

COURT FILE NUMBER 2201 09319
COURT COURT OF KING'S BENCH OF ALBERTA
JUDICIAL CENTRE CALGARY

Clerk's Stamp

PLAINTIFF ARNAKI LTD.
DEFENDANT SOLVAQUA INC.

DOCUMENT **BRIEF OF ARNAKI LTD.**

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INTRODUCTION

1. This Brief addresses the narrow issue (the “**EDC Assignability Dispute**”) remaining to be decided that will allow conclusion of this receivership: assignment of insurance related claims contained in the definition of “**Solvaqua Claims**” (as defined in the Stalking Horse Agreement, as amended) to 2464525 Alberta Ltd. (the “**Stalking Horse Purchaser**”).
2. In its position as secured lender, the Plaintiff, Arnaki Ltd. (“**Arnaki**”), supports inclusion of the insurance related claims in the definition of Solvaqua Claims and the order sought by MNP Ltd. (the “**Receiver**”).
3. The debtor, Solvaqua Inc. (“**Solvaqua**”), is entirely dormant and the Receiver has confirmed it will not proceed with contestation of the insurance related claims. Export Development Canada (“**EDC**”) is using the non-assignability clause in the contracts of insurance to insulate EDC’s rejection of claims already submitted by Solvaqua. As the only party with an interest in recovery under the rejected claims and the willingness to pursue the claims, Arnaki’s right to contest the rejected claims through assignment to the Stalking Horse Purchaser should be confirmed by this Honourable Court.

FACTS

4. On August 19, 2022, the Court of King’s Bench of Alberta (then known as the Court of Queen’s Bench of Alberta) granted a receivership order appointing the Receiver as receiver over all the current and future assets, undertakings and properties of Solvaqua.¹

¹ Third Report of the Receiver in the Matter of the Receivership of Solvaqua Inc. dated August 30, 2023 (“**Third Report**”) at para 1.

5. The receivership order was granted following Arnaki's application. Arnaki has a secured claim of approximately \$7.9 million pursuant to various general security agreements.²
6. On April 9, 2020, Solvaqua entered into a written agreement with Vivaventures Inc. ("**Vivakor**") for purchase of water treatment equipment by Vivakor from Solvaqua (the "**First Transaction**").³
7. EDC issued a policy of Export Receivables Insurance for the First Transaction to Solvaqua, effective May 1, 2020. One of the insured events under the policy was "Default (non-payment)" by the equipment purchaser, Vivakor.⁴
8. On August 31, 2020, Arnaki agreed in writing to provide Solvaqua with financing of USD \$2M and took security in the form of a General Security Agreement.⁵
9. Arnaki further secured its position by requiring that Solvaqua provide evidence of EDC having insured Solvaqua's receivables from the First Transaction.⁶
10. Solvaqua delivered a written Direction to Pay to EDC, instructing EDC to pay Murchinson Ltd.,⁷ the company with overall investment control of the ultimate parent company with an indirect interest in Arnaki. Internally at Murchinson and Arnaki, the Direction to Pay was referred to as an "assignment."⁸

² Third Report at para 2.

³ Affidavit of Dan Barona sworn November 30, 2022 ("**Barona Affidavit**"), at para 3.

⁴ Barona Affidavit at paras 4-5.

⁵ Affidavit of Ariel Belilo affirmed August 15, 2022 ("**Belilo Affidavit**"), at paras 7, 10-11.

⁶ Belilo Affidavit, Exhibit "B", s 3.1(h).

⁷ Barona Affidavit, Exhibit "E".

⁸ Undertaking Response to q 85 of Paul Zogala, Affidavit of Elvina Hussein sworn July 6, 2023, Exhibit "A".

11. There is no dispute that the security of EDC's insurance was important to Arnaki and probably the largest determining factor accounting for why Arnaki agreed to advance funds to Solvaqua.⁹
12. Arnaki eventually entered into two further similar loan agreements with Solvaqua relating to other transactions, each of which was secured by a similar GSA with additional security to be provided by insurance from EDC.¹⁰
13. Each of the three EDC insurance policies attaches a set of General Terms and Conditions which includes the following provision:

38. You cannot assign the Policy or any right, title or interest in it to anyone without our prior consent.¹¹
14. All of the parties affected by the EDC Assignability Dispute agree that:
 - (a) following the failure of the planned transactions with its buyers, Solvaqua commenced claims under the EDC policies;
 - (b) EDC paid USD \$1,386,000 on the (first) Vivakor-related claim, which was paid to Murchinson consistent with the Direction to Pay;¹² and
 - (c) EDC has rejected Solvaqua's claims under the second and third insurance policies entirely.
15. Arnaki, as the secured party to whom funds payable under the claims would be directed in satisfaction of Solvaqua's debts to Arnaki, has sought to dispute EDC's rejection of Solvaqua's other insurance claims, and the quantum paid by EDC under the Vivakor-

⁹ Transcript – Questioning of Paul Zogala on December 21, 2022, at p 25, line 22ff.

¹⁰ Belilo Affidavit at paras 7-8, 10.

