Federal Court Cour fédérale

Date: 20130305

Docket: T-1226-10

Citation: 2013 FC 221

Toronto, Ontario, March 5, 2013

PRESENT: Roger R. Lafrenière, Esquire
Case Management Judge

ADMIRALTY ACTION IN *REM* AGAINST THE VESSEL "QE014226C010"
AND *IN PERSONAM*

BETWEEN:

OFFSHORE INTERIORS INC.

Plaintiff

and

WORLDSPAN MARINE INC.,
CRESCENT CUSTOM YACHTS INC.,
THE OWNERS AND ALL
OTHERS INTERESTED IN
THE VESSEL "QE014226C010", AND
THE VESSEL "QE014226C010"

Defendants

and

WOLRIGE MAHON LIMITED
IN ITS CAPACITY AS APPOINTED VESSEL
CONSTRUCTION OFFICER OF THE
DEFENDANT VESSEL "QE014226C010",
HARRY SARGEANT III AND
MOHAMMAD ANWAR FARID AL-SALEH

Interveners

REASONS FOR ORDER AND ORDER

[1] As was stated by the late Prothonotary John Hargrave in *Striebel v Chairman (The)*, 2002 FCT 545, [2002] 4 FC 377, at paragraph 19: "Disputes between vessel owners and shipbuilders are invariably complex matters which, if litigated, lead to extremely complicated and lengthy proceedings." The same came to be said about clashes between *in rem* claimants jockeying for position in advance of a priorities hearing.

[2] The Plaintiff, Offshore Interiors Inc. (Offshore), seeks a declaration that the Mortgage granted to the Intervener, Harry Sargeant III (Sargeant), pursuant to the Vessel Construction Agreement does not create a lien or charge in the Vessel other than to secure delivery.

[3] The present motion turns on the interpretation of a builder's mortgage granted to Sargeant (the "Mortgage") against the Defendant Vessel "QE014226C010" (the "Vessel") pursuant to a Vessel Construction Agreement between Sargeant and the Defendant, Worldspan Marine Inc. (Worldspan) dated February 29, 2008 (the "VCA").

[4] Offshore submits that the Mortgage does not create a lien or charge in the Vessel, other than to secure delivery. The Claimants, Raider-Hansen Inc., Capri Insurance Services Ltd., and the Intervener, Mohammad Anwar Farid Al-Saleh adopt Offshore's position. Sargeant and the Intervener, Comerica Bank (Comerica) oppose the motion, arguing that the intent and effect of the Mortgage is to secure repayment of the amounts advanced by or on behalf of Sargeant.

[5] It will be useful to summarize the relevant provisions of the VCA and the Mortgage before I turn to the facts that gave rise to the present motion and consider the arguments advanced by the parties.

Relevant Provisions of the VCA and the Mortgage

[6] In accordance with the terms of the VCA, Worldspan undertook to design, construct, outfit, launch, complete, sell and deliver the Defendant Vessel, a 142 foot custom built luxury yacht, to Sargeant. In summary, the parties agreed as follows:

(a) Worldspan would retain title to the Vessel until delivery to Sargeant (section 12.1);

(b) the estimated price of the Vessel was $15.0 million USD subject to any agreed changes (section 4.2);

(c) during construction of the Vessel, Sargeant was required to make monthly payments in arrears to cover Worldspan's expenditure for the previous month (section 4.3(a));

(d) each month Worldspan would submit to Sargeant a Claim Certificate setting out that month's expenditure (section 4.3(c)); and

(e) upon completion, Worldspan agrees to deliver the Vessel to Sargeant (section 2.1), and provide a bill of sale and an affidavit confirming that materials furnished by

> Worldspan and all persons who provided labour or material to the Vessel have been paid in full (section 2.5).

