Court File No. CV-13-10279-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES CREDITORS ARRANGEMENT ACT,* R.S.C. 1985, c. C-36, AS AMENDED

B E T W E E N:

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO GROWTHWORKS CANADIAN FUND LTD.

Applicant

BOOK OF AUTHORITIES OF THE OFFEREE SHAREHOLDERS
(Motion and Cross-Motion returnable February 11, 2014)

January 31, 2014

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Tab 1

SUPREME COURT OF CANADA

CITATION: Hryniak *v.* Mauldin, 2014 SCC 7	**DATE:** 20140123 **DOCKET:** 34641

BETWEEN:

Robert Hryniak
Appellant
and
Fred Mauldin, Dan Myers, Robert Blomberg, Theodore Landkammer, Lloyd Chelli, Stephen Yee, Marvin Cleair, Carolyn Cleair, Richard Hanna, Douglas Laird, Charles Ivans, Lyn White and Athena Smith
Respondents
- and -
Ontario Trial Lawyers Association and Canadian Bar Association
Interveners

CORAM: McLachlin C.J. and LeBel, Abella, Rothstein, Cromwell, Karakatsanis and Wagner JJ.

REASONS FOR JUDGMENT: (paras. 1 to 96)	Karakatsanis J. (McLachlin C.J. and LeBel, Abella, Rothstein, Cromwell and Wagner JJ. concurring)

NOTE: This document is subject to editorial revision before its reproduction in final form in the *Canada Supreme Court Reports*.

HRYNIAK *v.* MAULDIN

Robert Hryniak *Appellant*

v.

Fred Mauldin, Dan Myers, Robert Blomberg, Theodore Landkammer, Lloyd Chelli, Stephen Yee, Marvin Cleair, Carolyn Cleair, Richard Hanna, Douglas Laird, Charles Ivans, Lyn White and Athena Smith *Respondents*

and

Ontario Trial Lawyers Association and Canadian Bar Association *Interveners*

Indexed as: Hryniak *v.* Mauldin

2014 SCC 7

File No.: 34641.

2013: March 26; 2014: January 23.

Present: McLachlin C.J. and LeBel, Abella, Rothstein, Cromwell, Karakatsanis and Wagner JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Civil Procedure — Summary Judgment — Investors bringing action in civil fraud and subsequently bringing a motion for summary judgment — Motion judge granting summary judgment — Purpose of summary judgment motions — Access to Justice — Proportionality — Interpretation of recent amendments to Ontario Rules of Civil Procedure — Trial management orders — Standard of review for summary judgment motions — Whether motion judge erred in granting summary judgment — Rules of Civil Procedure, R.R.O. 1990, Reg. 194, Rule 20.

In June 2001, two representatives of a group of American investors met with H and others to discuss an investment opportunity. The group wired US$1.2 million, which was pooled with other funds and transferred to H's company, Tropos. A few months later, Tropos forwarded more than US$10 million to an offshore bank and the money disappeared. The investors brought an action for civil fraud against H and others and subsequently brought a motion for summary judgment. The motion judge used his powers under Rule 20.04(2.1) of the *Ontario Rules of Civil Procedure* (amended in 2010) to weigh the evidence, evaluate credibility, and draw inferences. He concluded that a trial was not required against H. Despite concluding that this case was not an appropriate candidate for summary judgment, the Court of Appeal was satisfied that the record supported the finding that H had committed the tort of civil fraud against the investors, and therefore dismissed H's appeal.

Held: The appeal should be dismissed.

Our civil justice system is premised upon the value that the process of adjudication must be fair and just. This cannot be compromised. However, undue process and protracted trials, with unnecessary expense and delay, can prevent the fair and just resolution of disputes. If the process is disproportionate to the nature of the dispute and the interests involved, then it will not achieve a fair and just result.

