third party, the power of sale had by 1921 overtaken the notion of pursuing the judicial process.³⁶ In Newfoundland a judicial sale is less likely to be sought because of the ease

³² *In Commerce Capital Trust Co. v. Magna Investments Number One Limited*, *supra*, footnote 30, conduct of the sale was given to the second mortgagee who was able to obtain a conditional offer of \$1,100,000. The foreclosing creditor, the first mortgagee, obtained an unqualified offer of \$1,025,000. The court accepted the lower offer.

³³ See E.L.G. Tyler (ed.), *Fisher and Lightwood's Law of Mortgage* (9th ed., 1977), pp. 386-387 and 409; R.L. Cootes, *Law of Mortgages*, vol. 2 (9th ed., 1927), p. 1073. The reasoning advanced for allowing the mortgager to have conduct of the sale was based on the notion that it was in his best interest to obtain the best price possible.

³⁴ This view is confirmed by A. McEachern (C.J.S.C.B.C.), *On Foreclosure Practice* (1983), 41 *Advocate* 583, at p. 595.

³⁵ See text, *supra*, at footnote 25.

³⁶ An examination of Royal Gazettes published prior to 1919 indicates clearly that the judicial sale was the norm. Subsequent volumes disclose its impending demise, so much so that by 1921 virtually all notices of sale were pursuant to the contractual or statutory power. In any event, the possibility of proceeding by judicial sale has been virtually eliminated by the decision of the Rules Revision Committee to exclude any procedure and substantive guidelines from the new Rules of Court which came into effect on January 1, 1982. See Civil Procedure Rules Revision Committee (Barristers' Society of New Brunswick), *Final Report* (May 1981), p. 39. However, foreclosure as an equitable remedy is theoretically possible.

in invoking the power of sale, while in Prince Edward Island the "time-honoured" practice has been for creditors to rely on that power.³⁷

It might seem premature to launch a discussion of marketing techniques in these provinces without first determining the standard of care required by the courts in the exercise of the power of sale. Nonetheless, the fact is that New Brunswick, Prince Edward Island and Newfoundland adhere to a process which would not meet any standard of reasonableness. In Ontario, there is sufficient case law from which to draw some conclusions on the precautions necessary to ensure the reasonableness of sale price. Nevertheless, it is still difficult to draw broad generalizations because of the very nature of the power.

Notwithstanding the provincial variations ranging from a contractual to a statutory and to a short form power of sale, it is common to all that no reference is made to the scope of the marketing precautions to be adopted, other than to provide for a sale either by public auction or by private contract.³⁸ The foreclosing creditor must decide which is more appropriate. Excepting Ontario, the standard practice limits advertising to the publication of notices of the impending auction. The description below sets out sale processes comparable to those pursued in the judicial forum and which are subject to the same criticisms.

Ontario's liquidation procedure may be characterized as non-conforming because it deviates from the traditional approach to effecting a forced sale. Accepted practice is to list the property for sale with a real estate broker.³⁹ The duration of the listing agreement is a matter left to negotiation in the case of an exclusive listing. Where the agreement is a multiple listing then it appears that the minimum period is ninety days.⁴⁰ Yet the decision to effect a private sale through the efforts of a broker does not render a sale impregnable. Whether or not the security is properly exposed to the market place and for a sufficient period of time are

³⁷ With respect to the difficulties encountered when pursuing a judicial sale in Prince Edward Island, see *Federal Business Development Bank v. Group Plus One Ltd.* (1985), 54 Nfld. & P.E.I.R. 267 (P.E.I.C.A.)

³⁸ In New Brunswick the credit or is required to publish a notice of sale on four occasions but since it is directed at the debtor and not the general public, it is unreasonable to conclude that marketing is limited to legal advertisements; see text *infra*, at footnote 171.

³⁹ See Stambler, *op. cit.*, footnote 29, p. I-29. Given the fact that liquidation by power of sale is a relatively recent phenomenon, the standardization of sale practices in this province may not be complete. In this regard programmes presented by the Law Society's Department of Continuing Education detail the law and the procedures in an attempt to achieve this objective and to ensure that sales are free of collateral attacks. Of the presentations to date, the materials prepared by Mr. Stambler are instructive.

⁴⁰ See Stambler *ibid.*, pp. I-30-31. This minimum period would appear to be set by the local real estate board.

TABLE II

Province	Sale Mode	Marketing Precautions Notices of Sale	Time In Which To Attempt A Sale
New Brunswick	public auction conducted by Sheriff (1)	once a week for four consecutive weeks in local newspaper; posting of three printed handbills and one publication in Royal Gazette (2)	six to eight weeks
Newfoundland	public auction or tender (3) conducted by solicitor for mortgagee	once a week for two to four consecutive weeks	six to eight weeks
Prince Edward Island	public auction conducted by Sheriff	once a week for four consecutive weeks	six to eight weeks

(1) At times the solicitor of the foreclosing creditor conducts the auction.

(2) The notices are required if the sale is in accordance with the statutory power but they are expressly directed at the debtor and anyone with a legal interest in the land. As of 1986 publication in the Royal Gazette is no longer required.

(3) If the tendering process attracts no acceptable offer the creditor may resort to holding a public auction.

concerns which will be addressed in considering the law governing the proper standard of care.⁴¹

C. Is There A Real Problem?

It should not be difficult to convince anyone that sales by legal advertisement are ill-suited to attracting a wide range of potential buyers. This *a priori* conclusion can be tested by asking whether any owner would be willing to consent to a sale based on the best price offered in these circumstances. Greater resistance would be encountered if the sale mode were limited to the public auction. More concretely, the deficiencies in sale processes are shown in the numbers of reported decisions in which the foreclosing creditor is the successful purchaser, and in the kinds of issues raised for judicial determination. Of course, if the demand for property exceeds supply, there is every possibility that sale prices will be adequate and that it will be unnecessary for the creditor to purchase its own security.

However, liquidation procedures should be able to protect all parties interested in the sale proceeds from fluctuations in market activity. Yet even in stable markets present sale practices will not necessarily

⁴¹ See text, *infra*, footnote 112.

guarantee the adequacy of sale price. For example in *Briand v. Carver*,⁴² decided in 1967, the court refused to confirm a sale and to grant a deficiency judgment when the property, valued at \$5,500 by the court, sold for only fifty dollars to the foreclosing mortgagee, leaving a deficiency of \$4,400. The court was prepared to confirm the sale, but only if the claim for a deficiency judgment were abandoned. The observations of the court as to the lack of bidders at the sale are instructive:⁴³

It is difficult to explain satisfactorily how it could happen that housing accommodation in the Halifax-Dartmouth area could, in times of housing shortages like these, be exposed for sale at public auction after advertisement over a five-week period in a newspaper. . . without creating any real interest in the public in attending the sale and in bidding for the property.

The answer may lie in the nature and contents of the advertisements, the state of repair of the building, its location, or possibly in the inadequacy of marketing property solely by way of legal advertisement.

Ultimately the crux of the problem can be reduced to a combination of bad marketing and a sale method derived from nineteenth century English practices; that is, the public auction. The popularity of this sale mode during that century can be traced to the view that it represented the least objectionable mode of disposing of property. Moreover, "[w]hen the sale [was] conducted it [was] the most effectual method of ascertaining and obtaining the market value of the thing to be disposed of".⁴⁴ This observation was based on the belief that advertising in public papers and the posting of informative handbills on town walls were effective marketing techniques. It was also felt, as it is today, that the publicity surrounding the public auction rendered the sale contract more secure than a private one. A public sale was considered to be a bar to any inquiry as to the adequacy of consideration.⁴⁵ Finally, the sale was conducted by a licensed auctioneer, most likely an appraiser, who acted as the agent for the vendor and who was therefore under the duty to obtain "the best price which such property is fairly worth, and not to sell for a less price or in a different manner than is specified in his instructions, if any are given".⁴⁶

Within this historical context the popularity of the public auction can be understood. But as new and more appropriate media emerged this sale mode has lost much of its relevance in England.⁴⁷ Nonetheless the public auction continues to play a dominant role in the liquidation of

⁴² (1967). 66 D.L.R. (2d) 169 (N.S.T.D.).

⁴³ *Ibid.*, at p. 180.

⁴⁴ J. Bateman, *Law of Auctions* (3rd ed., 1846), p. 3.

⁴⁵ *Ibid.*, p. 3, footnote F.

⁴⁶ *Op. cit.*, footnote 44, p. 139.

⁴⁷ See text, *infra*, footnote 181.

debts in a number of Canadian provinces. Unfortunately, what has been forgotten is the extent to which pre-sale procedures such as marketing provide the basis upon which one can judge the auction to be an effective method of sale.

III. *Ultimate Controls with Respect to Sale Prices*

In all provinces there are in place various control mechanisms designed to prevent sales at unacceptably low prices. But it must be emphasized that they cannot be regarded as acceptable substitutes for the adoption of appropriate marketing schemes. Nor can they be regarded as mechanisms which secure substantial justice for the parties, as they do not ensure that the best price is obtained in the circumstances.

In the judicial forum court confirmation of sale price, the use of appraisals and the setting of a reserve bid are well recognized control mechanisms. Under the power of sale, the standard of care prescribed by law serves as the ultimate safeguard, although in a public auction the creditor's right to establish a reserve bid could afford some protection. However, the manner in which the reserve bid is determined in both the judicial and extra-curial forum is invariably identical and hence subject to similar criticism.

A. *The Judicial Sale*

At a theoretical level the primary advantage in pursuing a judicial sale, as opposed to a private one, lies in the notion that judicial supervision ensures that the remedies of the creditor are pursued in an equitable manner and that the sale price is reasonable. But in some provinces confirmation proceedings are either no longer required or have become a formality where the sale is by auction and a reserve bid has been set. The differences between provinces effecting sales by auction and those which solicit offers provide a convenient opportunity for jurisdictional comparisons. The two provinces which have been chosen to prohibit actions on the covenant in defined circumstances require separate analysis with respect to this legislated solution to the problem of price adequacy.

(1) *Sales By Public Auction*

If court confirmation is unnecessary it is because the sale is by auction and a reserve bid is established. Nonetheless, the manner in which the reserve bid is determined sidesteps the issue under consideration. It is a virtual requirement in Manitoba that the foreclosing creditor set a reserve bid based on the amount of the outstanding indebtedness.⁴⁸

⁴⁸ As conditions precedent to the granting of an order for foreclosure absolute the creditor must have attempted a sale by public auction and the reserve bid, equal to the

If it is met, then the mortgagee is empowered to execute all necessary instruments to complete the sale.⁴⁹ On the other hand, Quebec law requires that a minimum bid equal to twenty-five per cent of the municipal assessment be offered.⁵⁰ If that is received then the Sheriff is obliged to give the purchaser a "certificate of sale".⁵¹ Neither of these approaches is acceptable and for straightforward reasons.

Manitoba's reserve bid, determined in relation to the outstanding indebtedness, bears no relationship to the value of the property, except perhaps by chance. If the reserve bid exceeds the value then the debtor's equity is jeopardized, but if the converse were true then a sale is unlikely, in which case the creditor would have to settle for a decree of foreclosure absolute. Quebec's requirement may be criticized as being inordinately low, regardless of whether or not assessed value reflects market realities. A sale at this figure is most likely to be sidestepped since the hypothecary creditor is able to buy in at his own sale.⁵² One can presume that this would be usual to ensure that a windfall does not accrue to a third party. At the same time such a practice must undermine the policy of having a minimum bid requirement in the first instance.

While both Manitoba and Quebec do not require sale confirmation, it is not clear whether this procedure is either necessary or is being religiously followed in Nova Scotia. Even under the former Rules of Court it was not judicially settled whether confirmation was necessary.⁵³ If such an order were sought, then the court could refuse to confirm the sale on the ground of fraud, mistake, misconduct by the purchaser, default in the proceedings or inadequacy of sale price. Otherwise, the auction sale produced a binding and enforceable contract between the court and the purchaser.⁵⁴ The changes brought about by the present Rules, together

indebtedness, must not have been offered. Consequently, a credit or not wishing to eliminate the option of pursuing an order for foreclosure absolute will undoubtedly undertake a sale within those guidelines even though the legislation permits a sale by private contract: see Real Property Act, *supra*, footnote 23, s. 129(2), (3).

⁴⁹ Real Property Act, *ibid.*, s. 127(1).

⁵⁰ Art. 670, C.C.P.

⁵¹ Art. 690, C.C.P.

⁵² See text, *infra*, footnote 132, as to the right of the hypothecary creditor to purchase.

⁵³ In *Pew v. Zinck*, [1953] 1 S.C.R. 285, the Supreme Court held that under Nova Scotia law a court had no jurisdiction to allow a mortgagor to redeem after a sale had been concluded but before conveyance and before a report had been made and approved by it. As to whether the report had to be confirmed, four members of the bench proceeded on the assumption that Rule 8 of Order 51, which permitted property to be sold upon order with the approbation of the court, applied (at p. 287). The fifth judge held that the rule, coupled with the established practice, required either the mortgagee or the Sheriff to apply to the court for its approval of the sale (at p. 304).

⁵⁴ *Ibid.*, at p. 289, and see also *Briand v. Carver*, *supra*, footnote 42.

with an examination of a typical order for "foreclosure and sale", do not reveal a confirmation requirement, although one court held that it was necessary.⁵⁵ Common sense requires that both the foreclosing creditor and in particular the purchaser would want the approbation of the court. On the other hand, if the foreclosing creditor is in a position to seek a deficiency judgment then the sale price will necessarily be subjected to judicial scrutiny. In such circumstances it seems that an order of confirmation is necessary.⁵⁶

Neither Nova Scotia law nor custom requires that either the court or the foreclosing creditor set a reserve bid. If one is set it is done at the instance of the foreclosing creditor and is often calculated on the basis of the outstanding indebtedness, and thus vulnerable to the criticisms made of Manitoba practice.⁵⁷ With respect to appraisals, they are required by the court, but only where an application for a deficiency judgment is sought after the auction.⁵⁸

Legislation in Saskatchewan dictates that any sale order must prescribe "such upset price or reserve bid as the court or judge deems proper having regard to all the circumstances".⁵⁹ However, it is the foreclosing creditor and his solicitor who initially determine this amount. It remains subject to judicial scrutiny but the manner in which it is determined in the first instance is not unlike that previously discussed. It is to be preferred that the reserve bid should cover the outstanding indebtedness as of the date of the anticipated sale and other allowable items.⁶⁰ However, if it is felt that the debt exceeds the value of the property then consideration is given to setting a bid ten to thirty per cent below fair market value on the basis that properties generally sell for considerably less than this amount.⁶¹ While an affidavit as to value is required those

⁵⁵ Rule 47.08(1) does not stipulate that the sale is subject to the approbation of the court. Rule 47.17(1) merely requires that a report of the result of the sale as prepared by the Sheriff and as verified by the solicitor of the mortgagee be filed. In *Nova Scotia Savings and Loan v. Hill* (1981), 45 N.S.R. (2d) 689, at p. 698 (S.C.T.D.), the court held that an application to confirm the sale should have been made.