[7] Section 2.3 provides that:

> 2.3 Upon Delivery, the Vessel…shall be free and clear of all liens, mortgages, and encumbrances (except liens and encumbrances approved by Owner in favour of Owner's construction finance lender, if any)…which arise or attach prior to the delivery of the Vessel to Owner, against the Vessel or against the materials, labour, supplies or equipment furnished by Builder in performance of this Agreement

[8] Section 4.1 provides that the payments made to Worldspan by Sargeant during construction were in the nature of advances:

> 4.1 The cost of the Vessel and the final purchase price payable by Owner (the "Final Purchase Price") will be finally determined on a time-and-materials basis subject to reasonable verification/audit ... During the course of construction of the Vessel Owner will make payments on account of the Final Purchase Price as hereinafter provided but these payments will be in the nature of advances to Builder and the Final Purchase Price will not be earned by Builder until delivery and acceptance of the Vessel in accordance with this Agreement.

[9] Section 4.3(a) provides that Worldspan grants Sargeant a continuing first priority security interest in the Vessel to secure the sums advanced or paid to Worldspan. Sargeant is also permitted pursuant section 8.1 to freely assign the benefit of the VCA by way of security to any bank or financial institution providing financing in connection with the construction of the Vessel.

[10] By section 12.1, Worldspan grants Sargeant a continuing first priority security interest to secure the sums advanced to Worldspan:

> 12.1 Builder grants to Owner a continuing first priority security interest in the Vessel, including all work, materials, machinery, and equipment relating to the Vessel, to secure any sums advanced or paid to Builder under this Agreement ... In support of Owner's security interest in the Vessel Builder agrees to register a Ship's Mortgage in favour of Owner or Owner's construction lender (the form of the mortgage document is to be agreed upon between the parties acting reasonably)…

[11] Section 13.1 gives Sargeant the "right and power, without prejudice to any other remedy," to terminate the VCA in the event of certain events of default, including if Worldspan suspended payment of its debts or ceased to carry on business or make any arrangement or compromise with its creditors. By section 13.2 of the VCA, upon termination of the VCA by Sargeant, Sargeant is entitled to take over and complete the Vessel elsewhere.

[12] Section 13.3 provides Sargeant with rights in the alternative to require Worldspan on 30 days notice to cooperate in the prompt sale of the Vessel to be conducted in accordance with section 24 of the VCA. Section 24 of the VCA sets out a formula that applies in the event of a sale of the Vessel by Sargeant pursuant to which Worldspan is obligated to pay Sargeant a calculated sum in the event that the sale proceeds are less than the advances made by Sargeant to Worldspan; similarly, if the sale proceeds exceed the advances made by Sargeant to Worldspan, Sargeant is to pay a portion of the profit to Worldspan.

[13] Section 13.5 of the VCA provides that Worldspan has a right to terminate the VCA in the event that Sargeant fails to make payments pursuant to the VCA, in which case Worldspan may sell the Vessel and is liable to repay Sargeant from the sale proceeds the advances made to Worldspan under the Agreement, less Worldspan's out-of-pocket costs for storage and resale.

[14] A Builder's Mortgage in favour of Sargeant as against the Vessel was filed in the Vancouver Ship Registry on May 14, 2008. The mortgage is in the prescribed form and simply states that:

> There is an account current pursuant to that certain Vessel Construction Agreement dated February 29, 2008 among mortgagor and mortgagee which Agreement specifies the obligations hereby secured.

Background Facts

[15] The facts underlying the present motion are not in dispute. Construction of the Vessel began in March 2008, and by August 2009 payments made by or on behalf of Sargeant to Worldspan totalled $11,064,525.38 USD.

[16] In August 2009, Sargeant arranged a construction loan with Comerica for $9,400,000.00 USD to finance the remaining costs to complete construction of the vessel (the "Loan"). A Construction Loan Agreement dated August 14, 2009 between Comerica, Sargeant and others (the "CLA") addresses security for the Loan. Sargeant's interest in the VCA, the Vessel, and the Mortgage were assigned to Comerica Bank in exchange for funds advanced by Comerica.