A shift in culture is required. The proportionality principle is now reflected in many of the provinces' rules and can act as a touchstone for access to civil justice. The proportionality principle means that the best forum for resolving a dispute is not always that with the most painstaking procedure. Summary judgment motions provide an opportunity to simplify pre-trial procedures and move the emphasis away from the conventional trial in favour of proportional procedures tailored to the needs of the particular case. Summary judgment rules must be interpreted broadly, favouring proportionality and fair access to the affordable, timely and just adjudication of claims.

Rule 20 was amended in 2010 to improve access to justice. These reforms embody the evolution of summary judgment rules from highly restricted tools used to weed out clearly unmeritorious claims or defences to their current status as a legitimate alternative means for adjudicating and resolving legal disputes. They offer significant new tools to judges, which allow them to adjudicate more cases through summary judgment motions and attenuate the risks when such motions do not resolve the entire case. The new powers in rules 20.04(2.1) and (2.2) expand the

number of cases in which there will be no genuine issue requiring a trial by permitting motion judges to weigh evidence, evaluate credibility and draw reasonable inferences.

Summary judgment motions must be granted whenever there is no genuine issue requiring a trial. There will be no genuine issue requiring a trial when the judge is able to reach a fair and just determination on the merits on a motion for summary judgment. This will be the case when the process (1) allows the judge to make the necessary findings of fact, (2) allows the judge to apply the law to the facts, and (3) is a proportionate, more expeditious and less expensive means to achieve a just result.

The new fact-finding powers granted to motion judges in Rule 20.04 may be employed on a motion for summary judgment unless it is in the interest of justice for them to be exercised only at trial. When the use of the new powers would enable a judge to fairly and justly adjudicate a claim, it will generally not be against the interest of justice to do so. The power to hear oral evidence should be employed when it allows the judge to reach a fair and just adjudication on the merits and it is the proportionate course of action. While this is more likely to be the case when the oral evidence required is limited, there will be cases where extensive oral evidence can be heard. Where a party seeks to lead oral evidence, it should be prepared to demonstrate why such evidence would assist the motion judge and to provide a description of the proposed evidence so that the judge will have a basis for setting the scope of the oral evidence.

On a motion for summary judgment under Rule 20.04, the judge should first determine if there is a genuine issue requiring trial based only on the evidence before her, *without* using the new fact-finding powers. There will be no genuine issue requiring a trial if the summary judgment process provides her with the evidence required to fairly and justly adjudicate the dispute and is a timely, affordable and proportionate procedure, under rule 20.04(2)(a). If there appears to be a genuine issue requiring a trial, she should then determine if the need for a trial can be avoided by using the new powers under Rules 20.04(2.1) and (2.2). Their use will not be against the interest of justice if they will lead to a fair and just result and will serve the goals of timeliness, affordability and proportionality in light of the litigation as a whole.

Failed, or even partially successful, summary judgment motions add to costs and delay. This risk can be attenuated by a judge who makes use of the trial management powers provided in Rule 20.05 and the court's inherent jurisdiction. These powers allow the judge to use the insight she gained from hearing the summary judgment motion to craft a trial procedure that will resolve the dispute in a way that is sensitive to the complexity and importance of the issue, the amount involved in the case, and the effort expended on the failed motion. Where a motion judge dismisses a motion for summary judgment, in the absence of compelling reasons to the contrary, she should also seize herself of the matter as the trial judge.

Absent an error of law, the exercise of powers under the new summary judgment rule attracts deference. When the motion judge exercises her new fact-finding powers under Rule 20.04(2.1) and determines whether there is a genuine issue requiring a trial, this is a question of mixed fact and law which should not be overturned, absent palpable and overriding error. Similarly, the determination of whether it is in the interest of justice for the motion judge to exercise the new fact-finding powers provided by Rule 20.04(2.1) is also a question of mixed fact and law which attracts deference.