⁵⁶ See Practice Memorandum No. 16, *op. cit.*, footnote 26, art. 7.

⁵⁷ Apparently some mortgagees do obtain appraisal evidence in order to set the reserve bid.

⁵⁸ In *Fidelity Trust Co. v. Keltic Home Improvements Ltd.* (1985), 68 N.S.R. (2d) 425 (S.C.T.D.), the court rejected the mortgagee's claim for the cost of an appraisal as the rules of Civil Procedure limited this item to cases where a deficiency was being sought and the purchaser was the mortgagee.

⁵⁹ The Limitation of Civil Rights Act, *supra*, footnote 23, s. 5.

⁶⁰ See G.A. Richards and Mr. Justice D.H. Wright, Foreclosure Actions, in Saskatchewan Bar Admission Course Materials, p. 35.

⁶¹ *Ibid.*

who are willing to swear an opinion do not appear to have the essential qualifications.⁶² It seems as though the reserve bid serves only to protect the interests of the foreclosing creditor. If the reserve bid is met then the confirmation of sale price is a perfunctory exercise

(2) *Sale by Solicitation of Offers*

In those provinces where the courts remain seized of the task of determining minimum acceptable sale prices there is scant authority as to the proper test to be applied. At best one can speculate as to a test encompassing "gross inadequacy". Thus where property worth \$1,100 was sold for twenty five cents or property worth \$5,500 was sold for fifty dollars, the courts refused to confirm the sale and grant a deficiency judgment.⁶³ In such instances the creditor was forced to accept a decree of foreclosure absolute. While sales at nominal prices are unacceptable, there is still the possibility that sale prices will be significantly less than the deemed market value, but incapable of being characterized as grossly inadequate. Even if one argues that the decision on price-acceptability must be left to the discretion of the court, that discretion cannot be exercised properly unless due consideration is given to the nature and scope of marketing and sale techniques followed.

British Columbia practice clearly supports this position, notwithstanding the difficulties in prejudging the adequacy of an offer. The onus rests on the creditor having conduct of the sale to satisfy the court that reasonable efforts have been made to effect a sale, and that the offer is a reasonable one. Accordingly, the court will be advised as to the advertising undertaken, the nature and length of the listing and any other information relevant to the approval of the sale. Appraisals are provided to enable the court to adjudicate, albeit subjectively, on the adequacy of any offers. "Walk past" or "drive past" opinions on value are viewed with scepticism unless, for example, they update an earlier appraisal.⁶⁴ Even then, the decision to confirm a sale in British Columbia is not easily rendered.

For example, in *Bank of Nova Scotia v. Nargang*⁶⁵ the only offer received came from a subsequent encumbrancer for \$46,000. Of the two appraisals produced, one provided for a fair market value of \$51,00 and the other for \$71,000. Because of the opposing opinions each appraiser

⁶² *Ibid.*, p. 105, where the affidavit as to value is made by the mortgage administrator of the foreclosing creditor, and p. 102, where the affidavit as to value with respect to an application for foreclosure absolute is made by the solicitor for the foreclosing creditor.

⁶³ *Canada Permanent Mortgage Corporation v. Jesse* (1909) 11 W.L.R. 295 (Sask. S.C.) and *Briand v. Carver*, *supra*, footnote 42. In both cases the purchaser was the foreclosing creditor.

⁶⁵ See MacEachern, *loc. cit.*, footnote 34, at p. 585.

was examined on his affidavit. The major factor contributing to the divergence related to the extent of repairs necessary to place the home in a reasonable state. The court reluctantly approved the sale for \$46,000, noting that the debtor himself had been unable to obtain a higher price prior to the application for an order for sale. Similarly, with respect to appraisals and sufficiency of an offer, the court in *Canada Trust Company v. Sundist Holdings Ltd.*, *Colclough*⁶⁶ refused to set aside a confirming order simply on the basis of an appraisal for \$380,000 when an offer of \$320,000 had been accepted. As is obvious, it is quite impossible to predict whether or not a sale will be confirmed, particularly since the decision may be influenced by the views expressed by other encumbrancers and by the debtor himself.⁶⁷

Ultimately one must assume that the courts in British Columbia are exercising their discretion in an equitable manner. That conclusion is justified by a review of the marketing and sale techniques required by the courts in the province and of those decisions where sale price has been an issue. For Ontario the writer has yet to conclude whether judicial sale practices would meet fully a standard of reasonableness, or whether they are comparable to practices in British Columbia. In the absence of evidence to the contrary, and because property is listed for sale, the Ontario process cannot be challenged.

Alberta's sale process raises the question whether a court in that province has sufficient and appropriate evidence upon which to determine the adequacy of offers. Alberta's Rules of Court require that an affidavit of a value be filed with the application for sale.⁶⁸ Since the marketing techniques do little to attract purchasers the court must rely heavily on appraisal value when determining the reasonableness of an offer where one is received. One amelioratory facet of Alberta practice derives from the fact that the sale price is not predetermined by way of a reserve bid. It is still possible for a court to adjudicate upon the reasonableness of offers relative to suggested market values, and reach an equitable solution.

Leaving aside an analysis of appraisal theory and its application to foreclosures, it can be said that expert evidence as to value is noteworthy in one respect: the disparate opinions of value placed before a court suggest the presence of a fundamental disagreement over principles of

⁶⁵ (1978), 6 B.C.L.R. 182 (B.C.S.C.).

⁶⁶ (1981), 29 B.C.L.R. 1 (B.C.S.C.). See also *Eaton Bay Trust Co. (Alberta) v. Riley* (1985), 60 B.C.L.R. 86 (B.C.C.A.); *Roynat Inc. v. Gallagher Restaurants Ltd.* (1983), 49 B.C.L.R. 270 (B.C.S.C.) where the court in each case carefully considered all of the relevant factors before approving the sale.

⁶⁷ E.g., *Commerce Capital Trust Co. v. Magna Investments Number One Limited*, *supra*, footnote 30.

⁶⁸ Rule 686(7). (Alberta's Rules of Court).

valuation. For example, in one Alberta case the court was presented with two detailed reports, one of which appraised the security at three times the figure offered in the second.⁶⁹

Such anomalies are marked where debtors have challenged a sale under a power of sale. In one case the true market value of the property fell to be determined on the basis of six divergent opinions while in another four disparate appraisals ranging from \$190,000 to \$240,000 were put before the court.⁷⁰ Often there is a distinction made between fair and forced market value. Of course, that distinction is valueless if comparative forced sales are employed to determine forced sale values, or because they reinforce the negative effect on the realizable price which such phrases as "mortgage sale" or "sale receiver" have on any purchaser, including the unsophisticated.⁷¹ They are *indicia* that there is a "killing" to be made.⁷²

(3) *Prohibiting Actions On The Covenant*

It is from within the economic and social conditions which existed during the Depression that one finds the *raison d'être* for prohibiting actions on the covenant in both Alberta and Saskatchewan.

The possibility of a foreclosing creditor obtaining an unrealistic deficiency judgment would be routine in an utterly depressed market. This occurs not only because of national, but also because of local economic conditions. For example, a farming community may be subjected to unpredictable and devastating changes in climate or market prices as has occurred in both provinces in recent years. One of the marked consequences of the Depression was the disruption of the formerly held concepts of market value. Even where buyers could be found, prices offered for land did not approach those obtainable in normal times and the amounts claimed in a deficiency action reflected this state of affairs.

⁶⁹ *C.I.B.C. v. 302359 Alberta Ltd.* (1985), 59 A.R. 153 (Alta. Q.B.). The court stated that *viva voce* evidence should have been introduced to resolve the conflict.

⁷⁰ See *Wood v. Bank of Nova Scotia* (1979), 10 R.P.R. 156 (Ont. H.C.), *aff'd*, 14 R.P.R. 1 (Ont. C.A.) and *Sterne v. Victoria & Grey Trust Co.* (1984), 49 O.R. (2d) 6 (Ont. H.C.) respectively.

⁷¹ This matter is even more complicated where the market comparison approach is employed to estimate the value of the property. If comparative forced sales figures are used, which in turn are based on sales prices conducted without regard to proper marketing techniques, then such valuations should be rejected. There is also the further problem of valuation which is undertaken in a negligent manner: *cf.*, *Cantwell v. Peterson* (1983), 25 R.P.R. 290 (B.C.S.C.); *Avco Financial Services Can. Ltd. v. Jakubiec* (1981), 22 R.P.R. 219 (Alta. Q.B.).

⁷² The Canadian Real Estate Association when prescribing guidelines with respect to Real Estate Advertising Standards (2nd ed., March '79), notes that by referring to an "estate sale" the implication is that property is being sold by a trustee and therefore the property might be obtained more cheaply.

One humane option was to eliminate the deficiency judgment, in particular where the common law allowed the foreclosing creditor to purchase and to maintain an action for the deficiency. The impact of such legislation on creditors was minimal, since one cannot draw blood from a stone. One American author, writing during the Depression, reported that one of America's largest insurance companies had obtained approximately \$4,000,000 of deficiency judgments in 1930 but had received less than \$5,000 in payment.⁷³

Saskatchewan's Limitation of Civil Rights Act⁷⁴ and Alberta's Law of Property Act⁷⁵ eliminate the right of a foreclosing creditor to pursue personal judgment with respect to certain debtors. Both Acts prohibit any action on the covenant and dictate that the right to recover the indebtedness is restricted to the property itself.⁷⁶ In both provinces the legislative protections extend only to non-corporate debtors.⁷⁷ However, there is one critical difference between the two pieces of legislation.⁷⁸ Saskatchewan's Act expressly limits its scope to purchase money mortgages. However, the Alberta equivalent is not restricted to this type of loan transaction and thus is much broader in scope.⁷⁹ Nonetheless, the

⁷³ See J.W. Brabner-Smith, *Economic Aspects of The Deficiency Judgment* (1934), 20 Vir. L. Rev. 719, at p. 723.

⁷⁴ *Supra*, footnote 23.

⁷⁵ R.S.A. 1980, c. L-8.

⁷⁶ The Limitation of Civil Rights Act, *supra*, footnote 23, s. 2(1) and Law of Property Act, *supra*, footnote 75, s. 41(1)(1).

⁷⁷ In both provinces litigation has arisen over the applicability of the legislation where the equity of redemption has been sold by a non-corporate debtor to a corporate debtor, or *vice versa*. In determining whether or not the benefits of the respective Acts are available the courts have looked at the status of the original mortgagor. See M.J. Trussler, *Foreclosure of Corporate Mortgages* (1983), 21 Alta. L.R. 262, at pp. 262-263; Richards and Wright, *op. cit.*, footnote 60, p. 6; *First City Trust Co. v. Syrnyk*, [1985] 5 W.W.R. 285 (Sask. Q.B.). However the Alberta legislature amended the Law of Property Act in 1983 and 1984 so as to protect the noncorporate purchaser of the equity of redemption where the original mortgagor was a corporation and so long as the property is being used for residential or farm purposes; see Law of Property Act, *supra*, footnote 75, s.42(1.1) and s.43.4(1).

⁷⁸ They also differ to the extent that the Saskatchewan Act provides that the corporate debtor may agree in writing to waive the benefits of the Act (which presumably is a condition of the loan) while in Alberta the limiting provisions are deemed inapplicable if the mortgage is given by corporation; see The Limitation of Civil Rights Act, *supra*, footnote 23, s.40(2) and The Law of Property Act, *supra*, footnote 75, s.43(1).

⁷⁹ Until 1984 Saskatchewan courts had held that the action on the covenant was only abolished in cases where the mortgagee was the vendor of the land; *cf.*, *Guarantee Trust Company of Canada v. Douglas*, [1982] 6 W.W.R. 178 (Sask. Q.B.). However, the legislation was amended in that year (S.S. 1983-84, c.44) with the effect of abolishing that distinction; see *Inland Trust and Savings Co. v. Lewandoski* (1984), 38 Sask R. 10 (Sask. Q.B.) with respect to the effect of the amendment on transactions completed prior to 1984.

distinction is gradually being eroded by the willingness of Alberta courts to limit the applicability of the relevant provisions.

This has been achieved by the development of the "substance over form exception".⁸⁰ Through this judicially imposed exception a number of creditors have been able to sue on the "covenant" and obtain judgment in cases where the loan is secured by a promissory note and a collateral mortgage.⁸¹ From the reports one can identify the types of transactions which remain subject to the legislation: purchase money mortgages and loans that were substantially secured at the time of the advance. Admittedly the latter category is more problematic.⁸² But for the purposes of this article the legislation of both provinces is deemed identical, if only because an analysis of Alberta case law on this issue would unrewardingly detract from the present inquiry.

The question remains today whether or not such legislative intervention is warranted. But without knowing either the impact which the abolition of actions on the covenant has had on lending institutions in these two provinces or exploring the possibility of adopting other legislative means by which to deal with price inadequacy generated by depressed market conditions, it would be presumptuous to embrace one solution as opposed to another.⁸³ What is relevant to this inquiry is the extent to which the problem of price inadequacy is not to be avoided by this legislative panacea.

First, the fact that the non-corporate debtor is protected against a deficiency judgment, whatever its impact, should not detract from the need to apply a more stringent standard of care. The problem of price

⁸⁰ The origin of the exception is *Clayborn Investments Ltd. v. Wiegert* (1977), 77 D.L.R. (3d) 170, 3 Alta. L.R. (2d) 295, 5 A.R. 50 (Alta. C.A.).

⁸¹ E.g., *Canadian Imperial Bank of Commerce v. Andrejcsik*, [1984] 3 W.W.R. 153 (Alta Q.B.).

⁸² See J.T. Robertson, Section 41(1)(a) of the Law of Property Act And Puisne Mortgagees (1987), 76 A.R. 326.