[17] From August 2009 to March 2010, Comerica paid to Worldspan on Sargeant's behalf the sum of $9,387,398.67 USD on account of Claims Certificates issued by Worldspan under the VCA.

[18] A dispute arose between Sargeant and Worldspan concerning project costs and construction of the Vessel ceased in April or May 2010.

[19] Offshore commenced the underlying action on July 20, 2010 against Worldspan, Crescent Custom Yachts Inc. (Crescent), the Owners and all others interested in the Vessel, and the Vessel itself for unpaid invoices for services and materials rendered in connection with construction of the Vessel. The Vessel was arrested on July 29, 2010 and has remained under arrest to this date.

[20] On May 27, 2011, Worldspan and related entities filed a Petition in the British Columbia Supreme Court seeking relief under the *Companies Creditors' Arrangement Act*, RSC 1985, c C-36.

[21] By Order dated August 29, 2011, a Claims Process was established for all creditors with *in rem* claims against the Vessel. The Order provided that notice be given to all creditors of the requirement to file an affidavit containing particulars in support of the claim against the Vessel, specifying the nature of the claim in order that the Court can determine if such a claim constitutes an *in rem* claim and the priority position to be given to the claim.

[22] On October 14, 2011, Sargeant filed an affidavit in support of his claim against the Vessel. The claim is said to derive from payments that were made by or on behalf of Sargeant to Worldspan in excess of $21 million for the construction of the Vessel, and from the security interest in the Vessel granted to Sargeant by Worldspan to secure the payments.

Issue to be Determined

[23] A condition of participating in a priorities distribution is that the claimant has an existing, valid and enforceable claim *in rem* against the Vessel. In addition to presenting their own claim, each claimant may attack the claims of the other claimants, including their ranking in terms of priority.

[24] By the present motion, Offshore seeks a declaration that the Mortgage granted to Sargeant pursuant to the VCA does not create a lien or charge in the Vessel other than to secure delivery.

[25] The relief requested by Offshore is not intended to preclude either Sargeant or Comerica from participating in the upcoming priorities hearing. Offshore acknowledges that Sargeant and Comerica are fully entitled to attempt to prove that they have *in rem* claims. However, Offshore maintains that, based on the wording of the Mortgage and the VCA, their claims cannot include repayment of the funds advanced.

[26] In opposing the motion, Sargeant and Comerica have advanced similar arguments. They submit that the Mortgage, if not expressly then impliedly, secures repayment of the amounts advanced pursuant to the VCA, as particularized in their respective affidavits of claim. The VCA expressly provides that advances made by Sargeant to Worldspan are not earned until a future date: the delivery and acceptance of the Vessel. Sargeant and Comerica say that since the Vessel was never supplied, the advances are recoverable as money lent. In the alternative, they say that Sargeant has an equitable mortgage or they have a claim against the Vessel pursuant to section 22(2)(n) of the *Federal Courts Act* for the amounts advanced for the construction of the Vessel.

[27] For the reasons set out in paragraph 60 to 64 of the Plaintiff's supplementary written submissions, which I adopt and make mine, I conclude that the submission that Sargeant has an equitable mortgage or a section 22(2)(n) claim is of no moment. The question of whether there was an obligation under the Mortgage or the VCA requiring that the funds advanced by Sargeant be repaid by Worldspan depends on an interpretation of the language used in the contracts.