The motion judge did not err in granting summary judgment in the present case. The tort of civil fraud has four elements, which must be proven on a balance of probabilities: (1) a false representation by the defendant; (2) some level of knowledge of the falsehood of the representation on the part of the defendant (whether knowledge or recklessness); (3) the false representation caused the plaintiff to act; (4) the plaintiff's actions resulted in a loss. In granting summary judgment to the group against H, the motion judge did not explicitly address the correct test for civil fraud but his findings are sufficient to make out the cause of action. The motion judge found no credible evidence to support H's claim that he was a legitimate trader, and the outcome was therefore clear, so the motion judge concluded there was no issue requiring a trial. It was neither against the interest of justice for the motion judge to use his fact-finding powers nor was his discretionary decision to do so tainted with error.

Cases Cited

Referred to: *Bruno Appliance and Furniture, Inc. v. Hryniak*, 2014 SCC 8; *New Brunswick (Minister of Health and Community Services) v. G. (J.)*, [1999] 3 S.C.R. 46; *Medicine Shoppe Canada Inc. v. Devchand*, 2012 ABQB 375, 541 A.R. 312; *Saturley v. CIBC World Markets Inc.*, 2011 NSSC 4, 297 N.S.R. (2d) 371; *Szeto v. Dwyer*, 2010 NLCA 36, 297 Nfld. & P.E.I.R. 311; *Bal Global Finance Canada Corp. v. Aliments Breton (Canada) inc.*, 2010 QCCS 325 (CanLII); *Vaughan v. Warner Communications, Inc.* (1986), 56 O.R. (2d) 242; *Canada (Attorney General) v. Lameman*, 2008 SCC 14, [2008] 1 S.C.R. 372; *Aguonie v. Galion Solid Waste Material Inc.* (1998), 38 O.R. (3d) 161; *Dawson v. Rexcraft Storage and Warehouse Inc.* (1998), 164 D.L.R. (4th) 257; *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235.

Statutes and Regulations Cited

Code of Civil Procedure, R.S.Q., c. C-25, arts. 4.2, 54.1 *et seq.*, 165(4).

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APPEAL from a judgment of the Ontario Court of Appeal (Winkler C.J.O. and Laskin, Sharpe, Armstrong and Rouleau JJ.A.), 2011 ONCA 764, 108 O.R. (3d) 1, 286 O.A.C. 3, 97 C.C.E.L. (3d) 25, 14 C.P.C. (7th) 242, 13 R.P.R. (5th) 167, 93 B.L.R. (4th) 1, 344 D.L.R. (4th) 193, 10 C.L.R. (4th) 17, [2011] O.J. No. 5431 (QL), 2011 CarswellOnt 13515 (*sub nom. Combined Air Mechanical Services Inc. v. Flesch*), affirming a decision of Grace J., 2010 ONSC 5490, [2010] O.J. No. 4661 (QL), 2010 CarswellOnt 8325. Appeal dismissed.

Sarit E. Batner, *Brandon Kain* and *Moya J. Graham*, for the appellant.

Javad Heydary, *Jeffrey D. Landmann*, *David K. Alderson*, *Michelle Jackson* and *Jonathan A. Odumeru*, for the respondents.

Allan Rouben and Ronald P. Bohm, for the intervener the Ontario Trial Lawyers Association.

Paul R. Sweeny and David Sterns, for the intervener the Canadian Bar Association.

The judgment of the Court was delivered by

KARAKATSANIS J. —

[1] Ensuring access to justice is the greatest challenge to the rule of law in Canada today. Trials have become increasingly expensive and protracted. Most Canadians cannot afford to sue when they are wronged or defend themselves when they are sued, and cannot afford to go to trial. Without an effective and accessible means of enforcing rights, the rule of law is threatened. Without public adjudication of civil cases, the development of the common law is stunted.

[2] Increasingly, there is recognition that a culture shift is required in order to create an environment promoting timely and affordable access to the civil justice system. This shift entails simplifying pre-trial procedures and moving the emphasis away from the conventional trial in favour of proportional procedures tailored to the needs of the particular case. The balance between procedure and access struck by our justice system must come to reflect modern reality and recognize that new models of adjudication can be fair and just.