⁸³ The most obvious solution would entail a scheme of mortgage insurance for the benefit of borrowers, as opposed to the present situation in which it is the lender who obtains the benefits of the premiums paid by the former. The right of subrogation accorded the insurer in respect to any deficiency is perhaps one of the least known so far as consumers are concerned and one which should be addressed. If, however, the elimination of the action on the covenant is seen as an acceptable solution the following criticism demands attention. The distinction between a corporate and non-corporate debtor, albeit a convenient one, is arbitrary. For example, it does not accord generally with the goals of present consumer protection legislation in that it fails to consider the relevance of the purpose for which the mortgage loan is granted. By comparison, the American Uniform Land Transactions Act (West Publishing Co., Uniform Acts (1978), p. 9) abolishes deficiency judgments where security is given for the purpose of purchasing an owner-occupied residential dwelling; the investor, whether incorporated or not, must bear the risk of price inadequacy beyond the control of the creditor. As a matter of policy the consumer is to be protected.

adequacy should be of equal concern to the foreclosing creditor and subsequent encumbrancers as it is where the debtor is a corporate entity.

Second, not all non-corporate debtors are protected by the legislation. In Saskatchewan mortgages secured under the Federal Business Development Act are exempt,⁸⁴ while in Alberta the relevant provisions do not apply to a mortgage given under the National Housing Act.⁸⁵ Moreover, the latter exemption has been judicially extended to security taken by approved lenders and insured under that Act.⁸⁶ If the number of foreclosure actions in which the exceptions are applicable is significant, the protection afforded the non-corporate debtor may be more illusory than real. Regardless of the pervasiveness of the exceptions they, of necessity, undermine the objectives of the legislation and reveal the continued relevancy of the problem of price adequacy.

B. *The Power of Sale—The Standard of Care*

The development of the power of sale as an efficient means for liquidating a secured debt demands consideration of the duty to be exercised by the foreclosing creditor in realizing a proper price when effecting sale. However, the issue has never focused on whether or not a duty of care exists, but rather upon the standard of care to be observed by the foreclosing creditor. This standard is relevant equally to sales in the judicial forum, even though courts are not accountable for their decision other than by appeal. Given the century-long and continuing debate carried on in the reports surrounding the proper standard of care, a cursory historical analysis is warranted. This is all the more appropriate, given that in recent years creditors in British Columbia, Alberta and Manitoba have invoked this remedy, although not without difficulty.⁸⁷

(1) *England*

Initially English courts, in an attempt to prescribe the parameters of the obligation, viewed the answer as one dependent on the proper char-

⁸⁴ S.C. 1974-75-76, c.14.

⁸⁵ The Limitation of Civil Rights Act, *supra*, footnote 23, s. 45; The Law of Property Act, *supra*, footnote 75, s. 43(2).

⁸⁶ See generally *Thijssen v. Galusha* (1985), 59 A.R. 138 (Alta. Q.B.) and *Re Royal Trust Corp. of Canada and Vollan* (1985), 18 D.L.R. (4th) 312 (Alta. Q.B.), interpreting s. 43(2) of the Law of Property Act, *supra*, footnote 75. The exception provided under Saskatchewan's Housing and Special-care Homes Act, R.S.S. 1978, c.H-13, s. 39 has been narrowly construed; see *C.I.B.C. Mortgage Corporation v. Manson* (1984), 32 Sask. R. 303 (Sask. C.A.). *Thijssen v. Galusha*, *supra*, also decided that provincial agencies were not subject to the legislation. However, the Alberta Court of Appeal recently came to the opposite conclusion: *Alberta Mortgage and Housing Corporation v. Ciereszko* (1987), 77 A.R. 81 (Alta. C.A.). Leave to appeal to the Supreme Court of Canada was refused.

⁸⁷ *Supra*, footnote 24.

acterization of the mortgagor-mortgagee relationship *vis-à-vis* the power of sale. Since the development of the law of mortgages was paralleled by the evolution of the law of trusts it was inevitable that the mortgagee would be characterized as a quasi-trustee or fiduciary vendor. Ultimately, however, the analogy was rejected.⁸⁸ Accordingly, the issue was reformulated as follows: is a mortgagee, when exercising the power of sale, merely under a duty to act in good faith or in addition is he under a duty to take reasonable care to obtain a proper price?

The decisions have, in essence, turned on the type of conduct which has rendered the foreclosing creditor accountable to any affected party. While today one can argue forcefully that the creditor should be liable for any inadequacy in sale price caused by his negligence, it must be remembered that the courts of equity were asked to construct from the extant law innovative remedial alternatives. Their task was more complex given the fact that the notion of imposing liability for culpable conduct was until the 18th century a "skein of threads" and although the following century would see great strides in the assimilation of ideas in the search for a unifying principle, equity could not avoid the pains of growth.⁸⁹ Moreover, when the issue did arise, it did so surrounded by other considerations. Should the sale be set aside or should the debtor be awarded damages? If the former, what effect might such relief have on the viability of the sale process? If the latter, what type of conduct would render the creditor accountable? These are questions which must at least be explored if one is to appreciate the imposition of a standard restricted to good faith considerations. Nonetheless, an appreciation of these historical dilemmas does not justify a reduced standard today.

The pursuit of the answer to our principal question has generated a considerable volume of litigation, particularly in other debtor-creditor security relationships, and has attracted differing responses for nearly a century on both sides of the Atlantic. Yet it is only recently that we can say with some certainty that an answer can be given: a mortgagee owes both duties. This is true so far as English law is concerned, and there are strong indications that this same rule will be accepted in Canada.

It is quite impossible to reconcile the Anglo-Canadian authorities with respect to the linguistic subtleties used in prescribing the standard of care. Any chronological analysis of cases which attempts to do so will eventually run afoul of Viscount Haldane's perceptive remarks: "The

⁸⁸ The decision to reject the analogy of mortgagee as trustee with respect to the power of sale was made in *Farrar v. Farrars, Limited* (1888), 40 Ch. D. 395 (C.A.) and even then it took several decades to ensure full recognition of the break.

⁸⁹ "[B]ut till then [the 19th century] the history of negligence is a skein of threads, most of which are fairly distinct, and no matter where we cut the skein we shall get little more than a bundle of frayed ends."; P.H. Winfield, *The History of Negligence in the Law of Torts* (1926), 42 Law Q. Rev. 184, at p. 185.

consideration of cases which turn on particular facts may be useful for edification, but it can rarely yield authoritative guidance.”⁹⁰ To a degree that advice must be heeded, but it is difficult to ignore the English decision upon which the lower standard is premised and the one which has now, it is hoped, laid it to rest. By deliberately ignoring doctrinal argument as to which line of authority is correct or which is precedentially paramount, the issue can be seen as one of determining the justifications for prescribing the good faith standard. Unlike analyses in some areas of the law, the facts under consideration are extremely important in that whatever language is used to describe the standard, it is the actual result achieved in the circumstances which is instructive in determining future practices.

The decisions in the closing years of the nineteenth century of the English Court of Appeal and House of Lords in *Kennedy v. De Trafford*⁹¹ contain classic statements describing the foreclosing creditor's obligation as one of good faith. Here a mortgage given by two tenants in common went into default. The mortgagee was advised by his surveyor that it was unlikely that the property could be sold by public auction for an amount sufficient to pay the principal and interest, and accordingly he proceeded to advertise the property for sale by way of private tender. However, this technique did not attract purchasers. Eventually, one of the co-mortgagors offered to purchase the property himself for the amount owing on the condition that the mortgagee take back a mortgage for a substantial part of the purchase price. The mortgagee agreed to do so provided that he could not obtain a higher price elsewhere. Unable to obtain such a price, he sold the property under the power of sale to the co-mortgagor on the basis of his offer. Subsequently the trustee in bankruptcy of the other co-mortgagor commenced an action to have the sale set aside and for a declaration that a right to redeem existed. In the alternative, he claimed damages on the ground that the mortgagee had failed to obtain the market value of the property even though the price realized equalled the debt.

The trustee argued that the sale could be set aside on the ground that the co-mortgagor had fraudulently connived with the mortgagee to exclude him from any interest in the equity of redemption and on the ground that a co-mortgagor cannot buy his own property under the power of sale. These arguments were rejected by both appellate courts; and, given the reasonable efforts made by the mortgagee to sell the property,

⁹⁰ *Kreglinger v. New Patagonia Meat and Cold Storage Company, Limited*, [1914] A.C. 25, at p. 40 (H.L.). These remarks arose in the context of a mortgagor arguing that a collateral advantage which endured past the date of redemption is void *per se*. Lord Haldane discussed at length the historical reasons for the existence of the rule, which reasons, he felt, were no longer compelling.

⁹¹ [1897] A.C. 180 (H.L.), *aff'd* [1896] 1 Ch. 762 (C.A.).

so also was the claim that the mortgagee had acted negligently. In the Court of Appeal, Lindley L.J., who some eight years previously had held that a creditor owed both duties, now retreated from that earlier position.⁹² The good faith standard was now described in the following terms:⁹³

A mortgagee is not a trustee of a power of sale for the mortgagor at all; his right is to look after himself first. But he is not at liberty to look after his own interests alone, and it is not right, or proper, or legal, for him, either fraudulently, or willfully, or recklessly, to sacrifice the property of the mortgagor: that is all.

The House of Lords, while agreeing with the result, recognized the imprecision of such a formulation and deliberately avoided any attempt to define exhaustively all that might be encompassed to meet this standard.⁹⁴ Notwithstanding the apparent lack of certainty with respect to the parameters of this obligation, ultimately one must accept that the central issue is whether or not the good faith standard excludes accountability for negligent acts, that is the failure to adopt reasonable precautions or to carry them out in a non-negligent manner. When placed in this perspective, one must then ask what are the justifications for excluding the concept of negligence when determining the parameters of "good faith".

Those citing Lindley L.J.'s classic formulation often overlook this succeeding statement: "If it could be said in this case that the mortgagees had done any of those things, [acted fraudulently, willfully or recklessly] I can understand setting aside the sale".⁹⁵ When reviewed in this context, the attempt by the trustee in bankruptcy to have the sale set aside served only to conceal the corollary issue of whether the foreclosing creditor could be held accountable for failing to obtain a reasonable price due to inappropriate or inadequate marketing precautions, without necessarily affecting the position of a third party purchaser. To appreciate the significance of this dilemma one must read Lord Lindley's reasons for formulating the lower standard. These are all the more striking because they have been consistently ignored despite the lip-service paid to his judgment:⁹⁶

That there should be every facility for realizing mortgage securities is for the benefit both of those who want to borrow money on mortgage and of lenders. If mortgagees cannot realize their securities with comparative ease and safety, who would lend money on mortgage, and what would become of owners of property if their facilities of borrowing were destroyed by a strict, rigid application to powers of sale of principles which may possibly rest on very refined equities, but which are utterly inapplicable to ordinary business purposes?

⁹² *Farrar v. Farrars, Limited*, *supra*, footnote 88.

⁹³ *Supra*, footnote 91, at p. 772 (C.A.).

⁹⁴ *Ibid.*, at p. 185 (H.L.).

⁹⁵ *Ibid.*, at p. 772 (C.A.).

⁹⁶ *Ibid.*, at p. 773 (C.A.).

Such reasoning may have married well with the non-articulated economic philosophy of the courts at that time, particularly when viewed in light of the problems which had been encountered by creditors in securing an efficient means for liquidating a debt. Further, one might speculate that there were other underlying policy reasons for restricting the duty to good faith and excluding liability for negligence, reasons which were subconsciously embraced when choosing the term, "comparative ease and safety". The following explanations are offered.

It is not until the mid twentieth century that we find a willingness to speak of the creditor's failure as an example of legal negligence. During the preceding century the debtor's typical recourse was to seek an accounting for all monies received and that which should have been received by the foreclosing creditor. If because of identifiable "error" on his part a lesser sum was received, the creditor would be held accountable for the shortfall.⁹⁷ The right to an accounting was an acceptable means of assessing the conduct of the creditor without breaching equity's prejudice against awarding damages.⁹⁸ Moreover, the nineteenth century saw developments in other areas of the law which expressly rejected the notion that a person who acts negligently acts in bad faith and this may have influenced the courts in *Kennedy*. Two prime examples are examined below.

According to the law of negotiable instruments, codified by the Bills of Exchange Act⁹⁹ of 1882, a holder in due course was deemed to have acted in good faith provided that he acted honestly. Mere negligence, not amounting to wilful or fraudulent blindness, did not alter this conclusion.¹⁰⁰ In 1889 a concordant result was achieved by the House of Lords in the classic case of *Derry v. Peek*,¹⁰¹ which held that a false statement honestly believed to be true did not constitute fraud. More germane to our central question is the finding that even if the statement was made carelessly and without reasonable grounds a common law action for damages did not lie. Thus it is not surprising to find equity

⁹⁷ *E.g.*, *Tomlin v. Luce* (1889), 43 Ch. D. 191 (C.A.). The issue in this case turned on the amount for which the mortgagor would be liable for misdescribing the property to the purchaser.

⁹⁸ Even though under the Chancery Amendment Act, 1858, 21 & 22 Vict., c.27 (Lord Cairns' Act), a Court of Equity was given a limited power to award damages and even though the Judicature Act, 1873, 36 & 37 Vict., c.66, reinforced that position, there is still a concern as to whether or not a court exercising its equitable jurisdiction should award damages in terms of negligence law. The proper remedy is one of accounting: see R.P. Meagher, W.M. Gummow, and J.R. Leane, *Equity - Doctrines and Remedies* (1975), p. 47 *et seq.*, discussing the so-called "fusion fallacy".

⁹⁹ Bills of Exchange Act, 1882, 45 & 46 Vict., c.61, s. 90 (U.K.).

¹⁰⁰ Per Lord Blackburn in *Jones v. Gordon* (1877), 2 App. Cas. 616, at p. 628 (H.L.).

¹⁰¹ (1889), 14 App. Cas. 337 (H.L.).

choosing a solution with which it was both familiar and which had been earlier accepted at law.

An additional reason for adopting the lower standard may have stemmed from the fear that a higher expectation might be regarded as saddling the creditor with the obligation to postpone the sale until such time as a better price could be obtained. For "as a general rule a trustee sufficiently discharges his duty if he takes in managing trust affairs all those precautions which an ordinary prudent man of business would take in managing similar affairs of his own".¹⁰² The trust analogy, if it had persisted, would have perpetuated this view and thus a creditor would have been unable to liquidate his security with ease. Ultimately it may well have been the prospect of having to set aside a sale if a higher standard of care were to be imposed which determined the outcome.¹⁰³ The result would have been to discourage third parties from involvement in any sale. This rationale is by far the most compelling when it is realized that Courts of Chancery had willingly intervened in judicial sales to such an extent that Parliament was called upon to curtail their jurisdiction.¹⁰⁴

The need for reassessing the duty owed by the mortgagee did not squarely arise until 1971 in *Cuckmere Brick Co. Ltd. v. Mutual Finance Ltd.*¹⁰⁵ The plaintiff had borrowed £50,000.00 from the defendant, giving as security a site comprising nearly three acres for which planning permission had been obtained for a development consisting of one hundred apartments. Eventually the plaintiff ran into financial difficulty and was unable to proceed with the proposed development. Meanwhile, planning permission had been obtained for a less costly undertaking, namely the construction of thirty-three houses. Ultimately, the plaintiff went into default and the defendant proceeded to exercise the power of sale,

¹⁰² Per Lord Blackburn in *Speight v. Gaunt* (1893), 9 App. Cas. 1, at p. 19 (H.L.).