Analysis

[28] The aim of contractual interpretation is to determine the intentions of the parties in accordance with the language used in the written document, having regard to the context in which the contract was signed. In *Salah v Timothy's Coffees of the World Inc.,* 2010 ONCA 673 (CanLII), 2010 ONCA 673, 268 OAC 673, Winkler C.J.O. provided this instructive overview of the applicable principles at paragraph 16:

> When interpreting a contract, the court aims to determine the intentions of the parties in accordance with the language used in the written document and presumes that the parties have intended what they have said. The court construes the contract as a whole, in a manner that gives meaning to all of its terms, and avoids an interpretation that would render one or more of its terms ineffective. In interpreting the contract, the court must have regard to the objective evidence of the "factual matrix" or context underlying the negotiation of the contract, but not the subjective evidence of the intention of the parties. The court should interpret the contract so as to accord with sound commercial principles and good business sense, and avoid commercial absurdity. If the court finds that the contract is ambiguous, it may then resort to extrinsic evidence to clear up the ambiguity. Where a transaction involves the execution of several documents that form parts of a larger composite whole – like a complex commercial transaction – and each agreement is entered into on the faith of the others being executed, then assistance in the interpretation of one agreement may be drawn from the related agreements.

[29] In the case at bar, the Mortgage is in a standard form (Form 16) which allows only for two options: a principal sum and a fixed rate of interest, or an "account current". In his text *Essentials of Canadian Maritime Law, (Toronto: Irwin Law, 1993) at 246,* Edgar Gold explains the difference between the two options:

> The prescribed forms allow for a mortgage to secure a principal sum and a fixed rate of interest, or a mortgage to secure an account current, that is, a continuing security for a balance that may fluctuate and an interest rate that may change. An account current mortgage is the more flexible of the two kinds of mortgage because it allows for future advances, perhaps to cover operations or repairs to the ship after the initial loan for its purchase, and it can be used to accommodate financing by a revolving line of credit.

[30] The prescribed form requires that the mortgagor "describe the nature of the transaction so as to show how the amount of principal and interest due at any given time is to be ascertained and the manner and time of payments." The Mortgage states that there is "an account current" pursuant to the VCA, without more, and makes reference to the "obligations secured" the VCA. As a result, the

VCA must be reviewed to ascertain the rights of Sargeant and its assignee, Comerica, and the obligations of Worldspan.

[31] Section 12.1 of the VCA expressly grants Sergeant a first priority security interest in the Vessel to secure advances made by Sargeant to Worldspan. Section 4.1 also expressly provides that the advances will not be earned by Worldspan until delivery and acceptance of the Vessel.

[32] Sargeant and Comerica submit that the above language used in the VCA clearly indicates the intention of the parties that unless and until the Vessel was delivered and accepted, the advances to Worldspan were in the nature of a loan from Sergeant to Worldspan secured by the Mortgage. They assert that since the Vessel was never delivered and accepted, the advances received by Worldspan were never earned, and consequently are due and owing by Worldspan.

[33] All of the factors and circumstances considered, I am not persuaded that the evidence supports any such indebtedness.

[34] To begin with, the form of mortgage requires specifics of the transaction so as to determine the amount owing and the "time of payment." Neither the Mortgage nor the VCA contain such specifics.

[35] Further, the VCA sets out in detail the rights and obligations of the parties on breach and/or termination of the agreement. Upon completion of the contract and against payment, Worldspan was obliged to deliver the yacht and transfer title to Sargeant. Sargeant in turn was given certain

security rights against the yacht in the event of a default during construction by Worldspan as builder. By way of example, in the event of a breach by Worldspan, Sargeant had the specific right to take possession and complete the Vessel, or to compel a sale and accounting. However, there is no explicit provision for repayment of the funds provided for construction of the Vessel.

[36] Sargeant and Comerica submit that there is no other way of treating the advances other than as a loan in view of the express language of the VCA that the advances were not earned by Worldspan unless and until the Vessel was delivered and accepted. This result is said to be consistent with the express provisions in the VCA obligating Worldspan to repay Sargeant advances made in the event of a sale of the Vessel following termination of the agreement by either party. Sargeant and Comerica submit that any other result would be an un-businesslike outcome and a commercial absurdity.