[3] Summary judgment motions provide one such opportunity. Following the *Civil Justice Reform Project: Summary of Findings and Recommendations* (2007) (the Osborne Report), Ontario amended the *Rules of Civil Procedure*, R.R.O. 1990,

Reg. 194 (*Ontario Rules* or Rules) to increase access to justice. This appeal, and its companion, *Bruno Appliance and Furniture, Inc. v. Hryniak*, 2014 SCC 8, address the proper interpretation of the amended Rule 20 (summary judgment motion).

[4] In interpreting these provisions, the Ontario Court of Appeal placed too high a premium on the "full appreciation" of evidence that can be gained at a conventional trial, given that such a trial is not a realistic alternative for most litigants. In my view, a trial is not required if a summary judgment motion can achieve a fair and just adjudication, if it provides a process that allows the judge to make the necessary findings of fact, apply the law to those facts, and is a proportionate, more expeditious and less expensive means to achieve a just result than going to trial.

[5] To that end, I conclude that summary judgment rules must be interpreted broadly, favouring proportionality and fair access to the affordable, timely and just adjudication of claims.

[6] As the Court of Appeal observed, the inappropriate use of summary judgment motions creates its own costs and delays. However, judges can mitigate such risks by making use of their powers to manage and focus the process and, where possible, remain seized of the proceedings.

[7] While I differ in part on the interpretation of Rule 20, I agree with the Court of Appeal's disposition of the matter and would dismiss the appeal.

I. Facts

[8] More than a decade ago, a group of American investors, led by Fred Mauldin (the Mauldin Group), placed their money in the hands of Canadian "traders". Robert Hryniak was the principal of the company Tropos Capital, which traded in bonds and debt instruments; Gregory Peebles, is a corporate-commercial lawyer (formerly of Cassels Brock & Blackwell) who acted for Hryniak, Tropos and Robert Cranston, formerly a principal of a Panamanian company, Frontline Investments Inc.

[9] In June 2001, two members of the Mauldin Group met with Cranston, Peebles, and Hryniak, to discuss an investment opportunity.

[10] At the end of June 2001, the Mauldin Group wired US$1.2 million to Cassels Brock, which was pooled with other funds and transferred to Tropos. A few months later, Tropos forwarded more than US$10 million to an offshore bank, and the money disappeared. Hryniak claims that at this point, Tropos's funds, including the funds contributed by the Mauldin Group, were stolen.

[11] Beyond a small payment of US$9,600 in February 2002, the Mauldin Group lost its investment.

II. Judicial History

A. *Ontario Superior Court of Justice, 2010 ONSC 5490 (CanLII)*

[12] The Mauldin Group joined with Bruno Appliance and Furniture, Inc. (the appellants in the companion appeal) in an action for civil fraud against Hryniak, Peebles and Cassels Brock. They brought motions for summary judgment, which were heard together.

[13] In hearing the motions, the judge used his powers under the new Rule 20.04(2.1) to weigh the evidence, evaluate credibility, and draw inferences. He found that the Mauldin Group's money was disbursed by Cassels Brock to Hryniak's company, Tropos, but that there was no evidence to suggest that Tropos had ever set up a trading program. Contrary to the investment strategy that Hryniak had described to the investors, the Mauldin Group's money was placed in an account with the offshore New Savings Bank, and then disappeared. He rejected Hryniak's claim that members of the New Savings Bank had stolen the Mauldin Group's money.

[14] The motion judge concluded that a trial was not required against Hryniak. However, he dismissed the Mauldin Group's motion for summary judgment against Peebles, because that claim involved factual issues, particularly with respect to Peebles' credibility and involvement in a key meeting, which required a trial. Consequently, he also dismissed the motion for summary judgment against Cassels Brock, as those claims were based on the theory that the firm was vicariously liable for Peebles' conduct.

