REGINA VS. CARNIE ET AL

ARGOSY FINANCIAL GROUP OF CANADA

SYNOPSIS

Argosy Financial Group, comprising Argosy Finance Company Limited and Argosy Investments Limited, commenced their syndicated mortgage program in 1975. The program expanded rapidly, particularly during 1978, to include loans for development in Alberta as well as Ontario. The company would solicit funds from the public for investment in a specific mortgage, upon representations given as to the nature of the loan and the security provided. During 1978, the period of its most rapid expansion, the Argosy group experienced an increasingly severe negative cash flow from operations. This condition persisted until March, 1980, when the Argosy Group went into receivership. The receivership was primarily the result of:

- the apparent inability of the mortgagors (borrowers) to make interest payments on account of their mortgage
- the apparent inability of the mortgagors to pay principal amounts upon maturity.

This inability to repay apparently reflected the status of the property provided as security for loans by the mortgagor and the limited financial resources of the mortgagor. The property was intended for residential or commercial development. In many cases, however, the developers could not get the necessary government approvals or these approvals were delayed, so development could not begin promptly. Thus, developers could not realize the appraised potential of the property. In other cases, where development did commence, market conditions prevented the developer from generating sufficient funds to pay out the Argosy loan upon maturity.

In some cases when loans matured and were not repaid, it would appear that Argosy did not pursue available courses of legal action. The status of the project and the resources of the mortgagor were apparently insufficient to satisfy the balance outstanding at that date. In other cases, the loans were extended at maturity, and some loans were increased in amount to allow the mortgagor to continue attempts to develop the property as intended.

In view, however, of the deteriorating financial health of the Argosy Group - illustrated by the increasingly serious negative cash flow from operations and the status of the syndicated mortgage portfolio - investors in the Argosy syndicated mortgage program were placed in a position of increased economic risk.

The increased economic risk arose out of the following conditions:

- Argosy investors assumed some of the risks normally associated with ownership of the land, i.e., the land lacked the appropriate government approvals and the mortgagor and/or its principals had little apparent tangible equity in the property.

- Security provided in support of some loans was questionable - most notably in the case of loans provided by Argosy to developments in Alberta (Western projects) which were M.U.R.B. tax shelter properties. The value provided as security was more than the true market value and represented the value to a taxpayer of reducing his personal income taxes.

- Security was diluted through the conversion of Argosy loans for particular projects to uses outside those projects.

- The continuing deterioration of Argosy's financial condition affected its ability to meet its obligations to the syndicate mortgage investors.

One example from the Argosy syndicate mortgage portfolio is a loan to 116410 Developments Ltd., a company owned by Carnie and Saunders.

The company had committed itself to purchasing land in Lloydminster, Alberta, at a price of $400,000.00. It planned to build a 300-suite apartment complex on the land. Before the closing of the transaction, the company had been unsuccessful in obtaining mortgage financing due to the location of the land and environmental concerns. Argosy provided a loan of $1.0 million to 116410 Developments Ltd., secured by a first mortgage on the property. Funds were solicited from the public for investment in this mortgage. It was represented that the mortgage proceeds had been used for interim construction of a 300-unit residential complex.

However, an examination tracing the mortgage proceeds revealed a different story. Out of the proceeds, $400,000.00 was used to cover the cost of property purchased by the company. Thus, the purchase was financed entirely by the Argosy loan. Of the remaining funds, $115,000.00 was disbursed by Argosy to Carnie Investments, Inc., in Florida.

The unaudited financial statements of Carnie Investments, Inc. at November 30, 1978, showed a deficit of approximately $296,000.00. Funds were thus needed in Florida. The company's unaudited financial statements at March 31, 1979, indicate a further deterioration in its financial position and an apparent inability to repay the funds advanced.

National Land Corporation, another company owned by Carnie and Saunders, received, directly from Argosy, numerous advances on the loan to 116410 Developments Limited. The records of 116410 Developments Ltd. recorded these advances as amounts owing to it from National Land. Of these funds, $65,000.00 was used by National Land to purchase preference shares of Argosy Finance Company Limited. National Land also used these funds to help pay interest on Argosy loans to other companies in which Carnie and Saunders had an interest.

The underlying security given to the Argosy Investors is highly questionable in light of the following:

- the mortgage for $1.0 million was on land purchased for $400,000.00

- CMHC advised that the property was unsuitable for NHA financing
- the property remained undeveloped
- the developers were unable to obtain alternate mortgage financing
- the mortgage proceeds were not used as purported.

The accused in the case pleaded guilty and received sentences ranging from three to six-and-one-half years.