¹⁰³ In *Sterne v. Victoria & Grey Trust Co.*, *supra*, footnote 70, the court held that there were two lines of authority respecting the duty of a mortgagee. The good faith standard is applied when the action is to have the sale set aside. The standard encompassing reasonable precautions is applied when the mortgagee is called upon to account for the sale price realized.

¹⁰⁴ Prior to 1867 it had become common practice for courts of equity in cases of sales by way of auction to direct a reopening of the biddings if a new offer exceeded the reported bid by ten per cent. In that year the practice was abolished by an amendment to the Sale of Land by Auction Act, 1867, 30 & 31 Vict., c.48, s.7. Thereafter all sales were to be confirmed to the highest *bona fide* bidder, absent fraud or improper conduct in the management of the sale. The language used to convey this directive is as strong and clear as one could ever expect from any legislature. When viewed with other amendments to this Act it is beyond doubt that equity was being severely chastised for meddling in auction sales. Its legislated role was to protect bidders and not debtors. However the right to reopen biddings is one presently exercised by Ontario courts; *cf.*, *Sparling v. 10 Nelson Street Ltd.* (1981), 18 R.P.R. 1 (Ont. H.C.).

¹⁰⁵ [1971] Ch. 949, [1971] 2 All E.R. 633 (C.A.).

entrusting the property to estate agents who undertook advertising in national and local newspapers in anticipation of the impending auction. Posters were published as well and particulars of sale were sent out to land developers throughout the country. However, any reference to the existence of planning consent for one hundred apartments was omitted. The property was sold, but for an amount much less than would have been paid had the bidders known this fact. The defendant was held liable for the difference.

In the Court of Appeal the issue with respect to price inadequacy was resolved by a unanimous holding that the mortgagee was under a duty to act in good faith and to take reasonable care. Thus, although the creditor had unquestionably acted in good faith, he was held liable. The binding effect of the *Kennedy* decision was avoided by seizing upon the fact that since the mortgagee had taken reasonable precautions in that case the statements contained therein were *obiter*.

With respect to Lord Lindley's fear that prospective lenders may be reluctant to loan money unless they can be assured that the security can be sold with ease, the *Cuckmere* decision has not departed from the traditional stance in one important respect:¹⁰⁶

Once the power has accrued, the mortgagee is entitled to exercise it for his own purposes whenever he chooses to do so. It matters not that the moment may be unpropitious and that by waiting a higher price could be obtained. He has the right to realize his security by turning it into money when he likes. Nor, in my view, is there anything to prevent a mortgagee from accepting the best bid he can get at an auction, even though the auction is badly attended and the bidding exceptionally low. Providing none of these adverse factors is due to any fault of the mortgagee, he can do as he likes.

Any inadequacy in sale price caused by depressed market conditions even though temporary will not enable the debtor to hold the creditor accountable. The duty only encompasses the adoption of reasonable precautions which are to be performed in a careful manner. The value of the property is equated with the best price obtainable in the prevailing circumstances.

(2) *Canada*

Until recently there were few Canadian decisions dealing with this issue in the context of real property mortgages. Until the *Cuckmere* decision, the standard of good faith as enunciated in the *Kennedy* decision was applied.¹⁰⁷ But the debate has never been limited to sales of

¹⁰⁶ *Ibid.*, per Lord Salmon L.J., at pp. 965 (Ch.), 643 (All E.R.).

¹⁰⁷ *E.g.*, *British Columbia Land & Investment Agency v. Ishitaka* (1911), 45 S.C.R. 302. In the same year the Privy Council adopted an identical approach in *Haddington Island Quarry Company Limited v. Huson*, [1911] A.C. 722. The court did not refer to *Kennedy*, but the case was cited by counsel, *ibid.*, at p. 724. In so doing the Judicial

real property. Sales under the Bank Act,¹⁰⁸ a chattel mortgage or made by a receiver have provided fertile ground in which to perpetuate the enigmatic problem of balancing authorities or redefining the proper standard of care.¹⁰⁹ Cases which are traditionally viewed as supporting one of the standards are often used to support the rival view.¹¹⁰ Attempts are rarely made by the courts to explain just how the two differ in practical terms or to justify in policy terms why the mortgagee's obligation should be merely one of good faith.

More recent decisions dealing with the power of sale show that the *Cuckmere* decision has influenced some, but not all, Canadian courts in the defining of a standard of care. Moreover it has provided an underlying framework by which our courts have been able to review the nature of the undertakings to be observed when discharging this obligation. Nonetheless, there is still a degree of uncertainty surrounding the requirements if this standard is to be met and which requires analysis on a provincial basis.

(a) *Ontario*

In turning to the power of sale, creditors in Ontario have, on a number of occasions, been faced with an aggrieved debtor seeking recompense following a sale at a price alleged to be inadequate. Of the recent cases both reported and unreported, we need examine only one as representative of those which have followed.¹¹¹ Regardless of the verbal formulae adopted by the court, paying particular attention to the impact

Committee changed its advice with regard to an earlier decision: *National Bank of Australasia v. United Hand-in-Hand & Band of Hope Co.* (1879), 4 App. Case 391, on appeal from the Supreme Court of Victoria. Two years after the *Huson* decision the Committee rendered a different opinion: *McHugh v. Union Bank of Canada*, [1913] A.C. 299, on appeal from the Supreme Court of Canada. The mortgagee was not required to act as the reasonable man would in the realization of his own property. Only those who are firm proponents of *stare decisis* would attempt to determine the binding effect, if any, of the *Ishitaka* decision in these circumstances. Of course, in strict constitutional theory the Privy Council was never bound by precedent, since as a Judicial Committee it merely offered advice to the Monarch and did not render decisions.

¹⁰⁸ S.C., 1980-81-82-83, c. 40.

¹⁰⁹ With respect to s. 88 Bank Security [now s. 179 of the Banks and Banking Law Revisions Act, S.C. 1980, c. 40] see, *Canadian Imperial Bank of Commerce v. Heppner* (1965), 52 W.W.R. 295, at p. 302 (Sask. Q.B.); *Flying "L" Ranching Co. Ltd. v. The Toronto-Dominion Bank* (1976), 9 Nfld. & P.E.I.R. 209, at p. 219 (Nfld. C.A.). With respect to the standard to be exercised by a receiver, see *Industrial Development Bank v. Douglas Plywood Log Sales Ltd.*, [1972] 4 W.W.R. 114 (B.C.C.A.); *Ostrander v. Niagara Helicopters Ltd.* (1973), 1 O.R. (2d) 281 (Ont. H.C.).

¹¹⁰ *E.g.*, *J. & W. Investments Ltd. v. Black* (1963), 41 W.W.R. 577, at p. 592 (B.C.C.A.), per Sheppard J.A.

¹¹¹ There are two early Ontario cases which limit the creditor's obligation to one of good faith: *Kaiserhof Hotel Co. v. Zuber* (1912), 46 S.C.R. 651, 9 D.L.R. 877, aff'ing (1911), 25 O.L.R. 194 (Ont. C.A.), aff'ing (1911), 23 O.L.R. 481 (Ont. Div. Ct.);

of marketing precautions on the outcome of the litigation is instructive in determining future conduct.

Undoubtedly the sale practices followed in Ontario since 1979 have been influenced by the standard of care enunciated in *Wood v. Bank of Nova Scotia*,¹¹² and especially by the nature of the marketing techniques suggested by the court to meet that standard. The defendant bank, through its solicitors, before proceeding to sell the plaintiff's property, obtained an "informal appraisal" from a real estate agent who placed the property value at \$52,000. Shortly thereafter an exclusive listing was given to the agent and about a month later an offer of \$45,000 was accepted and applied against the \$56,000 owing on the mortgage. After obtaining two appraisals, one at \$93,200 and another at \$95,000, the debtor commenced an action to have the sale set aside, or, in the alternative, damages for selling at "gross undervalue".

As to the proper standard of care the court adopted the criterion of the *Cuckmere* decision. The court noted that the agent led no evidence as to his efforts to sell the property and concluded that inadequate efforts were made to bring the property to the attention of the market place in the customary way. A proper sale would have entailed a multiple listing agreement or such other steps to ensure that the property was exposed to a wide segment of the market. However, the court clearly stated that it was not calling for a multiple listing in every case, but at least advertising by the simple device of a "for sale" sign on the property should have been considered. In addition, some thought should have been given as to whether it was necessary to sell the property so quickly. If not, then it should have been left on the market for a longer period as prescribed in the customary listing agreement. Finally, in regard to this latter advice, the decision implies that property should not have been sold in mid-winter unless necessary.¹¹³ In the circumstances the bank was held responsible for the negligent acts of the agent. Moreover, it was deemed to have been careless in looking after its own interests by accepting an offer which did not extinguish the debt.

With respect to the argument that the sale price mirrored that of the appraisal, the court concluded that it too was inadequate since it ignored

Wilson v. Taylor (1913), 11 D.L.R. 455 (Ont. C.A.), aff'ing (1912), 7 D.L.R. 316 (Ont. H.C.). More recently the more stringent standard has been applied in *Bank of Nova Scotia v. Barnard* (1984), 32 R.P.R. 292 (Ont. H.C.); *Sterne v. Victoria & Grey Trust Co.*, *supra*, footnote 70; *Siskind v. The Bank of Nova Scotia* (1984), 46 O.R. (2d) 575 (Ont. H.C.).

¹¹² (1979), 10 R.P.R. 156 (Ont. H.C.).

¹¹³ "There does not appear to have been any overwhelming need to sell the property quickly, nor in the middle of winter. The property could well have been left on the market for a longer period such as a normal listing period."; per Eberle J, *ibid.*, at p. 170.

such factors as zoning, services and "market value".¹¹⁴ In adhering to the "income approach" as a method of valuation, the agent also used inaccurate figures given by an employee of the defendant bank. As for setting aside the sale, the court held that as there was no covert scheme or arrangement between the purchaser and the bank a sale even at gross undervalue was not sufficient to warrant such relief.¹¹⁵ Damages were awarded on the basis of the value of the property (\$65,000, as fixed by the court after hearing the evidence of three other agents) less the debt and the real estate commission payable if the property had sold at the higher price.

Notwithstanding the plaintiff's success with respect to damages, an appeal was launched on the ground that these were inadequate. The defendant cross-appealed maintaining that the standard of care adopted by the trial judge was improper. The Court of Appeal refused to vary the damage award and held that in the circumstances the application of either standard would not affect the result as the defendant bank had failed to meet both.¹¹⁶ The appeal judgment is cursory and refers only to the good faith requirement as being less stringent than the other standard.¹¹⁷

Whether one regards the *Wood* case as compelling authority for Ontario courts or as persuasive authority in the remaining provinces, there are several aspects of the decision which require elaboration. The first pertains to the conclusion that the property was sold at a "gross undervalue". With respect, it is difficult to accept that a sale at seventy per cent of market value, as determined by the court, comes within this description. Secondly, to deem the bank careless for failing to obtain an offer equal to the debt is to impose an obligation unknown to the law of mortgages. It is to be remembered that liability is dependent upon the failure to adopt reasonable precautions or to carry them out in a non-negligent manner, and not on the failure to obtain the so-called "fair market value" of the property or to accept a price equal to the debt.¹¹⁸

¹¹⁴ The court found it strange that the agent ignored the "market value" when giving his opinion as to value. It appears that value was determined in accordance with the income method of valuation rather than the comparative market analysis approach.

¹¹⁵ It is interesting to note that although the court dismissed the action against the purchaser it would not award her costs given the suspicious circumstances of the sale.

¹¹⁶ (1981), 14 R.P.R. 1 (Ont. C.A.).

¹¹⁷ *Ibid.*, at p. 4.

¹¹⁸ In *Bank of Nova Scotia v. Bernard*, *supra*, footnote 111, the court did hold that there was no duty to obtain the true market value of the property, but found that it was listed below this value because of the negligence of the creditor and his appraiser. However, the court did rely on the fact that the property was sold quickly as a result of the low listing price determined in regard to the appraisal. See also *Sterne v. Victoria & Grey Trust Co.*, *supra*, footnote 70, where the creditor was held liable for failing to recognize the distinct character of the property as a hobby farm and to advertise accordingly, and for failing to ensure that the appraisals reflected the true market value.

¹¹⁹ (1980), 115 D.L.R. (3d) 612 (Nfld. S.C.).

Once it is determined that the foreclosing creditor or his agent has acted improperly the courts must then seek to place a value on the property against which to compensate the debtor for his loss. At times there is a tendency to judge the conduct of the creditor by comparing the value of property (as determined by the court) with the sale price. If there is a preoccupation with appraisal evidence, coupled with an unawareness of the scope of marketing precautions, the result may well be the creation of a standard of care no creditor can hope to meet.

(b) *Newfoundland*

The formulation used to set the standard of care required of a foreclosing creditor in this province is individual to this jurisdiction. In 1980 the issue came squarely before the courts in *Frost Ltd. v. Ralph*,¹¹⁹ where Goodridge J., after examining the authorities, including the *Cuckmere* decision, expanded upon the traditional good faith standard:¹²⁰

A mortgagee is not acting in good faith when the price realized is plainly and significantly short of the true value of the property sold, when the mortgagee acts willfully and recklessly in the conduct of the sale with the result that the interests of a mortgagor are sacrificed, when he fails to take reasonable precautions to obtain a proper price, or fails to act in a prudent and business-like manner with a view to obtaining as large a price as may fairly and reasonably with due diligence and attention be under the circumstances obtainable.