B. *Court of Appeal for Ontario, 2011 ONCA 764, 108 O.R. (3d) 1*

[15] The Court of Appeal simultaneously heard Hryniak's appeal of this matter, the companion *Bruno Appliance* appeal, and three other matters which are not before this Court. This was the first occasion on which the Court of Appeal considered the new Rule 20.

[16] The Court of Appeal set out a threshold test for when a motion judge could employ the new evidentiary powers available under Rule 20.04(2.1) to grant summary judgment under Rule 20.04(2)(a). Under this test, the "interest of justice" requires that the new powers be exercised only at trial, unless a motion judge can achieve the "full appreciation" of the evidence and issues required to make dispositive findings on a motion for summary judgment. The motion judge should assess whether the benefits of the trial process, including the opportunity to hear and observe witnesses, to have the evidence presented by way of a trial narrative, and to experience the fact-finding process first-hand, are necessary to fully appreciate the evidence in the case.

[17] The Court of Appeal suggested that cases requiring multiple factual findings, based on conflicting evidence from a number of witnesses, and involving an extensive record, are generally not fit for determination in this manner. Conversely, cases driven by documents, with few witnesses, and limited contentious factual issues are appropriate candidates for summary judgment.

[18] The Court of Appeal advised motion judges to make use of the power to hear oral evidence, under Rule 20.04(2.2), to hear only from a limited number of witnesses on discrete issues that are determinative of the case.

[19] The Court of Appeal concluded that, given its factual complexity and voluminous record, the Mauldin Group's action was the type of action for which a trial is generally required. There were numerous witnesses, various theories of liability against multiple defendants, serious credibility issues, and an absence of reliable documentary evidence. Moreover, since Hryniak and Peebles had cross-claimed against each other and a trial would nonetheless be required against the other defendants, summary judgment would not serve the values of better access to justice, proportionality, and cost savings.

[20] Despite concluding that this case was not an appropriate candidate for summary judgment, the Court of Appeal was satisfied that the record supported the finding that Hryniak had committed the tort of civil fraud against the Mauldin Group, and therefore dismissed Hryniak's appeal.

III. Outline

[21] In determining the general principles to be followed with respect to summary judgment, I will begin with the values underlying timely, affordable and fair access to justice. Next, I will turn to the role of summary judgment motions generally

and the interpretation of Rule 20 in particular. I will then address specific judicial tools for managing the risks of summary judgment motions.

[22] Finally, I will consider the appropriate standard of review and whether summary judgment should have been granted to the respondents.

IV. Analysis

A. *Access to Civil Justice: A Necessary Culture Shift*

[23] This appeal concerns the values and choices underlying our civil justice system, and the ability of ordinary Canadians to access that justice. Our civil justice system is premised upon the value that the process of adjudication must be fair and just. This cannot be compromised.

[24] However, undue process and protracted trials, with unnecessary expense and delay, can *prevent* the fair and just resolution of disputes. The full trial has become largely illusory because, except where government funding is available,[1] ordinary Canadians cannot afford to access the adjudication of civil disputes.[2] The

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[1] For instance, state funding is available in the child welfare context under *G. (J.)* orders even where legal aid is not available (see *New Brunswick (Minister of Health and Community Services) v. G. (J.)*, [1999] 3 S.C.R. 46, or for cases involving certain minority rights (see the Language Rights Support Program).

[2] In M. D. Agrast, J. C. Botero and A. Ponce, the 2011 *Rule of Law Index*, published by the World Justice Project, Canada ranked 9th among 12 European and North American countries in access to justice. Although Canada scored among the top ten countries in the world in four rule of law categories (limited government powers, order and security, open government, and effective criminal justice), its lowest scores were in access to civil justice. This ranking is "partially explained by

cost and delay associated with the traditional process means that, as counsel for the intervener the Advocates' Society (in *Bruno Appliance*) stated at the hearing of this appeal, the trial process denies ordinary people the opportunity to have adjudication. And while going to trial has long been seen as a last resort, other dispute resolution mechanisms such as mediation and settlement are more likely to produce fair and just results when adjudication remains a realistic alternative.