[37] Sargeant and Comerica further contend that, even in the absence of an express covenant to repay, it is an implied term of a mortgage to repay monies as "every mortgage, though no covenant or bond to pay the money, implies a loan, and every loan implies a debt.": see *J. D. Buchan, Mortgages of Ships: Marine Security in Canada* (Vancouver: Butterworths, 1986) at 58; *King v King* (1735), 3 P. VVms. 358, 24 E.R. 100 [*King*], at 360.

[38] Sargeant and Comerica assert that the advances referenced in section 4.1 of the VCA to be secured under section 12.1 are clearly the monies that comprise the "account current" referenced in the Mortgage.

[39] However, whether a mortgage implies a loan is dependent on the circumstances of the specific situation. Notwithstanding what is stated in the Mortgage, there is no evidence of any "account current" being created pursuant to the VCA. In fact, the terms of the VCA clearly allowed Worldspan to retain all advances made by Sargeant for the purpose of making payments for the labour and materials to construct the Vessel.

[40] In support of its position, Offshore relies on a decision by Arbitrator Mr. John J. McIntyre (the "Arbitrator") dated August 31, 2010 in an arbitration between *F.C. Yachts Ltd., P.R. Yacht Builders Ltd.* and *New World Expedition Yachts, LLC* [NWEY Arbitration]. Dealing with facts strikingly similar to the case at bar, the Arbitrator made the following observations regarding the mortgage entered into between the parties, at paragraph 11:

> "The Mortgage was not actually entered until March 18, 2009. It is in a standard form Builder's Mortgage. No amount for principal is stated. Rather the relevant mortgage term is as follows:
>
> Whereas there is an account current between [PRYB], as Mortgagor and [NWEY] as Mortgagee in the support of the Mortgagor's obligations under a [YCA] dated the 13th of March, 2008 for which the amount of principle (sic) and interest due at any time may be ascertained by reference to the Mortgagor's records and books...
>
> PRYB's obligations under the YCA were to construct the Vessel substantially in fit and finish to the Standard (para. 1(a)); to use all reasonable commercial efforts to build and deliver the Vessel at the earliest possible date (para. 2(a)); to charge for labour to construct the Vessel the total of CDN$4,340,000.00 (para. 3(a)); to keep complete and accurate accounts of all funds expended in the Contract Price (para. 3(b)); to give [NWEY] bi-weekly invoices (para. 3(c)); to deliver the Vessel free and clear of all liens and encumbrances after the conclusion of the sea trials (para. 4(a)). These are not all the obligations, but the principle ones.

> There are no financial obligations that PRYB has to NWEY under the YCA. There are no payments for principal or interest due from PRYB to NWEY. The financial obligations are the reverse, i.e. for NWEY to advance funds to PRYB to a Labour and Materials ("L&M") account from which the latter will make payments for the labour and materials to construct the Vessel. There is nothing in the wording of the YCA that characterize the payments by NWEY to the L&M account as a loan by NWEY to PRYB."

[41] The Adjudicator stated that there was "a dearth of evidence" that the accounts of the mortgagor recorded any amount owing to the mortgagee either for principal or interest or manner and time of payment. He also found that the evidence of the yacht construction agreement "did not support any such indebtedness." The Adjudicator concluded as follows:

> I am not satisfied that the Mortgage was to secure amounts advanced to PRYB by NWEY. Rather, it appears to me that what was intended was to transfer a form of property interest in the vessel and the components and equipment acquired to be incorporated into the vessel as it was being built. This is consistent with the expression of intention in Recital B to Schedule B of the YCA. While PRYB and NWEY may have intended to give NWEY a first ranking security interest in the Vessel they did not accomplish the task by using a standard form of builder's mortgage. The requirement of a debt obligation from PRYB to NWEY in order to give some validity to the use of such a form is completely missing from the record.

