September 9, 2024

Supreme Court of Canada Rules that Securities Commissions' Administrative Penalties Do Not Survive Bankruptcy Discharge

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Case commented on: *Poonian v British Columbia (Securities Commission)*, 2024 SCC 28 (CanLII)

With the release of *Poonian v British Columbia (Securities Commission)*, 2024 SCC 28 (CanLII), the Supreme Court of Canada has settled the question about the status of provincial securities commissions' unpaid administrative penalties and discharge orders upon a bankrupt's discharge. The Court determined that administrative penalties do not fall under the statutory exceptions in sections 178(1)(a) or (e) of the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 (BIA) meaning these penalties are discharged upon a bankrupt's discharge. Disgorgement orders, however, are captured by the s 178(1)(e) exception, and will not be discharged.

Facts

In August 2014, the British Columbia Securities Commission (the Commission) found that the appellants, Thalbinder Singh Poonian and Shailu Poonian, together with their friends, relatives, and associates, had engaged in market manipulation contrary to s 57(1) of the *Securities Act*, RSBC 1996, c 418, between 2007 and 2009, defrauding investors of millions of dollars. The Commission ordered Mr. Poonian to pay $10 million and Ms. Poonian to pay $3.5 million in administrative penalties, and Mr. Poonian to pay ~$1.3 million and ~$1.1 million jointly and severally with another participant, and Ms. Poonian ~$3.1million in disgorgement damages.

In April 2018, the Poonians made a voluntary assignment in bankruptcy. When they applied for a discharge from bankruptcy in February 2020, the Commission and the Canadian Revenue Agency opposed it. The Supreme Court of British Columbia dismissed the Poonians' application for discharge in April 2020 (*Poonian (Re)*, 2020 BCSC 547 (CanLII)) and they currently remain undischarged bankrupts (at para 10).

Before the Supreme Court of British Columbia, 2021 BCSC 555 (CanLII), the Commission applied to have the court declare that the amounts the Poonians owed to it would not be released after the Poonians had been discharged from bankruptcy, under ss 178(1)(a), (d) and (e) of the BIA. The chambers judge allowed the Commission's application. He found that the exceptions in s 178(1)(a) and (e) applied, meaning the debts would survive a discharge.

The Poonians appealed to the British Columbia Court of Appeal, arguing against the chambers judge's interpretation of the BIA exceptions. In *Poonian v British Columbia (Securities Commission)*, 2022 BCCA 274 (CanLII), the Court of Appeal upheld the chambers judge's

conclusion that the Commission's administrative penalties and disgorgement orders came within the s 178(1)(e) exception, as the Poonians' debt had arisen through them obtaining property through fraudulent misrepresentation.

SCC Decision

The Supreme Court considered whether the Commission's administrative penalties and disgorgement orders fall within s 178(1)(a) or (e) of the BIA, such that they would not be released by an order of discharge from bankruptcy.

For a debt to survive bankruptcy under s 178(1)(a), a creditor must establish the debt is a fine, penalty, restitution order or other order similar in nature that was "imposed by a court". The Court found that an administrative tribunal or regulatory body does not fall within the word "court" (at para 46) and that registering an administrative decision with a court "does not change the fact that it was made an imposed by an administrative decision maker", as in, it does not make it "imposed by a court" (at para 49). For those reasons, the exception in s 178(1)(a) could not apply, as an administrative decision cannot be one that is "imposed by a court" (at para 51).

Under s 178(1)(e), the BIA says that an order of discharge does not release the bankrupt from "any debt or liability resulting from obtaining property or services by false pretences or fraudulent misrepresentation…" The Court maintained that the creditor must establish three elements for a debt or liability to fall under s 178(1)(e): (1) false pretences or fraudulent misrepresentation; (2) a passing of property or provision of services; and (3) a link between the debt or liability and the fraud (at para 54).

Under the first element, the Court followed the long line of case law that relied on *Derry v Peek* (1889), 14 App. Cas. 337, which laid out the elements for establishing fraudulent misrepresentation: (1) a representation was made; (2) the representation was false; (3) the representation was made knowingly, without belief in its truth; and (4) the creditor relied on the representation and turned over property to the debtor. For false pretences, the elements are the same except that detrimental reliance is not required. However, for the purposes of s 178(1)(e), which requires that property or services be obtained as a result of the fraudulent misrepresentation or false pretences, that difference is irrelevant (at para 64).

Under the second element, the bankrupt need not be the recipient of the property of which the creditor was deprived; the element would be satisfied if the property passes to a third person at the direction of the bankrupt (at para 73). Under the third element, the expression "resulting from" requires a causal link between the debt and the false pretence or fraudulent misrepresentation, as in, the debt must have arisen as a result of the false pretence or fraudulent misrepresentation (at para 74).