[25] Prompt judicial resolution of legal disputes allows individuals to get on with their lives. But, when court costs and delays become too great, people look for alternatives or simply give up on justice. Sometimes, they choose to represent themselves, often creating further problems due to their lack of familiarity with the law.

[26] In some circles, private arbitration is increasingly seen as an alternative to a slow judicial process. But private arbitration is not the solution since, without an accessible public forum for the adjudication of disputes, the rule of law is threatened and the development of the common law undermined.

[27] There is growing support for alternative adjudication of disputes and a developing consensus that the traditional balance struck by extensive pre-trial processes and the conventional trial no longer reflects the modern reality and needs to be re-adjusted. A proper balance requires simplified and proportionate procedures for

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shortcomings in the affordability of legal advice and representation, and the lengthy duration of civil cases" (p. 23).

adjudication, and impacts the role of counsel and judges. This balance must recognize that a process can be fair and just, without the expense and delay of a trial, and that alternative models of adjudication are no less legitimate than the conventional trial.

[28] This requires a shift in culture. The principal goal remains the same: a fair process that results in a just adjudication of disputes. A fair and just process must permit a judge to find the facts necessary to resolve the dispute and to apply the relevant legal principles to the facts as found. However, that process is illusory unless it is also accessible — proportionate, timely and affordable. The proportionality principle means that the best forum for resolving a dispute is not always that with the most painstaking procedure.

[29] There is, of course, always some tension between accessibility and the truth-seeking function but, much as one would not expect a jury trial over a contested parking ticket, the procedures used to adjudicate civil disputes must fit the nature of the claim. If the process is disproportionate to the nature of the dispute and the interests involved, then it will not achieve a fair and just result.

[30] The proportionality principle is now reflected in many of the provinces' rules and can act as a touchstone for access to civil justice.[3] For example, Ontario Rules 1.04(1) and 1.04(1.1) provide:

> **1.04** (1) These rules shall be liberally construed to secure the just, most expeditious and least expensive determination of every civil proceeding on its merits.
>
> **1.04** (1.1) In applying these rules, the court shall make orders and give directions that are proportionate to the importance and complexity of the issues, and to the amount involved, in the proceeding.

[31] Even where proportionality is not specifically codified, applying rules of court that involve discretion "includes . . . an underlying principle of proportionality which means taking account of the appropriateness of the procedure, its cost and impact on the litigation, and its timeliness, given the nature and complexity of the litigation" (*Szeto v. Dwyer*, 2010 NLCA 36, 297 Nfld. & P.E.I.R. 311, at para. 53).

[32] This culture shift requires judges to actively manage the legal process in line with the principle of proportionality. While summary judgment motions can save time and resources, like most pre-trial procedures, they can also slow down the proceedings if used inappropriately. While judges can and should play a role in controlling such risks, counsel must, in accordance with the traditions of their profession, act in a way that facilitates rather than frustrates access to justice.

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[3] This principle has been expressly codified in British Columbia, Ontario, and Quebec: *Supreme Court Civil Rules*, B.C. Reg. 168/2009, Rule 1-3(2); *Ontario Rules*, Rule 1.04(1.1); and *Code of Civil Procedure*, R.S.Q., c. C-25, art. 4.2. Aspects of Alberta's and Nova Scotia's rules of court have also been interpreted as reflecting proportionality: *Medicine Shoppe Canada Inc. v. Devchand*, 2012 ABQB 375, 541 A.R. 312, at para. 11; *Saturley v. CIBC World Markets Inc.*, 2011 NSSC 4, 297 N.S.R. (2d) 371, at para. 12.

Lawyers should consider their client's limited means and the nature of their case and fashion proportionate means to achieve a fair and just result.

[33] A complex claim may involve an extensive record and a significant commitment of time and expense. However, proportionality is inevitably comparative; even slow and expensive procedures can be proportionate when they are the fastest and most efficient alternative. The question is whether the added expense and delay of fact finding at trial is necessary to a fair process and just adjudication.