[42] Sargeant and Comerica submit that the NWEY Arbitration can be distinguished because the contract at issue in that case is a different contract to the VCA. Specifically, unlike the VCA:

(a) the Yacht Construction Agreement (the "YCA") did not provide that payments made by NWEY were in the nature of advances that were not earned until delivery of the vessel;

(b) the YCA included no wording supporting a finding that the payments to the builder were in the nature of loan or that a promise to repay could be implied: and

(c) the arbitrator held that the mortgage in that case was not to secure amounts.

[43] The Plaintiff filed a supplementary affidavit attaching a copy of the YCA in the NWEY Arbitration as an exhibit to establish that the YCA in fact contained a repayment provision. I am neither prepared, nor do I feel it is appropriate, to go behind the Arbitrator's decision to examine the evidentiary record before him. The decision speaks for itself. Accordingly, the Plaintiff's supplementary affidavit was disregarded.

[44] It remains that the reasoning of the Arbitrator in the excerpts reproduced above is sound and that the situation before me is indistinguishable from the germane facts as described in the Arbitrator's decision.

[45] The parties plainly contemplated that all monies provided for construction of the Vessel would be utilized in its construction and would not exist as a fund. This is consistent with section 2.5 of the YCA that required Worldspan, upon delivery, to provide an affidavit confirming that materials furnished and all persons who provided labour or material to the Vessel had been paid in full.

[46] Further, I agree with the Plaintiff, it must have been contemplated by the parties that, following a breach, Worldspan would have no ability to repay the substantial amounts of money required to construct the Vessel and Sargeant would be left with the obvious remedy of taking the Vessel from the yard and completing it elsewhere or selling it.

[47] The VCA clearly sets out what happens in the event of a breach by either party. Different scenarios were contemplated by the parties and expressed in clear terms. In each scenario, there is simply no provision for repayment of the advances provided by Sargeant. A term will not be implied merely because, in hindsight, it would have been reasonable to do so.

[48] I adopt and make mine paragraph 57 of the Plaintiff's supplementary written representations, which is elegant in its simplicity:

> In the case at hand the VCA contains express terms as to what obligations are required by the builder... The VCA is not a loan agreement. It is an agreement for the construction of a Vessel. The VCA contemplates the building and delivery of a Vessel, not the repayment of a loan. If a "loan" was contemplated, it would have been a simple matter to draft such into an Agreement. …If the monies advanced were a "loan", this Agreement would say so. It does not. If the monies were to be repaid, the Agreement would say so. It does not.
>
> (Plaintiff's underlining)

[49] For the above reasons, I conclude that there are no financial obligations that Worldspan has to Sargeant under the VCA. If Worldspan was in breach, Sargeant's remedies were limited to possession and ownership of the Vessel and an *in personam action* against Worldspan.

ORDER

THIS COURT ORDERS that:

1. The motion is granted.

2. The Builder's Mortgage granted to the Intervener, Harry Sargeant III, against the Defendant Vessel "QE014226C010" pursuant to a Vessel Construction Agreement between Harry Sargeant III and the Defendant, Worldspan Marine Inc. dated February 29, 2008 does not create a lien or charge in the Vessel other than to secure delivery.

3. Costs of the motion shall be paid to the Plaintiff by each of the Interveners, Harry Sargeant III and Comerica Bank, in the amount of $1,500.00, inclusive of disbursements and taxes.

"Roger R. Lafrenière"

Case Management Judge

FEDERAL COURT

SOLICITORS OF RECORD

DOCKET:	T-1226-10
STYLE OF CAUSE:	OFFSHORE INTERIORS INC. v. THE VESSEL "QE014226C010" ET AL
PLACE OF HEARING:	Vancouver, British Columbia
DATE OF HEARING:	April 5, 2012
REASONS FOR ORDER AND ORDER:	LAFRENIÈRE, P.
DATED:	March 5, 2013

APPEARANCES:

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Dinoysios Rossi	FOR THE INTERVENER, MOHAMMAD ANWAR FARID AL-SALEH
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