The need to express the creditor's obligations in these terms arose from a sale in which two hotel properties, valued at slightly under \$3,000,000, were sold to a third party privately for the sum of \$123,000. The latter figure represented the debt owing to the foreclosing creditor, a second mortgagee. The amount owing on the first mortgage was \$60,000. Goodridge J. concluded that the mortgagee, by omitting to obtain an appraisal, by failing to test the market in a public arena and by selling the property for barely enough to satisfy his mortgage debt, had failed to meet the standard of good faith. The Court of Appeal agreed with Goodridge J.'s reformulation of the law and its application to the circumstances of the case.¹²¹

The court's approach to delineating the standard of care bridges the gap between two standards perceived to be in opposition. Nonetheless, had the court determined that the standard did not encompass responsibility for negligent acts the result should have been no different. No one would deny that the sale price was *prima facie* fraudulent, or at the very least that the creditor acted in bad faith. This appreciation finds support in the remedial relief granted by the court. The sale was set aside on the basis of the amount paid by the purchaser, and in light of the fact that

¹²⁰ *Ibid.*, at p. 622. Goodridge J. maintained that his analysis of the law was merely a restatement of the good faith theory.

¹²¹ *Frost Ltd. v. Ralph et al.* (1982), 140 D.L.R. (3d) 572 (Nfld. C.A.).

the creditor had prearranged a private sale with him in the event the debtor failed to redeem.

Although the judgment contains only limited advice on the precautionary measures required, the passing reference to exposing the property in a public forum leads one to ask whether a sale by auction or by tender was the sole means contemplated. Sales conducted after the *Frost* decision and subjected to judicial scrutiny reveal that both methods are now employed. The ineffectiveness of such sale practices is apparent, given the fact that the foreclosing creditor either buys in at the auction or sells privately.

For example, in *Finance America Ltd. v. Card*¹²² the foreclosing creditor was unsuccessful in attracting a single bid at the auction, perhaps because the reserve bid was close to the amount of the debt, but in excess of the appraised value. The property was then listed for a sale for a period of ninety days but no offers were received.¹²³ A month later the property was sold privately for \$25,000. The creditor's claim for a deficiency judgment based on the sale price was rejected. The parties agreed that the issue before the court was whether the property sold at fair market value. Since the foreclosing creditor had obtained an appraisal at \$34,000 he was condemned to a judgment based on his own evidence.¹²⁴ Had the parties realized that even the more onerous standard of care does not require that the market value be obtained, then the litigation might have taken a different course.

The only other relevant aspect of sale practices in this province, which will be examined later, relates to the foreclosing creditor as purchaser.¹²⁵ This will provide an opportunity to examine the precedential value of the *Frost* decision.

(c) *Prince Edward Island*

If auction sales generate little interest then the alternative is to sell privately as there is no legal basis upon which the foreclosing creditor in this province may purchase the property. He may not purchase for the purpose of preventing a sale at an undervalue nor is he entitled to purchase as an independent third party.¹²⁶ Thus, the setting of a reserve bid

¹²² (1982), 41 Nfld. & P.E.I.R. 114 (Nfld. Dist. Ct.).

¹²³ The property was listed for \$37,000 although the mortgagee admitted that he was prepared to accept any offer. None was received.

¹²⁴ The appraised value was determined by comparing the property being foreclosed with one other similar property.

¹²⁵ See text, *infra*, footnote 151.

¹²⁶ With respect to the right of a mortgagee in Prince Edward Island to purchase for the purpose of preventing a sale at undervalue, it has been held that he cannot bid; *Royal Trust Corporation of Canada v. Reid* (1984), 47 Nfld. & P.E.I.R. 199 (P.E.I.S.C.). *Quaere*—could not the mortgagee advertise the property for sale, reserving the right to bid?

is of critical importance, but if it is not met for whatever reason then a private sale is required unless the property is re-auctioned. Apparently, a private sale is more common in which case the services of a real estate agent may be sought. A province with a population of 125,000 is unlikely to generate a great deal of precedent governing sale practices. There are only two reported decisions which deal with the problem of price inadequacy provoked by improper liquidation procedures. Both appear to embrace the less onerous standard of care, although the judgments are ambiguous.

In 1975 the Court of Appeal rejected the argument of several guarantors that the foreclosing creditor had been negligent when selling property by auction to one of ten bidders in attendance.¹²⁷ The court held that even if the allegations were true the contract of guarantee precluded the guarantor from raising this defence in the deficiency action. Only where the conduct of the foreclosing creditor constituted a flagrant abuse amounting to fraud would the court, despite the wording of the contract, absolve the guarantors of liability. The similarities between this approach and that found in *Kennedy v. De Trafford* are striking. Whether the application of a higher standard would have altered the outcome of the decision is questionable. The Court of Appeal was not prepared to disturb the trial judge's finding that a willing purchaser would have paid a higher price.

It was not until 1984 that we find a debtor and his guarantor objecting to the amount being claimed in a deficiency action. The steps taken by the foreclosing creditor as set out in *Royal Trust Corporation Canada v. Reid*¹²⁸ confirm that the power of sale is both efficient and ineffective. After inserting a notice of sale in a local newspaper once a week for four consecutive weeks, the property was offered for sale by auction. The Sheriff announced a reserve bid of \$28,000, determined in accordance with the amount of the indebtedness. There were no offers, although it is unclear whether this was due to the absence of interested persons or their reluctance to bid. The property was withdrawn from sale and a week later listed with the foreclosing creditor's subsidiary real estate firm for \$23,000. Three weeks later it was sold for \$19,000. The court concluded that there was no merit in the argument that the reserve bid was too high, as prospective purchasers could have made known their interest in the property following the auction sale. As to the argument that the foreclosing creditor failed to make reasonable efforts to sell the property for a better price, the court was powerless to adjudicate upon this issue. The case proceeded by way of an agreed statement

¹²⁷ *Industrial Enterprises Inc. v. Schelstraete* (1975), 61 D.L.R. (3d) 710 (P.E.I.C.A.); leave to appeal to S.C.C. refused February 16, 1976.

¹²⁸ *Supra*, footnote 126; rev'd on other grounds, *sub nom.*, *Reid v. Royal Trust Corporation of Canada* (1985), 54 Nfld. & P.E.I.R. 201 (P.E.I.C.A.).

of facts which made no reference to an appraised value of the property. Thus the debtor and guarantor were condemned to the deficiency judgment claimed, if only because of the lack of evidence to substantiate their allegations. The court was not prepared to intervene unless the sale price could be shown to be fraudulent, failing which the sale must be upheld.

The mere fact that a foreclosing creditor in this province may eventually sell by private contract through the services of an agent does not insulate him from liability. There is still the further problem of determining the adequacy of the services rendered, and it is uncertain whether the courts in this province will insist upon a standard which will relieve the creditor of responsibility for negligent acts. Thus the law found and applied, for example, in Ontario, may well prove to be more beneficial than present sale practices.

(d) *New Brunswick*

In 1984 sale practices in this province attracted notoriety Canada-wide when the Federal Auditor General reported that the Department of Regional Economic Expansion had honoured loan guarantees for \$315,000 following the sale of the "Riviera Motel" by the foreclosing creditor, a first mortgagee, for \$200 to the second mortgagee.¹²⁹ The successful bidder resold the property a day later for \$75,200, which resale price equalled the amount due on the second mortgage plus \$200. While the sale by auction took place in 1982, a 1978 appraisal valued the property at \$550,000.

The investigation conducted by the commercial fraud section of the Royal Canadian Mounted Police was never released, but a trial by media ensued. Allegations of negligence were "swapped" by Ottawa and the foreclosing creditor. Finally, an out of court settlement was reached providing for the repayment of \$186,000.¹³⁰ Canadian taxpayers were required to contribute \$129,000. This revealing incident might lead one to conclude that neither the legislature nor the common law imposes any standard of care upon creditors in this province.

The extent to which such a perception is true will be examined within the context of the foreclosing creditor as purchaser. The vast majority of sales in New Brunswick are effected in this manner and it is within this framework that sale prices have been challenged. But it is one thing for a foreclosing creditor to purchase for a nominal amount, and another to sacrifice the property to a third party at everyone's expense, in particular those liable on the covenant. The creditor's conduct in the "Riviera Motel" case defies rational analysis. This sale remains an anomaly at some distance from accepted practice and common sense.

¹²⁹ See *Globe and Mail*, Friday, June 1, 1984 p. 9, (Tor. & Nat. Eds.).

¹³⁰ See *Telegraph-Journal*, Saint John, Saturday, September 1, 1984.

C. Summary

If we exclude the provinces of British Columbia and Ontario we can say that court adjudication upon the reasonableness of sale price is non-existent in Quebec and Manitoba and illusory in Nova Scotia and Saskatchewan. Of those provinces which resort to a reserve bid as the principal means for ensuring the adequacy of sale price, the manner of determination is self-serving when fixed according to the indebtedness. As is discussed below, another solution is for the foreclosing creditor to buy in at the auction. So long as a deficiency judgment can be pursued this option is far more appealing than a decree of foreclosure absolute. Turning to the power of sale we find that only Ontario practice and law attack the problem of price adequacy in a realistic manner. But the evidence, when viewed nationally, leads to the conclusion that there is no guarantee that sale prices will be maximized simply because one is foreclosing in the judicial forum as opposed to a private one.

IV. *The Foreclosing Creditor as Purchaser*

The adherence to ineffective marketing techniques gives rise to yet further issues should the foreclosing creditor be permitted to purchase its security. The price to be paid, and the right to pursue the debtor for the deficiency are matters which require analysis, as the potential for abuse is obvious. Once these two concerns are analyzed on a provincial basis it becomes self-evident in which provinces the problem of price inadequacy is most acute.

A. *The Judicial Sale*

In those provinces where there are appropriate marketing techniques there is less likelihood that a sale to the foreclosing creditor will remain attractive or necessary. Thus it is not surprising to find that the right of the foreclosing creditor to purchase is a question of law yet to be decided in both British Columbia and Ontario.¹³¹ In the absence of reported decisions on this point one might speculate that the foreclosing creditor would rarely welcome the opportunity to purchase the property if another buyer can be found. The marketing sale techniques followed appear to have rendered such sales a moot issue. In the remaining provinces which foreclose by judicial sale none prohibits the foreclosing creditor from purchasing its security, but the issues under consideration are approached differently in each province.

¹³¹ When sales by auction in Ontario were in vogue, the foreclosing creditor could bid in at the sale by leave of the court in which case conduct of the sale would be carried by another party; see Dunn and Freyseng, *op.cit.*, footnote 28, pp. 200-201. Since courts in British Columbia do grant conduct of the sale to another party, there is no inherent objection to the foreclosing creditor in this province submitting an offer in competition with other prospective purchasers.

The Civil Code of Quebec deems a sale to the hypothecary creditor to have been effected at a price equal to the property's "fair yielding, investment or commercial value in times of normal economic activity, regardless of its depreciation for the time being through a regional or general economic depression".¹³² However, should the creditor subsequently sell the property then the price is deemed to be the resale amount.¹³³ This scheme epitomizes the purist's opinion that security should not be sacrificed to the hypothecary creditor.¹³⁴ Despite the protection afforded the Quebec debtor in these circumstances there remains the difficulty of determining market value no matter how well defined by legislation. The question also remains why property may not be sacrificed to the hypothecary creditor but to any independent third party. The reality may well be that auction sales are poorly attended in Quebec, with the result that the creditors are obliged to purchase unless they wish to pursue another judicial sale. Undoubtedly, even if the limited advertising produces other bidders, the creditor is not going to permit a sale to a party at his expense. The question remains, as in all other provinces, are creditors looking after their own interests regardless of the value of property?

The number of reported decisions in Nova Scotia in which the closing creditor is the successful purchaser is suggestive in itself of the ineffectiveness of marketing property solely by way of legal advertisement, and then disposing of it by public auction. Moreover, the writer's research reveals that it is not uncommon for the creditor to be the sole bidder in attendance, in which case the sale price is usually for a nominal amount.¹³⁵ The fact that the provisions of Quebec's Civil Code and the recently amended Rules of Court in force in Nova Scotia are analo-

¹³² Art. 1202a(c). Where the foreclosing creditor buys in at the sale the debtor, upon application to the court, may be released from any liability with respect to the debt provided that the property had a value equal to the total amount of the creditor's claim. As one would expect, the release of the principal debtor entails the release of his sureties (Art. 1202j). Should the value of the immovable or the resale price be less than the creditor's claim, then the debtor may obtain a release by paying to the creditor the amount required to make up the difference (Art. 1202(e)).

¹³³ Art. 1202b (a) C.c. If the purchaser is, for example, the second hypothecary creditor, then the property must have a value at least equal to the total amount of his claim and that of the first.

¹³⁴ It is to be noted that the provisions of the Civil Code are applicable to any hypothecary creditor who has taken the immovable as security and who has bought in at the auction.

¹³⁵ It cannot be presumed that the sale price is always a nominal amount. In *Bank of Montreal v. Saoud* (1985), 68 N.S.R. (2d) 148 (N.S.T.D.), the mortgagee bid \$100,000 against a debt of \$117,000. As the issue before the court was with respect to the consideration to be stated in the deed of transfer there is no indication whether the mortgagee was the sole bidder. In *Central Trust v. Conway* (1982), 56 N.S.R. (2d) 208 (N.S.T.D.), the foreclosing creditor purchased the property for \$25,000 and resold it five months later for \$41,000. The time lapse between the date the action was started and the property was sold a second time was seven months. In *Nova Scotia Savings & Loan Co. v. MacKay* (1979), 41 N.S.R. (2d) 432 (N.S.T.D.), the property was sold to the foreclos-

gous is most likely a consequence of the failure on the part of both provinces to analyze effectively the primary source of the problem, that is the continual utilization of ineffective marketing techniques.

Understandably, the idea of calculating a deficiency judgment based on a nominal purchase price has necessitated the intervention of the courts and resulted in amendments to the Nova Scotia Rules of Court. If the foreclosing creditor has paid less than the fair market value as of the date of the auction sale, the court may calculate the deficiency utilizing that figure rather than the auction amount.¹³⁶ However, it would appear that this rule would be invoked only where the creditor elects not to effect a resale and is seeking a deficiency judgment. Nonetheless, this Rule can be faulted for its dependence upon appraisal evidence and despite the fact that it requires that fair market value be established by an independent appraiser.

The alternative solution, and a popular one, is for the foreclosing creditor to buy in at the sale and then seek an order of confirmation, requesting leave to postpone for a maximum of six months the application for a deficiency judgment.¹³⁷ The delay is necessary so that the property can be resold before the expiration of the postponement period. The objective is to obtain a deficiency judgment based on the second sale which is carried out in a more appropriate manner by listing the property for sale. However, there is a cap on the amount that can be claimed after a genuine sale. The deficiency may not exceed that claimable after the auction sale.¹³⁸

This limitation is of greater significance in situations where the amount bid by the foreclosing creditor exceeds a nominal amount. Secured creditors have sought to calculate the deficiency on the basis of the resale price and to include legal fees, expenditures for repairs and maintenance and accrued interest.¹³⁹ However, the total amount being claimed

ing mortgagee for \$10,500 and subsequently resold for \$17,000 some twelve months later. The property had been listed on the open market with a real estate agent for eight months at \$29,000. However, the building had fallen into disrepair due to vandalism and only one offer had been received, that for \$17,000. In *C.M.H.C. v. Farrell* (1980), 11 R.P.R. 73 (N.S.T.D.) the successful bidder, who was not the foreclosing creditor, immediately resold the property for a \$3,000 profit. It is proper to ask whether the second purchaser was also in a position to profit at the expense of both the debtor and perhaps the creditor.