¹¹ Barona Affidavit, Exhibit "D".

¹² Barona Affidavit at para 7.

related claim. EDC relies on the non-assignment provision in the General Terms and Conditions to oppose assignment of the ability to **contest** EDC's rejections to the Stalking Horse Purchaser.

ISSUE

16. Does the non-assignment provision in the EDC insurance policies' General Terms and Conditions prevent assignment of the insurance claims to the Stalking Horse Purchaser?

ARGUMENT

17. Arnaki submits that:
- (a) nothing about the insurance policies prevents Solvaqua's assignment of the proceeds of the insurance claims and, with the claims already crystalized through Solvaqua's submission of claims, the ability to contest EDC's rejections should be transferred to the Stalking Horse Purchaser as an incident of that assignment; and
 - (b) EDC's withholding of consent to the assignment is an unreasonable attempt to block the only party with an interest in contesting the rejections, Arnaki via the Stalking Horse Purchaser, inconsistent with the purpose of the policy's non-assignment provision.

No Prejudice from Assignment of Proceeds

18. First, it is necessary to distinguish between assignment of an insurance policy and assignment of the proceeds of an insurance policy. As explained by Barbara Billingsley in her textbook, *General Principles of Canadian Insurance Law*:

By assigning the proceeds of an insurance contract, the insured promises a third party that money payable to the insured under the contract will be paid directly to the third-party assignee. The assignment addresses only who will

receive the payment of insurance funds: the insurance contract itself remains exclusively between the insured and the insurer. This means that the third party's ability to recover insurance proceeds is entirely dependent upon the insurer's contractual obligation to pay the insured. So, for example, if the insured has forfeited its right to coverage by breaching the insurance contract, the insurer has no obligation to pay the insured or the third party. The assignment of proceeds is simply an assignment by the insured of any monies owed to the insured under the insurance contract. The assignee is not a party to the insurance contract and so does not need an insurable interest in the subject-matter of the insurance.

The insured's agreement to assign the proceeds of insurance to a third party does not affect the insurer's underwriting considerations because the assignment does not change the risk assumed by the insurer. So, an assignment of proceeds can take effect without the insurer's advance knowledge or consent. The ability of the insured to assign insurance proceeds depends solely upon the validity of the insurance contract.¹³

19. Here, there is no doubt that EDC would have paid the proceeds of Solvaqua's insurance claims to Solvaqua's designated payee, Murchinson, had EDC not rejected Solvaqua's second and third claims: that is precisely what happened with respect to the portion of Solvaqua's insurance claim with respect to the First Transaction that EDC allowed.
20. As Arnaki is the only party with an interest in contesting EDC's rejections, there is simply no prejudice to a transfer of the claims to the Stalking Horse Purchaser. Solvaqua's claims have already been submitted, there will be no change to what was insured by EDC (the risk of default by overseas buyers), and there is no change to the risk profile that EDC insured. The claims are entirely crystalized and all that is sought is the *procedural* economy that would follow from the ending the receivership and allowing the Stalking Horse Purchaser to contest the rejections as assignee of Solvaqua's claims.

¹³ Barbara Billingsley, *General Principles of Canadian Insurance Law*, 3rd Ed. (LexisNexis Canada Inc., 2020), s A.2.a Assignment of the Proceeds of an Insurance Contract [footnotes omitted].

21. While dealing with whether the specific provisions of s. 132(1) of Ontario's *Insurance Act*¹⁴ limited the Court's equitable jurisdiction to assign rights under an assignment of insurance proceeds, the Ontario Superior Court of Justice dealt with a somewhat analogous situation in *Ernst & Young Inc. v. Chartis Insurance Company of Canada*.¹⁵ In holding that nothing about s. 132(1) limited the Court's jurisdiction, Lederer J. observed that:

[54] The right to receive an indemnity under an insurance contract is a "chose in action" and, as such, is capable of being assigned. *McGillivray and Parkington on Insurance Law*, 11th Edition, para. 20-005, at p. 560, states:

...the assured may wish merely to transfer the right to recover under the policy. This is a chose in action and can be effectively assigned at common law provided that the requirements of s. 136 of the Law of Property Act 1925 are fulfilled.

[55] This was given effect in *1124980 Ontario Inc. v. Liberty Mutual Insurance Co.* 2003 CarswellOnt 1474; 2003 CanLII 45266 (ON SC), 33 B.L.R. (3d) 206. In that case, employees and retirees of Inco Ltd. were to receive certain benefits, including payment for prescription drugs. Inco Ltd. financed the plan itself, but it was administered by the respondent insurance company. The applicant owned and operated a pharmacy. The applicant refused to enter into a letter of understanding with Inco Ltd. to limit its dispensing fee charged under the Inco Ltd. benefit plan. In response, Inco Ltd. instructed the respondent to refuse to recognize assignments of benefits made by individuals covered under the plan in favour of the applicant. Inco Ltd. acknowledged the obligation to pay the cost of prescriptions and dispensing fees the applicant charged to those entitled to benefits, but it refused to allow the right of assignment to be exercised in favour of the applicant to enable direct payment to the pharmacy. In part, the question was whether the assignments were valid. In concluding that they were, Madam Justice Epstein observed:

¹⁴ RSO 1990, c 1.8.