After applying the requirements, the Court concluded that the Commission's administrative penalties did not result from the Poonians' fraudulent scheme, but that they arose "indirectly as a result of the Commission's decision to sanction the Poonians for having obtained property through deceitful statements to investors" (at para 103). As a result, these administrative penalties did not fall under the s 178(1)(e) exception and would not survive the Poonians' bankruptcy.

Conversely, however, the Commission's disgorgement orders were captured by the s 178(1)(e) exception. These amounts represented the amounts the Poonians obtained as a result of their fraudulent market manipulation, thereby establishing the direct link between their fraud and the Commission's orders (at para 113).

In summary, the majority of the Court allowed the appeal in part. It affirmed the Court of Appeal's conclusion that the disgorgement orders were caught by s 178(1)(e) but overturned its conclusion that the administrative penalties were also caught by s 178(1)(e) (at para 115).

Karakatsanis and Martin JJ dissented, maintaining that both orders survived the bankruptcy and would have dismissed the appeal. They disagreed with each other, however, on the scope of the causation requirement, contemplated by the words "resulting from" in s 178(1)(e) (at paras 117-18).

Commentary

One of the two main goals of bankruptcy is the financial rehabilitation of the debtor, known as a financial fresh start, which has two aspects. The first aspect is the bankrupt's eventual discharge from bankruptcy, meaning the debtor does not remain a "bankrupt" forever. The second aspect is the discharge of debts at the end of the bankruptcy process, meaning the bankrupt does not have to pay the debts they carried when they entered bankruptcy proceedings. This "fresh start" policy, which is found under s 178(2) of the BIA, allows the discharged bankrupt to reintegrate into economic life and once again become a productive member of society without having their previous debts holding them back.

There are some exceptions to the fresh start, found in s 178(1), which prevent certain debts from being discharged. This comment will focus on the false pretences and fraudulent misrepresentation exception.

The Court found that a debt or liability resulting from obtaining property or services by false pretences or fraudulent misrepresentation encompasses disgorgement orders but not administrative penalties. Professor Thomas Telfer and I advocated for this position in our two papers, Jassmine Girgis & Thomas G. W. Telfer, "Do Securities Commission Debts Survive a Bankruptcy Discharge? An Analysis of *Poonian v. British Columbia (Securities Commission) (BCCA)*" (2023) 67 Can Bus LJ 438 and Jassmine Girgis & Thomas G. W. Telfer, "The Fraudulent Misrepresentation and False Pretences Exception to the Bankruptcy Discharge: Balancing the Debtor's Fresh Start with Confidence in the Credit System" (2022) 20 Ann Rev Insol L, 2022 CanLIIDocs 4295.

The exceptions to discharge set out in s 178(1) are, for the most part, debts that arise from morally blameworthy conduct that society has deemed to be undeserving of discharge. But this is not morally blameworthy conduct in general – the provision is not a catch-all. It must be conduct that falls specifically within the exceptions. For this reason, the exceptions must not be interpreted too broadly, as an overly broad interpretation, which is what the British Columbia Court of Appeal gave, undermines the fresh start goal. An overly narrow interpretation is also not ideal, as it further

victimizes creditors from qualifying for the protection Parliament intended for them to have. For these reasons, an appropriate balance is necessary when interpreting these provisions.

The Supreme Court's interpretation struck that appropriate balance by deciding that the Commission's administrative penalties would not be caught by the provisions, and would therefore be discharged, but that the disgorgement orders would not be discharged. By reverting back to the policy underlying the provisions, namely that these provisions were enacted to provide creditors victimized by the debtor's fraudulent conduct with the opportunity to recoup their losses, the Court was able to distinguish between the two types of orders. The administrative penalties did not arise from the debtor's fraud and the Commission had not been victimized by the debtor. The disgorgement orders, however, were different. They were made under s 161(1)(g) of the *Securities Act*, the provision enacted "to compel a wrongdoer to give up any ill-gotten amounts", providing a direct link between the fraud and the orders. The amount retrieved under these orders could also be used to compensate the victims of the Poonians' fraud (at para 112).

I have maintained that this is a significant setback for securities commissions, and that the federal government may consider amending the BIA to provide them with more protection. But that protection should not come through an overly broad reading of the legislation. The legislated priorities and the exceptions to discharge are products of hard-fought battles by various stakeholders, all of whom are also impacted by the debtor's bankruptcy. It is therefore vital that courts interpret the legislation while considering the policy underlying it, without providing overly narrow or broad interpretations that grant or deny privileges that Parliament did not intend.

This post may be cited as: Jassmine Girgis, "Supreme Court of Canada Rules that Securities Commissions' Administrative Penalties Do Not Survive Bankruptcy Discharge" (9 Sept 2024), online: ABlawg, http://ablawg.ca/wp-content/uploads/2024/09/Blog_JG_Penalties&Bankruptcy.pdf