¹³⁶ Rule 47.10(2)(a).

¹³⁷ Rule 47.10(3).

¹³⁸ *Ibid.*, codifying *Traders Group Ltd. v. Mason* (1974), 10 N.S.R. (2d) 115 (N.S.C.A.); *Nova Scotia Savings and Loan v. MacKay*, *supra*, footnote 135; *Central Trust Company v. Bartlett* (1983), 30 R.P.R. 267 (N.S.C.A.).

¹³⁹ *Central Trust Company v. Conway*, *supra*, footnote 135; *Atlantic Trust Co. of Canada v. Aslin*, December 8, 1983, unreported decision of Nathanson J. (N.S.T.D.) S.H. No. 39765.

superseded the deficiency as determined at the date of the auction with the result that the auction price is employed to measure the amount of any deficiency. In holding that a deficiency judgment can be no greater than that arising from the Sheriff's sale, the Nova Scotia Court of Appeal stated: "Following such a practice would be. . . in accord with the equitable principles that have always intervened in disputes between mortgagors and mortgagee."¹⁴⁰ What the court overlooks is that the essential problem is the manner in which the initial sale is attempted and not the terms of the mortgage contract, nor the conduct of either of these litigants. There are other criticisms.

The limitation of the amount which may be claimed as a deficiency may be inconsequential if the creditor's bid is a nominal one. However, this attack supports the creditor who may be able to obtain a deficiency judgment equal to that which could have been claimed had a proper sale been ordered in the first instance. Whether or not all the sums claimed are permitted by law or by the mortgage document is a question which should be answered by the court following a properly conducted sale. It should not be determined solely on the basis of the amount offered by the foreclosing creditor at a non-representative auction.

Some of the difficulties encountered in determining the limits of an acceptable sale price in both Quebec and Nova Scotia could have been avoided if the foreclosing creditor were unable to pursue judgment on the covenant for a deficiency.¹⁴¹ Such solution is imposed by section 16 of the Mortgage Act¹⁴² of Manitoba which applies equally to all creditors regardless of status.¹⁴³ With respect to non-corporate borrowers in Alberta and Saskatchewan it would be of no benefit to the foreclosing creditor to submit an offer with the purpose of establishing a deficiency judgment as there is no right to sue on the covenant at any time.¹⁴⁴

This leaves the corporate debtor in these two provinces in the inevitable position of having to attack the sale price offered by the foreclosing creditor. This is particularly the case in Alberta where the court adjudicates upon the reasonableness of offers, as opposed to Saskatchewan practice where creditors set a reserve bid equal to the debt or a percentage of the fair market value. As to the right of the foreclosing creditor to purchase, this possibility was reaffirmed in 1984 by the Alberta

¹⁴⁰ *Central Trust Company v. Bartlett*, *supra*, footnote 138, at p. 283.

¹⁴¹ There is always the possibility that the value of the property will exceed the indebtedness; in which case this solution is irrelevant.

¹⁴² R.S.M.1970, c.M-200.

¹⁴³ *Manitoba Development Corporation v. Berkowits*, [1979] 5 W.W.R. 138 (Man. C.A.).

¹⁴⁴ This statement is not entirely true since the debt is not extinguished and the creditor has a right to realize on collateral security; *Krook v. Yewchuck*, [1962] S.C.R. 535.

Court of Appeal in *Canada Permanent Trust Co. v. King Art Developments Ltd.*¹⁴⁵ Given the similarities between the relevant legislation in this province, and that of its neighbour one would expect Saskatchewan courts to reach the identical conclusion. In any event commentators and courts assume that this is the law in Saskatchewan.¹⁴⁶

Once it is established that the foreclosing creditor in Alberta may submit an offer for the consideration of the court the only issue left for analysis is that of its reasonableness.¹⁴⁷ In *King Art Developments* the court rejected as a binding proposition that the creditor must always offer the fair market value of the property. On the facts, the court allowed the sale to the foreclosing creditor on a forced sale evaluation. Prior to the Court of Appeal's judgment, decisions as to acceptable sale prices were in conflict. In three cases the court rejected a proposal where the offer was less than the alleged market value and in another it was accepted.¹⁴⁸ The decision in *King Art Developments* has not settled the controversy and courts in Alberta are still debating the value that should be used for a sale to the mortgagee.

D. The Power of Sale

Other than for the purpose of preventing a sale at an undervalue, an English creditor has never been permitted to buy in at its own auction under a power as though he were an independent third party.¹⁴⁹ In New

¹⁴⁵ *Supra*, footnote 27.

¹⁴⁶ See Richards and Wright, *op. cit.*, footnote 60, pp. 11-12; *Co-operative Trust Co. v. O'Grady* (No. 2) (1984), 32 Sask. R. 224 (Sask. Q.B.)

¹⁴⁷ There are at least two methods by which the foreclosing creditor can purchase. If no offers are received the creditor may apply for a Rice Order setting out a proposal for the purchase of the property. If acceptable to the court, then a stay of execution for a specified period, usually two months, is given to the debtor to enable him to procure a better offer. Failing this the creditor would be declared purchaser and a deficiency judgment would be granted. The alternative method is for the creditor to submit a tender along with other persons. As to which one is preferable the court in *King Art Developments* outlined factors to be considered and also indicated that it might be desirable to list the property for sale.

¹⁴⁸ See *Crown Life Insurance Co. v. Clark* (1915), 9 W.W.R. 333 (Alta. App. Div.); *Heritage Savings & Trust Co. v. Unicorp International Investments Ltd.* (1981), 34 A.R. 90 (M.C.); *Fuhr v. Madison Development Corp. Ltd.*, [1984] 3 W.W.R. 334 (Alta Q.B.), where the court would not accept an offer equal to the "forced market value for cash". More recently the court in *Yorkshire Trust Co. v. H.B. Neilson Management Corp. Ltd.* (1984), 34 Alta. L.R. (2d) 174 (Alta. Q.B.) confirmed a sale to the foreclosing creditor at "forced market value on terms". The latter valuation takes into consideration the possibility of the foreclosing creditor providing the purchaser with financing.

¹⁴⁹ With respect to the foreclosing creditor purchasing under its power of sale, English courts have not been swayed by any argument in support of this right. The foreclosing creditor "cannot sell to himself either alone or with others, nor to a trustee for himself, nor to anyone employed by him to conduct the sale"; *Farrar v. Farrars*,

Brunswick this right is established by statute,¹⁵⁰ while in Prince Edward Island the foreclosing creditor who is unable to affect a sale by auction must sell privately and to a third person before seeking judgment on the covenant for any deficiency. In Newfoundland foreclosing creditors are buying in at their auction as though permitted to do so by statute.¹⁵¹ Neither the courts nor the solicitors of creditors in this province appear to be concerned with the legal basis for this practice.¹⁵² The fact that the provision regulating this aspect of the statutory power in Newfoundland, as in Ontario, is modelled almost verbatim on the English legislation should arouse suspicion.¹⁵³ Solicitors searching titles to property where there is a deed from the mortgagee to the mortgagee should be wary. But that problem must be resolved elsewhere, as the concern here lies with sale prices and deficiency actions.¹⁵⁴

(1) Newfoundland

The fact that Nova Scotia, Quebec and Newfoundland arrived at an identical solution to a common problem is fortuitous and must derive from common failure to analyze the origins of their problems. Under the law of Newfoundland a foreclosing creditor may buy in at the auction for a nominal amount and seek a deficiency judgment based on the resale amount.¹⁵⁵ At this point one could maintain that he is purchasing merely for the purpose of preventing a sale at an undervalue. However,

Limited, *supra*, footnote 88, at p. 409. In support of their position, the nineteenth century Chancery Courts invoked two rationales: first a man cannot contract with himself, and second a trustee cannot purchase a property which is the subject of the trust; *ibid.*, at pp. 404 and 409, and *Downes v. Grazebrook* (1817), 3 Mer. 200, 36 E.R. 77 (Ch.). Today we simply acknowledge that a creditor purchasing under his power of sale will be in conflict with his duty to take reasonable care. Otherwise, it could be to his advantage to pay as little as possible if he is able to pursue a deficiency judgment based on the price which he has offered.

¹⁵⁰ R.S.N.B. 1973, c.P-19, s.44(1).

¹⁵¹ As early on as 1977 mortgagees have been buying at their own sale; see *Re Hallmark Construction Limited* (1978), 19 Nfld. & P.E.I.R. 165 (Nfld. S.C.).

¹⁵² If the decision of the New Brunswick Court of Appeal in *Gauvin v. Dionne* (1919), 51 D.L.R. 294 is cited as authority for such a proposition one must be mindful of the doubt expressed in W.B. Rayner and P.H. McLaren, *Falconbridge On Mortgages* (4th ed., 1977), pp. 741-742 and note 8, as to its correctness and the fact that under English law such conduct has always been prohibited.

¹⁵³ Compare; Conveyancing Act, R.S. Nfld. 1970, c. 63, s.5(1)(a); Mortgages Act, R.S.O. 1980, c. 196, s.23(1); Law of Property Act 1925, c.20, s.101(1)(i) (U.K.).

¹⁵⁹ If it were decided that the mortgagee may not purchase for this purpose, then a subsequent sale to a third party would most likely be held voidable rather than void. Presumably the court would not interfere with a sale to a *bona fide* purchaser for value; see *Otter v. Lord Vaux* (1856), 2 K. & J. 650, 69 E.R. 943, aff'd 6 DeG. M. & G. 638, 43 E.R. 1381.

¹⁵⁵ *Nova Scotia Savings and Loan v. Miller* (1985), 53 Nfld. & P.E.I.R. 41 (Nfld. S.C.).

should he purchase for an amount greater than the resale price, then the deficiency judgment is limited to that which could have been claimed after the auction.¹⁵⁶ It is the application of this rule which has the effect of legitimizing a sale to the foreclosing creditor in the first instance.

As might be expected, sales under a power provide the debtor with the opportunity to allege improvident sales measures on the part of the foreclosing creditor in relation to the second sale. Yet in *Nova Scotia Savings & Loan Company v. Miller*¹⁵⁷ the court applied the good faith test as derived from *Kennedy v. De Trafford* and ignored its formulation in *Frost Ltd. v. Ralph*.¹⁵⁸ The foreclosing creditor was held to have acted in good faith. He had first sought tenders, had then bought in August of 1982 at a public auction at which he purchased for \$14,000 and sold five months later for \$159,000. It may be that the latter figure represented the market value of the property, although it had been purchased in 1977 for \$217,000, listed for sale by the debtor in February of 1982 for a period of two months at \$304,000, and appraised in May of 1982 by the foreclosing creditor for \$221,000. Are we to assume that the appraisal was made in "error"? Until the Court of Appeal has the opportunity to redefine the limits of the creditors' obligations and to re-examine the legal basis upon which they may purchase it is unlikely that sale practices will change in this province.

(2) *New Brunswick*

Since it is customary for an auction to be conducted by the Sheriff of the judicial district in which the land is situated, shrieval estimates as to the percentage of sales at which the foreclosing creditor, or his solicitor, were the sole participants substantiates the claim that marketing solely by legal notices of sale is ineffective. In four of these districts it has been suggested that between eighty and nine-nine per cent of the sales were conducted without a bidding audience.¹⁵⁹ The general practice not only involves a mortgagee buying in at his own sale, but also encourages purchases for nominal amounts varying from \$100 to \$1,000.¹⁶⁰ Another practice is to buy in for the amount of the outstanding debt, while some lenders have settled upon fixing a reserve calculated on the basis of a percentage of market value at which the mortgagee will agree to take title to the property if there are no other bidders.¹⁶¹ Invariably

¹⁵⁶ *Federal Business Development Bank v. Gaslard* (1984), 44 Nfld. & P.E.I.R. 89 (Nfld. C.A.).

¹⁵⁷ *Supra*, footnote 155.

¹⁵⁸ *Supra*, footnotes 119 and 121.

¹⁵⁹ See J.T. Robertson, *Foreclosure by Power of Sale: Securing a Proper Price in New Brunswick* (1983), 32 U.N.B.L.J. 83, at p. 106, footnote 89.

¹⁶⁰ *Ibid.*, at p. 115, footnote 124.

¹⁶¹ *Ibid.*

this amount is insufficient to extinguish the debt. It is well recognized in the legal community that property will be never sold to a third party for a nominal amount.¹⁶² The foreclosing creditor will set either a reserve bid or buy in or do both, rather than allow a third party to make a windfall at his expense.

The New Brunswick courts have been inconsistent when dealing with the required standard of care. In 1979 the Court of Appeal in *Canadian Imperial Bank of Commerce v. Haley*¹⁶³ adopted the *Cuckmere* position. The influence of *Haley* on sale practices has been negligible because it is thought irrelevant to the mortgage situation, as the facts of that case involved security taken under section 88 of the Bank Act.¹⁶⁴ Moreover, in 1981 the Court of Appeal rejected the argument that the mortgagee, when seeking a deficiency judgment, must give credit for the market value of property rather than the amount for which he became the successful purchaser.¹⁶⁵ The property was alleged to have had a fair market value of \$60,000, a realizable market value of \$45,000 but was purchased by the foreclosing creditor for \$25,000. The court summarily held that the secured creditor was not prevented from selling the property for less than the appraised market value, notwithstanding the fact that it intended to look to the debtor and guarantor for the deficiency.¹⁶⁶

No one would debate that this is an accurate statement of the law when reviewed in the abstract. But once it is recognized that the court did not even consider the marketing techniques followed, nor examine the parameters of the creditor's obligations, the rationale of this case does not provide a solution to the problems described. Regardless of the manner in which the issue was framed for the court, a sale to the creditor at forty per cent of the property's market value should be deemed, in the writer's opinion, *prima facie* evidence of a sale at a "gross undervalue".

The litigation on sale prices has not proceeded beyond the trial level. Therein we find two conflicting solutions to the problem of price

¹⁶² This observation requires further examination in light of a sale of a cedar shingle mill, valued at \$1.3 million dollars, for \$5,000. The mill opened in 1983 with the assistance of a \$450,000 provincial government loan guarantee and federal grants totalling \$544,969; see *Fredericton Daily Gleaner*, September 12, 1984, p. 3.