¹⁵ 2012 ONSC 5020 (CanLII), <<https://canlii.ca/t/fssqf>> [*Ernst & Young*].

...Where an insurer receives a notice of an assignment of proceeds payable under an insurance policy, the insurer is obliged to pay the proceeds to the assignee and, although this may be pursuant to the contract with the assignor, the insurer pays out the assignor at its peril.

...

This right to receive an indemnity under an insurance contract is a chose in action and is capable of being assigned.

(1124980 Ontario Inc. v. Liberty Mutual Insurance Co., supra, at paras. 45 and 46)

[56] Unlike *1124980 Ontario Inc. v. Liberty Mutual Insurance Co.*, in the case I am asked to decide, **there is no assignment from Central Guaranty Trust to Ernst & Young Inc. There is, however, the order of Mr. Justice Houlden. It specified that Ernst & Young Inc. can continue the action and, if successful, look to any applicable policy of insurance to satisfy the judgment.** By his order, Mr. Justice Houlden reserved any proceeds from insurance to satisfy any judgment or settlement of the action, free of any claims by the Provisional Liquidator of Central Guaranty Trust. The order also made clear that Ernst & Young Inc., if successful in the action, was to have no right to issue execution against the estate of Central Guaranty Trust. **In this way, the proceeds from any applicable insurance policy would be available to satisfy any judgment made in favour of Ernst & Young Inc. Other creditors would not be prejudiced by the continuation of the action.** The estate of Central Guaranty Trust would be available in the liquidation. This is consistent with the approach taken in *Algoma Steel Corp. v. Royal Bank of Canada*. Nonetheless, counsel for Chartis submitted that Mr. Justice Houlden did not have the jurisdiction to make the order.¹⁶

22. As no other creditors will be prejudiced, and EDC's risk profile is unchanged, Arnaki submits that a similar approach should be taken regarding assignment of the insurance claims to the Stalking Horse Purchaser.

¹⁶ *Ernst & Young*, at paras 54-56.

EDC's Consent Cannot be Unreasonably Withheld

23. It is now an established principle of Canadian contract law that:

the duty to exercise contractual discretion in good faith requires the parties to exercise their discretion in a manner consistent with the purposes for which it was granted in the contract, or, in the terminology of the organizing principle in *Bhasin*, to exercise their discretion reasonably.¹⁷

24. The contractual purpose of EDC's consent being required to transfer the policies or rights in the policies to third parties is to prevent changes in the risk that EDC has insured, absent EDC's consent. This is a reflection of the nature of a contract of insurance, in which the insurer provides coverage to a specific insured based on the likelihood of loss occurring to that insured in respect of the subject-matter of the insurance. For instance, EDC could reasonably decline consent to transfer of the policies had Solvaqua sold its business and different entity was thereafter responsible for fulfillment of the contracts with overseas purchasers before those purchasers' defaults.
25. Again, this is simply not the case in respect of the EDC Assignability Dispute. The claims have been submitted and it is only the right to contest EDC's rejections, without any change in the risk insured, that is at issue.
26. EDC's unwillingness to consent to transfer of the claims is a purely procedural block intended to prevent contestation of its rejections of Solvaqua's claims. EDC knows that Solvaqua is in no position to contest the claims. The Receiver has confirmed that it will not proceed with contesting the claims. No other party has an interest in advancing the claims other than Arnaki who, by virtue of its first secured position, is the only party that

¹⁷ *Wastech Services Ltd. v. Greater Vancouver Sewerage and Drainage District*, 2021 SCC 7 at para 63 (CanLII), <<https://canlii.ca/t/jd1d6>>.

would recover in the event the claims are allowed or EDC's rejection is found to be a breach of contract.

27. Arnaki submits that such exercise of discretion by EDC is inconsistent with the purpose of the non-assignment provision and should not be a bar to inclusion of the insurance claims in the definition of Solvaqua Claims and assignment to the Stalking Horse Purchaser.

CONCLUSION

28. Arnaki therefore requests that the Receiver's application be allowed and Arnaki's right to contest the rejected claims through inclusion in the definition of Solvaqua Claims and assignment to the Stalking Horse Purchaser confirmed.

Submitted this 31st day of August, 2023.

ALL OF WHICH IS RESPECTFULLY SUBMITTED
CHITIZ PATHAK LLP

Per:  _____

Michael Crampton,
solicitor for Arnaki Ltd.

TABLE OF AUTHORITIES

TAB

1. Barbara Billingsley, *General Principles of Canadian Insurance Law*, 3rd Ed. (LexisNexis Canada Inc., 2020)
2. *Ernst & Young Inc. v. Chartis Insurance Company of Canada*, 2012 ONSC 5020 (CanLII), <<https://canlii.ca/t/fssqf>>
3. *Wastech Services Ltd. v. Greater Vancouver Sewerage and Drainage District*, 2021 SCC 7 at para 63 (CanLII), <<https://canlii.ca/t/jd1d6>>