Claims That Survive Bankruptcy, Delayed Discharges, and the Stay of Proceedings: Things Bankrupts Often Don't Know About bankruptcy

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Presented by:
Alexander Mosaico
Mosaico Law
Edmonton, Alberta

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THINGS BANKRUPTS OFTEN DON'T KNOW ABOUT BANKRUPTCY**

INTRODUCTION

The purpose of this paper is to provide an introduction to the procedure and law regarding: claims
that survive bankruptcy under s 178(1) of the *Bankruptcy and Insolvency Act* (the "**BIA**"), opposition
to a bankrupt's discharge from bankruptcy under 173 and 172.1 of the *BIA*, and the stay of
proceedings created by virtue of s 69.3 of the *BIA*. In particular, I will attempt to provide some useful
tips for lawyers who have very little bankruptcy experience. This paper is meant to be an
introduction, and not a detailed analysis of the subject matter.

THE STAY OF PROCEEDINGS

Section 69.3 of the *BIA* states that, subject to some exceptions, "on the bankruptcy of any debtor, no
creditor has any remedy against the debtor or the debtor's property, or shall commence or continue
any action, execution or other proceedings, for the recovery of a claim provable in bankruptcy". This
provision enacts an automatic stay of proceedings, which begins on the date of bankruptcy, and
continues until the date when the trustee is discharged.[1] In the case of a Notice of Intention, a stay
of proceedings arises by virtue of *BIA* s 69(1); s 69.1 in the case of Division 1 Proposals, and s 69.2
in the case of Consumer Proposals; however, the focus of this paper will be on the stay of
proceedings arising in the case of a bankruptcy, ie. *BIA* s 69.3[2].

Practically, what this means is that, with few exceptions, any legal action being taken against a
bankrupt is stayed: if you have started an action against a bankrupt regarding a pre-bankruptcy
liability, it is stayed; if you are about to start an action against a bankrupt regarding a pre-bankruptcy
liability, you may no longer do so without leave of the court (discussed below). One of the most
common concerns civil litigators will have when they discover the stay of proceedings in respect of a
potential defendant is the impact it will have on their limitation period. Some counsel will apply to
have a stay lifted just to the point where a claim may be filed and served, to ensure that they will not
have a limitation issue later in time. However, as per Houlden & Morawetz, the stay of proceedings
has the effect of suspending statutory limitations periods[3]. But be careful: limitation periods are only

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[1] Professor Roderick Wood, *Bankruptcy & Insolvency Law*, 2nd ed., p 168

[2] There are differences in the scope of the stay under each provision; for example the treatment of actions by secured
creditors, lessors, and regulatory bodies varies depending on the applicable stay provision under the *BIA*.

[3] *Houlden & Morawetz, Bankruptcy and Insolvency Analysis: Bankruptcy and Insolvency Law of Canada*, fourth edition, by
the Honourable Mr. Justice Lloyd W. Houlden, Mr. Geoffrey B. Morawetz, and Dr. Janis P Sarra: WestlawNext ("Houlden &
Morawetz") at G47; see also *Environmental Metal works v Murray et al*, 2013 ABQB 479 at 24; see *Decker v Canada et al* ,
2010 BCA 189 for a further discussion of limitation periods and the discharge of the trustee.

suspended where the stay of proceedings applies (discussed below); so, with respect to claims arising after bankruptcy, secured claims, or proprietary claims, for example, the limitations clock continues to run.

The stay of proceedings only applies against the bankrupt person and generally does not affect actions against third parties, such as guarantors of the bankrupts debts[4], or parties that are jointly bound with a bankrupt to pay a debt.[5]

Only claims that are provable in bankruptcy are subject to this automatic stay of proceedings. "Claims provable in bankruptcy" are defined under s 121(1) of the *BIA* as follows:

> All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

So, for example, claims that arise after the date of bankruptcy are not automatically stayed. According the B.C. Superior Court, a decision by the securities commission that occurs after the date of bankruptcy is <u>not</u> a claim provable in bankruptcy, even though the impugned conduct occurred <u>prior</u> to the bankruptcy[6] (there is more discussion on this case later in this paper).

However, while a creditor with a post-bankruptcy claim can take action against a bankrupt, the said creditor will generally not be able to enforce any judgment it obtains against the bankrupt, as all of the bankrupt's property is vested in the trustee, as discussed below.

As indicated, the claim must have existed on the date of bankruptcy in order to be a provable claim.[7] According to Professor Wood, there are two main policy reasons for this. First, it ensures efficiency, reducing the costs associated with multiple discrete claims. And second, it ensures an orderly, *pro rata*, sharing of the assets of the debtor among the creditors, which means that the value received for the assets will likely be enhanced.[8]

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[4] See *G-Star Canada Inc v John Stiles,* 2014 ABQB 33 – Master Robertson looked carefully sat the wording of the guarantee in that case in determining that there would be no stay pending the outcome of the bankruptcy of the principal debtor

[5] See Houlden & Morawetz, at H69 for a discussion regarding the effects of bankruptcy on third parties who are also liable for the bankrupt's debts (co-makers of notes, guarantors, co-defendants, etc).

[6] *Re Thow,* 2009 BCSC 1176 (CanLii)

[7] *Ibid*, at p 167

[8] *Ibid*, at p 166