¹⁶³ (1978), 25 N.B.R. (2d) 304 (N.B.C.A.); applied in *The Bank of Nova Scotia v. Beck* (1986), 67 N.B.R. (2d) 6 (N.B.C.A.), which dealt with a chattel mortgage. However the latter decision makes no reference to those decisions at the trial level regarding real property mortgages.

¹⁶⁴ R.S.C. 1970, c.B-1. Section 88 is now section 179 of the current Act, *supra*, footnote 108.

¹⁶⁵ *Central & Eastern Trust v. Rosebowl Holdings* (1981), 34 N.B.R. (2d) 308 (N.B.C.A.).

¹⁶⁶ Counsel for one of the defendants informed the writer that the issue was not pursued in detail in light of other issues before the court. This is verified by the cursory treatment given to it by the Court of Appeal; see *ibid.*, at p. 319.

adequacy. One seeks to balance the interests of all those concerned while the other does little to instill confidence in the debtor that his basic rights will be protected. In each case the foreclosing creditor faithfully adhered to the statutory notice requirements but failed to adopt any other marketing techniques.

The first solution to be adopted unknowingly copied that available in Nova Scotia, Quebec and Newfoundland. In *Nova Scotia Savings and Loan v. MacKenzie*¹⁶⁷ the court reduced the foreclosing creditor's claim for a deficiency by \$9,000 following the purchase of the property for \$10,000 and its resale for \$19,000 after a three-month listing with a real estate agent. The court applied the law as stated in *Haley* and held that the plaintiff had failed to take any reasonable precautions to obtain the true market value of the property. Accordingly, its value was equated with the price obtained on the resale. Even though the court expressly declined the opportunity to make an "academic reconciliation" of certain statutory provisions, which are viewed as extricating the foreclosing creditor from liability with respect to the first sale, the result is justified to the extent that it recognizes the plight of borrowers: ". . . it must be borne in mind that New Brunswick, contrary to other provinces gives statutorily very little protection to the mortgagor in cases where the mortgage purchases at the sale".¹⁶⁸

While the court declined to attempt the "academic reconciliation" this writer has tried to do so elsewhere and concluded that the deficiency granted by the court was warranted, although it is by no means certain that the second sale would have met the more onerous standard of care.¹⁶⁹ The fact that the foreclosing creditor in New Brunswick was forced to calculate his deficiency according to the resale price, and that it is done voluntarily in two of the provinces speaks for itself. But any analogy between sale practices in the Atlantic region must end here since an opposite approach was taken in 1984 in *Bank of Montreal v. Allender Investments Ltd.*¹⁷⁰

In essence, the foreclosing creditor bought in at its own sale for \$100 and then sued the mortgagor and guarantor for the full amount of

¹⁶⁷ (1979), 29 N.B.R. (2d) 78 (N.B.Q.B.).

¹⁶⁸ *Ibid.*, per Angers J., at p. 80.

¹⁶⁹ The arguments turn on the interpretation of a number of subsections which refer to the loss for which the mortgagee will or will not have to account. They are examined in Robertson, *loc. cit.*, footnote 159, at p. 107 *et seq.* It should be noted that similar arguments could be made in both Ontario and Newfoundland: see Property Act, R.S.N.B. 1973, c.P-19, ss. 44(1)(a), 47(2), 47(6); Mortgages Act, *supra*, footnote 153, s.23(1); Conveyancing Act, *supra*, footnote 153, ss. 5(a), 7(2) and 7(6). But it should be remembered that these provisions are a mirror of those found in England and have never been used to exonerate the mortgagee of liability in the manner contemplated.

¹⁷⁰ (1983), 53 N.B.R. (2d) 143 (N.B.Q.B.).

debt, \$47,000 less \$100, while retaining title to the property. Its appraised market value at the date of sale was \$46,000 as compared with \$75,000 on the date the security was given. The court granted the deficiency judgment as requested and held that as long as the statutory and contractual provisions are followed strictly then no question of negligence can arise. In effect the court held that the statutory and contractual notice requirements represents a complete code as to the conduct required of the foreclosing creditor. This conclusion rests on the mistaken assumption that the notice requirements serve as conduits for attracting potential purchasers. A historical review of the relevant statutory provisions reveals that publication in newspapers and the Royal Gazette were alternatives to serving notice of the impending sale on the debtor.¹⁷¹ This explains why notices today are directed solely at the debtor and those with an interest in the equity of redemption but never to the general public.

While strict compliance with the power is necessary, it does not thereby follow that the creditor is relieved of the duty to undertake reasonable sale measures in a non-negligent manner. A court could just as easily have held that the statutory power represents a minimum standard of conduct. Moreover, one cannot forget that the foreclosing creditor must be able to justify his decision to sell by public auction since he has the right to sell privately. The ability of the creditor to purchase his own security, if the sale is by auction, cannot be regarded as a relevant factor when making that determination.

The practice of buying in for a nominal amount can certainly be viewed as an abuse of a remedial process, but until the *Allender* decision it was thought that most creditors would have waited until a second sale had been effected in the normal commercial manner before commencing a deficiency action. The amount claimed would then be based on the second sale. However, in that particular case it appears that the creditor was unable to dispose of the property during the three years following the auction. In these circumstances the fact that he was prepared to reconvey the mortgaged premises, upon payment of the amount claimed, provided a means by which the court could have achieved an equitable result. It also attests to the creditor's desire to avoid being characterized as "unscrupulous". However, the court chose to treat this proposal as "inconsequential".

It might be thought that the flawed reasoning of the *Allender* decision would not have had much influence, but it has been applied in subsequent cases to the extent that the price paid at the auction overrides the resale amount.¹⁷² Fortunately, in both instances the amount paid the

¹⁷¹ See Robertson, *loc. cit.*, footnote 159, p. 107 *et seq.*

¹⁷² In *Nova Scotia Savings and Loan Company v. Buraglia* (1983), 47 N.B.R. (2d) 64 (N.B.Q.B.), Hoyt J. noted that the subsequent resale, effected nine months later after

foreclosing creditor exceeded a nominal price. In one the resale price was \$875 greater than the auction price while in the other the difference amounted to \$9,000. Yet neither of these solutions is acceptable.

The criticisms of *Allender* are manifold. If the decision stands, the result is to sanction a system of double recovery; forfeiture of the land and the ability to realize virtually the full amount of the outstanding indebtedness without having to reconvey the property. Moreover, it lends support to the legitimacy of the sale of the "Riviera Motel" and undermines fundamental principles of mortgage law developed over four centuries. It ignores the fact that the law has, until now, never sanctioned a sale at a gross undervalue nor accepted negligence as a defence to such an allegation and explains the adamant refusal of English courts to permit a sale to the foreclosing creditor when he exercises his power of sale.

C. Summary

Without question defective sale processes can lead to substantial injustice should the foreclosing creditor be permitted to purchase its security and to maintain a claim for the deficiency. To the extent that a potential windfall may accrue to the creditor, this possibility is avoided if it elects to resell the property, as is permitted in Nova Scotia, Newfoundland and Quebec. However, it is a trap for the unwary in the two Atlantic provinces should the foreclosing creditor bid an amount greater than could be expected on a resale. There is also no guarantee that the resale price is a result of effective marketing efforts which would meet the higher standard of care.

Should the foreclosing creditor in any one of these three provinces elect to claim the deficiency before reselling only Quebec and Nova Scotia have responded to the potential problem of unjustified enrichment. But to deem the sale price equal to the property's market value places a mistaken reliance upon appraisal evidence, and raises a question to which there does not appear to be an answer at this time: is the creditor obliged to account to the debtor for the unrealized surplus where value exceeds indebtedness? An affirmative response would dictate that the creditor would want to re-elect in favour of pursuing a second sale.

The foregoing solutions are less objectionable than those found in Alberta and Saskatchewan where the debtor is unable to obtain the benefit of legislation eliminating actions on the covenant. To adjudicate on the adequacy of non-competitive offers supported by estimates as to value is, in Alberta, an exercise fraught with danger. The way in which

listing with two real estate agents, was at a price only marginally more than the price offered at the auction sale and marginally less than its appraisal value. In *Nova Scotia Savings & Loan Company v. Doucet* (1984), 54 N.B.R. (2d) 72 (N.B.Q.B.), Jones J. agreed with the reasoning and the result of the court in *Allender*.

the reserve is calculated in Saskatchewan renders a sale to the foreclosing creditor as questionable as the sale to a third party. With respect to non-corporate debtors in these two provinces, and to all debtors in Manitoba, the elimination of deficiency judgments is justified if it can be assumed that debt exceeds value. If the opposite is true then this solution is unacceptable.

Despite all of these criticisms neither the practices nor the law is subject to the adverse analyses made of New Brunswick. This province remains in a category unto itself. A sale to the foreclosing creditor for a nominal amount should not be viewed as a sale under any circumstances.

V. Formulating and Meeting the Proper Standard of Care

The primary objective when pursuing a sale, either by judicial decree or by power of sale, is to maximize sale price and for obvious reasons.

Effecting a sale in a manner which is conducive to realizing the "best price" obtainable in the circumstances will enhance the possibility of protecting any equity the debtor may have in the property. Regardless of the debtor's equity position, a sale conducted in an appropriate manner may extinguish the debt, and, if not, it will reduce the amount of any deficiency judgment which the creditor might pursue. From the creditor's point of view such conduct may ensure that he suffers no financial loss. Even where the sale price is insufficient to extinguish the debt it will minimize the loss to be borne by the creditor where the pursuit of a deficiency judgment is pointless.

The parties to the security transaction are not the only ones affected by the price ultimately accepted by a court or by the foreclosing creditor. The legitimate interests of those who agree to act as surety are well recognized.¹⁷³ The amount for which a guarantor is liable in a deficiency action will be based upon the sale price. The same is true with regard to those who have sold their equity of redemption to a subsequently defaulting third party.¹⁷⁴ And finally, should the sale price be sufficient to satisfy the foreclosing creditor then any surplus devolves in order of priority to those with an interest in the property. Subsequent mortgagees, judgment creditors or lien claimants, although in the unwanted position of forfeiting their right to realize upon their security, are entitled to

¹⁷³ It is accepted in law that a surety is entitled to any right of set-off or counterclaim which the principal debtor possesses against the creditor; see D.G. Marks and G.S. Moss (eds.), Rowlatt, *On The Law Of Principal and Surety* (4th ed., 1982), p. 192.

¹⁷⁴ In the absence of a novation the original mortgagor remains liable. Even if the purchaser of the equity of redemption renews the mortgage for a further time period at an increased rate of interest the courts have not always been willing to characterize the original debtor as a quasi-surety and thereby discharge him from liability on the covenant.

assurances that the property will not be sacrificed to a purchaser to their loss.¹⁷⁵

The justifications offered for imposing a higher standard of care are but one way of delineating the classes of persons to whom this duty of care is owed. The task is much simplified because of the ease in identifying those who have an interest in the conduct of a sale. By using the traditional language of tort law we can now address the problem of formulating an abstract test which will describe the appropriate standard of care.

The precise formulation can be derived from a myriad of sources. One might rely on the standard of conduct identified in *Cuckmere* which, in essence, relied on the reasonable man test appropriate to the law of negligence. However, in recent years there has been a proliferation of statutory standards imposed upon other types of secured creditors who pursue a self-help remedy. So it is common to find that the creditor is obliged to discharge his obligations in a "commercially reasonable manner",¹⁷⁶ or is required to "act honestly and in good faith [by dealing] with the property in a timely and appropriate manner".¹⁷⁷ Likewise the American Uniform Land Transactions Act¹⁷⁸ provides a legislative framework regulating the foreclosing creditor's remedial options and describing the standard in the following terms:¹⁷⁹

Sale may be at a public sale or by private negotiations, by one or more contracts, as a unit or in parcels, at any time and place, and on any terms including sale on credit, *but every aspect of the sale, including the method, advertising, time, place and terms must be reasonable.*

However, the sophistication of the language will not preclude a party from arguing that the foreclosing creditor has failed to fulfil its obligations.¹⁸⁰ Even though all lawyers acknowledge that any standard

¹⁷⁵ E.g., *Canada Permanent Toronto General Trust Co. v. Hollis Pharmacy Ltd et al.* (1964), 48 D.L.R. (2d) 747 (N.S.S.C.), dealing with an application by the second mortgagee for payment out of surplus proceeds in priority to two judgment creditors; *Tomlin v. Luce*, *supra*, footnote 97, an action by second mortgagee against first mortgagee claiming an account of all monies that were received or should have been received but for the latter's error in describing the property at the auction sale.

¹⁷⁶ Uniform Personal Property Security Act, 1982, s.64(1) submitted by the Uniform Law Conference of Canada and the Canadian Bar Association.

¹⁷⁷ Banks and Banking Law Revisions Act, *supra*, footnote 108, s. 179(5).

¹⁷⁸ *Supra*, footnote 83. ULTRA was approved in 1975 by the National Conference of Commissioners on Uniform State Laws and recommended for enactment in all states. ULTRA remains a truly theoretical construct since no state has seen fit to adopt it.

¹⁷⁹ *Ibid.*, Art. 3-508(a). (Emphasis added). This standard is applicable if the foreclosure process is by way of power of sale and by virtue of Art. 3-509(c) is applicable to a judicial sale. The prescribed standard has a precursor in Art. 9-504(3) of the Uniform Commercial Code.

¹⁸⁰ E.g., *Canadian Imperial Bank of Commerce v. Whitman* (1984), 63 N.S.R. (2d) 407 (N.S.C.A.), dealing with s.179 Bank Act security.

prescribed by law or by statute is to be applied objectively, we also recognize that this is only true to the extent that the litigants are not permitted to adjudicate on the adequacy of the precautions taken. Such judgment is the function of the court which in turn must reach its own conclusions. Ultimately, it is the customary application by a court of this objective standard which will determine whether or not the duty has been discharged. Where, on the other hand, the foreclosing creditor seeks a judicial sale, then the standard of care should reflect the same considerations involved with the power of sale and be applied in order. Yet in both of these foreclosure settings a more practical problem must be addressed: exactly what type of conduct will satisfy the requirements of the more onerous standard?

The law of negligence has historically avoided the formulation of precise rules of conduct, and instead has been content to deal with each situation as it arises. However, when it comes to the disposition of property, we are dealing with a most familiar item, and although we would not wish to formulate inflexible codes of conduct we can, without difficulty, at least identify those matters which must be considered when effecting a sale.

The manner in which a voluntary sale should be undertaken is generally understood. By analogy the same techniques should apply to a forced sale. The psychological impact with respect to the price which potential purchasers will pay for property, when it is known that a sale is a forced one, is impossible to ascertain and one which may be unavoidable. However, it can be minimized by demonstrating that the property will not and cannot be sacrificed at the expense of interested persons. The closer the forced sale resembles a sale in the market place then the greater the probability that the best price will be realized. Fair market value is, in reality, only an estimate based on the assumption that reasonable care will be taken to expose the property to the greatest number of individuals in any open market.

Despite the imprecision inherent in any formulated standard of care, the sale of real property would normally be undertaken by persons familiar with such a task. In this regard an examination of the liquidation procedures followed by England's largest Building Society as they relate to residential dwellings is instructive.¹⁸¹ The Halifax Building Society requires that an independent valuation be obtained for the purpose of estimating the property's fair value in a forced-sale situation. Its branch office is then instructed to choose the "best possible selling agent". Once selected the agent is instructed to carry out a forced-sale valuation and is advised that the Society is under an obligation to obtain the best

¹⁸¹ The author wishes to thank Susan Boyd and John S. Thornton, officers of the Halifax Building Society, for their co-operation in explaining the mechanics of a forced sale under the power of sale.

selling price. This caution is lodged for a specific purpose. Pursuant to the Building Societies Act, 1962,¹⁸² any society selling under a power of sale is under an obligation "to take reasonable care to ensure that the price at which the estate is sold is the best price which can reasonably be obtained". Notwithstanding the statutory directive it is generally believed that there is no difference between the duty imposed on a building society and that on an ordinary mortgagee. This view is supported by case law.¹⁸³

As a minimum, the agent is required to insert an advertisement in a local paper once a week for two consecutive weeks. No reference is made to the Society's involvement, nor to the fact that it is a forced sale, nor to any "acceptable" sale price. The latter practice is adhered to for the purpose of testing the accuracy of the valuation offered by the estate agent, and the one that the Society had obtained independently, without distorting the market place by pre-setting a figure. If no satisfactory response is received as a result of the initial effort the estate agent is then directed to commence further advertising which will include a statement to the effect that "offers over. . . will be considered".¹⁸⁴ Any offer received is forwarded to the head office for its consideration.

In the event that an acceptable offer is not immediately forthcoming, the property will remain in the market place until such time as one is received.¹⁸⁵ In the interim advertising is undertaken on a regular basis. While it is clear in law that under the statutory duty there is no obligation on a building society to postpone a sale until such time as a better price can be obtained, the practice described above may go beyond the present concept of acceptable conduct.¹⁸⁶ The justification is in part a practical one and in part a precautionary one arising from the fact that the sale mode is being restricted to the receipt of offers. To do otherwise would prevent the foreclosing creditor from being certain that he had acted reasonably if, for example, an arbitrary listing period had to be set. This practice avoids the task of attempting to foresee local market

¹⁸² 10 & 11 Eliz. 2, c.37, s.36(1)(a) (U.K.).

¹⁸³ The opinion is justified if one compares the duty of care formulated in *Cuckmere* with that in *Reliance Permanent Building Society v. Harwood-Stamper*, [1944] 1 Ch. 362 (Ch. D.). The latter dealt with the standard of care as determined by the statutory provision (then s.10). Although the decision primarily responded to the task of defining the phrase "best price" the result, in the writer's view, would have been no different had the court been able to use the standard formulated in the *Cuckmere* decision.

¹⁸⁴ Although the initial cost of advertising is borne by the estate agent he may expect to be reimbursed in total for all out of pocket expenses in addition to receiving a commission based on the selling price ultimately obtained.

¹⁸⁵ The writer was advised by officers of the Society that in the majority of cases the property is sold relatively quickly, otherwise it remains on the market for a considerable period of time.

¹⁸⁶ *Reliance Permanent Building Society v. Harwood-Stamper*, *supra*, footnote 183.

conditions which may well fluctuate by the month or the year. Of course such uncertainties could be minimized if the sale were effected by way of public auction. It is rare for the Society to adopt this sale mode, and if it did so it would be on the recommendation of the estate agent.

The exposure of property to the market place by usual commercial practice should ensure that the standard of care will be met in most situations. However, the employment of a real estate agent should not be mandatory. If other means exist by which the property can be exposed to the greatest number of people expected to have an interest in its purchase, then such opportunities should be permissible. Therefore, whether or not property should be listed with real estate agents is but one consideration. How it may be exposed effectively to the market place is another. Even if we exclude the use of the realtor it would only seem reasonable that expert advice be sought when searching other avenues. However, where the foreclosing creditor or his solicitor conclude that they have the necessary experience to make such a determination, they must do so at their own peril. This writer believes that the utilization of real estate agents should become the norm, rather than the exception, regardless of the foreclosure process pursued.

As to the proper sale mode, the choice is restricted to the receipt of tenders, a public auction or to a private sale effected through the solicitation of offers with or without the involvement of real estate agents. Provided that proper marketing techniques are adopted in the first instance, then the choice should depend on which of these is most likely to maximize the sale price. This decision should be made with the advice of those most familiar with the sale of property of the class to be foreclosed. Overall, the writer believes the solicitations of offers through the efforts of an agent to be the most effective means for disposing of property.

It may be that in sales of undeveloped land and other commercial properties a disposition by auction is proper.¹⁸⁷ It is difficult to justify this sale mode in regard to residential structures because of the customary practices followed when effecting a voluntary sale. Ultimately the adoption of a particular sale mode must be justifiable in terms of effectiveness, not merely supported by reliance on anachronistic traditions. However, proper exposure to the market place and the selection of a proper sale mode will not necessarily ensure an acceptable sale price.

¹⁸⁷ The propriety of this sale mode in the context of commercial industrial and investment real estate has been considered by one Toronto company. The proposal is to establish an auction house which would promote, in foreign and Canadian markets, at least 100 major properties valued at more than 500 million dollars. In so doing the company hopes to provide an alternative method of marketing which is usually confined to forced sales. On the basis of past experience, the promoters feel that it is as successful as other conventional marketing techniques: see *The Globe and Mail*, September 5, 1984, p. B10 (Tor. & Nat. Editions).

First, a determination as to the adequacy of all offers has to be made, or, alternatively where the sale is by auction there is the requirement of setting a proper reserve bid. Provided that reasonable marketing has been undertaken then the value of the property might be presumed to be reflected in the highest price offered. To a certain extent this approach appears to dispense with the need to obtain one or more appraisals. But if the sale is to mirror a voluntary one, then a mortgagee-vendor must be able to bargain on an equal footing with potential purchasers. Competent appraisals should serve only as a basis for determining the theoretical value of the property and must not be taken as accurately reflecting what any single purchaser within a particular time frame is willing to offer. The adequacy of any offer is a question of judgment as is the setting of a reserve price. While the minimum acceptable price will be influenced by the creditors' investment in the property, it cannot be determined without regard to the interests of persons affected by this decision as reflected in the appraised value.

Second, the amount of time which is to elapse before a private sale is to be consummated remains a critical determinant when approaching the standard of care. For example, the judicial sale, by custom, envisages a process whereby at some specific time a court will grant its *imprimatur* to the proceedings, including the sale price. While the English practice of leaving the property on the open market until a reasonable offer is received may go beyond the duty presently imposed at law, it is perhaps the only practical choice for residential structures. In a voluntary sale the time a property remains on the market varies from city to city.

For example, in July of 1984 the average length of time in which to effect a sale from the listing date in Collingwood, Ontario was 113 days, whereas in Ottawa it was only 39 days.¹⁸⁸ Therefore, although the law may dictate that the creditor does not have to postpone his right to sell until the most propitious moment, an arbitrarily fixed time period is hard to support. The demand for housing, for example, in any one community depends upon a number of variables which may include demographic influences, the cost of credit, consumer preferences, income levels, inflation and rates of unemployment. These factors fluctuate not only within a particular period of time but also vary on a national, regional or local basis. Although a judicial sale may not always be appropriate in

¹⁸⁸ The average selling times of residential properties as of July, 1984, for the following cities was obtained from real estate boards utilizing computerized systems of record: Vancouver, 60 days; Halifax, 65.7 days; Niagara Falls, 86 days; Belleville, 59 days; Muskoka, 62 days; Sudbury, 71 days; North Bay, 60 days; St. Catharines, 53 days; Barrie, 59 days. Most boards do not accumulate this information since only properties listed through the multiple listing service show expiry dates. I am indebted to David Hawkins and E. Mack Parliament of the Canadian Real Estate Association for their co-operation and assistance in providing this information.

liquidating a debt secured by property of this class, if it is the chosen or the required method, ample time must be given before a sale is to be completed. Alternatively, the creditor must be expected to convince the court of the adequacy of sale attempts.

Undoubtedly one of the most problematic aspects of any sale process is the measuring of an appropriate marketing period where the market is severely depressed or non-existent. As outlined earlier one solution is to abolish actions on the covenant in defined circumstances, but the writer declines to incorporate this possibility into the model until the full implications of such legislation have been analysed and other options are reviewed. For example, since the present scheme of mortgage insurance, though widespread and paid for by the debtor, does not eliminate the insurer's right of subrogation, consideration could be given to a scheme which eliminates this right.

The immediate solution is found in the standard of care already proposed above, that is, the property should remain on the market until a reasonable price is obtained. This decision will, in part, be dependent upon local market conditions regarding voluntary sales and in part upon the adequacy of the offer when compared to the appraisal value. Those conditions should provide some guidance as to the time needed to market property and provide a basis for determining the general effects of market activity on sale prices. This solution appears to reject the creditor's common law right to proceed expeditiously and instead impose upon him or a court an obligation to refrain from accepting an offer until market conditions have improved. Indeed, the writer recognizes this restriction where the market place is having a similar impact upon voluntary sales.

The proposal advanced is based on the informal judgment that the problem of price adequacy cannot be addressed properly unless the impact of economic instability is recognized as a variable integral to any liquidation process. Fluctuations in economic activity occur in differing communities and in different degrees of severity. The economic forces seem unpredictable and defy precise measurement at any one point unless there is a total collapse of the market. Whether or not a particular market is depressed is a subjective appreciation, and often ignores the fact that fluctuations in market values of property appear to be inevitable in all economic climates. The value of real property and the time needed to effect a sale cannot be predetermined other than within the context of presently existing local conditions which may or may not reflect the national or provincial experience. It is the marketplace which should dictate the acceptable price and the desirable time frame for marketing the security. The courts and creditors must respond to the economic climate prevailing at the time when foreclosure processes are initiated, rather than proceeding on the basis of historical and unchallenged prac-

tices which cloud the problem of determining what is a reasonable or acceptable sale price.

In the context of a depressed market, the solution offered may be viewed with skepticism in light of the foreclosure experience witnessed by Calgary homeowners in 1984.¹⁸⁹ The fact that housing prices had fallen significantly in a three year period may be, in part, the consequence of an unprecedented demand for housing during the late seventies, which resulted in sale prices in excess of those expected even during an inflationary period. Alternatively this phenomenon may have been due to sacrificial prices willingly accepted by foreclosing creditors who knew that there was no demand. Indeed, the description of this particular market as "depressed" may not be accurate. Perhaps it is more aptly characterized as one that was or is non-existent. If, however, sale prices based on equivalent voluntary exchanges attest to the forty per cent drop in market value, then the loss should rest with the debtor. Where any marked discrepancy exists between forced sale prices and those offered in the open market, the creditor must bear the loss represented by the difference.

Undoubtedly there will be instances where there is no market for a particular item. For example, persons living in communities dependent upon a single employer which closes its doors will usually find that any sale attempts, voluntary or otherwise, are unsuccessful. In such a case the creditor might as well leave the debtor in possession and forego his remedial options on the basis of impracticality. However, the writer does not rule out the possibility of the creditor pursuing an action on the covenant. What is to be rejected is the idea of selling the property for a nominal or arbitrary amount to a purchaser, whether it be a third party, in particular the foreclosing creditor, with a view to pursuing a deficiency judgment. Until other solutions, such as the abolition of deficiency judgments and mortgage insurance, are adequately examined there is little else which a foreclosing creditor can be required to do.

Conclusion

When viewed inter-provincially the disparate treatment accorded debtors in this country suggests that sale practices and the governing law were more likely the result of an unsuccessful attempt to resolve a "Rubic's Mortgage Cube", derived from English antecedents, rather than from any conscious effort to maximize sale prices. Notwithstanding that observation, the procedures followed and the law applied in the provinces could in most instances be explained in historical terms. However, the practices defy justification when contrasted with the procedures and the law as applied in England today.

¹⁸⁹ See text, *supra*, at footnote 15.

In the majority of provinces the entire sale process is geared toward the standardization of practices with the result that form tends to dominate substance. Unfortunately, other than in British Columbia, and Ontario, the primary objective of ensuring the adequacy of sale price seems to have been lost in an irrational attachment to irrelevant sale practices.¹⁹⁰ The problem remains as relevant in the context of a judicial sale as it in regard to the power of sale. Judicial sales theoretically minimize the possibility of a sale at an undervalue, and judicial scrutiny in theory offers guarantees that remedies will be exercised in the best interests of all parties. Yet, in the majority of provinces the evidence does not support such a generalization.

The judicial sale will remain as ineffective as the power of sale so long as there remains an unquestioning reverence for the past. Admittedly, in those provinces where confirmation proceedings are an integral part of the judicial process there is at least the possibility that property will be sold at a reasonable price. However, the proper exercise of this judicial function will be prejudiced if courts are consistently confronted with non-competitive offers and highly speculative opinions as to value.

While judicial orders of confirmation virtually guarantee immunity against a successful challenge so far as sale price is concerned, the foreclosing creditor exercising the power of sale in Ontario is still required to compensate those who suffer a loss at his hands. Thus, in practice, we find differing standards of care. Those who are able, and so choose to pursue this extra-curial remedy are likely to be held to a standard encompassing good faith and reasonable care.

Should present sale practices and the governing law remain intact in the majority of provinces, then the abolition of actions on the covenant, regardless of the status of the debtor, might be viewed as a partial solution to this problem. The immediate and alternative solution is found in the standard of care proposed. As to the right of the foreclosing creditor to purchase its security, this possibility should be eliminated, particularly in cases of sales pursuant to a power.

¹⁹⁰ In light of the decision in *Canada Permanent Trust Co. v. King Art Developments Ltd.*, *supra*, footnote 27, and changes in such practices, the exclusion of Alberta may be unwarranted.