B. *Summary Judgment Motions*

[34] The summary judgment motion is an important tool for enhancing access to justice because it can provide a cheaper, faster alternative to a full trial. With the exception of Quebec, all provinces feature a summary judgment mechanism in their respective rules of civil procedure.[4] Generally, summary judgment is available where there is no genuine issue for trial.

[35] Rule 20 is Ontario's summary judgment procedure, under which a party may move for summary judgment to grant or dismiss all or part of a claim. While, Ontario's Rule 20 in some ways goes further than other rules throughout the country, the values and principles underlying its interpretation are of general application.

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[4] Quebec has a procedural device for disposing of abusive claims summarily: see arts. 54.1 ff of the *Code of Civil Procedure*. While this procedural device is narrower on its face, it has been likened to summary judgment: see *Bal Global Finance Canada Corp. v. Aliments Breton (Canada) inc.*, 2010 QCCS 325 (CanLII). Moreover, s. 165(4) of the Code provides that the defendant may ask for an action to be dismissed if the suit is "unfounded in law".

[36] Rule 20 was amended in 2010, following the recommendations of the Osborne Report, to improve access to justice. These reforms embody the evolution of summary judgment rules from highly restricted tools used to weed out clearly unmeritorious claims or defences to their current status as a legitimate alternative means for adjudicating and resolving legal disputes.

[37] Early summary judgment rules were quite limited in scope and were available only to plaintiffs with claims based on debt or liquidated damages, where no real defence existed.[5] Summary judgment existed to avoid the waste of a full trial in a clear case.

[38] In 1985, the then new Rule 20 extended the availability of summary judgement to both plaintiffs and defendants and broadened the scope of cases that could be disposed of on such a motion. The rules were initially interpreted expansively, in line with the purposes of the rule changes.[6] However, appellate jurisprudence limited the powers of judges and effectively narrowed the purpose of motions for summary judgment to merely ensuring that: "claims that have no chance of success [are] weeded out at an early stage".[7]

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[5] For a thorough review of the history of summary judgment in Ontario, see T. Walsh and L. Posloski, "Establishing a Workable Test for Summary Judgment: Are We There Yet?", in T. L. Archibald and R. S. Echlin, eds., *Annual Review of Civil Litigation 2013* (2013), 419, at pp. 422-32.

[6] *Ibid.*, at p. 426; for example, see *Vaughan v. Warner Communications, Inc.* (1986), 56 O.R. (2d) 242 (H.C.J.).

[7] *Canada (Attorney General) v. Lameman*, 2008 SCC 14, [2008] 1 S.C.R. 372, at para. 10.

[39] The Ontario Government commissioned former Ontario Associate Chief Justice Coulter Osborne Q.C., to consider reforms to make the Ontario civil justice system more accessible and affordable, leading to the report of the Civil Justice Reform Project (the Osborne Report). The Osborne Report concluded that few summary judgment motions were being brought and, if the summary judgment rule was to work as intended, the appellate jurisprudence that had narrowed the scope and utility of the rule had to be reversed (p. 35). Among other things, it recommended that summary judgment be made more widely available, that judges be given the power to weigh evidence on summary judgment motions, and that judges be given discretion to direct that oral evidence be presented (pp. 35-36).

[40] The report also recommended the adoption of a summary trial procedure similar to that employed in British Columbia (p. 37). This particular recommendation was not adopted, and the legislature made the choice to maintain summary judgment as the accessible procedure.

[41] Many of the Osborne Report's recommendations were taken up and implemented in 2010. As noted above, the amendments codify the proportionality principle and provide for efficient adjudication when a conventional trial is not required. They offer significant new tools to judges, which allow them to adjudicate more cases through summary judgment motions and attenuate the risks when such motions do not resolve the entire case.

[42] Rule 20.04 now reads in part:[8]

> **20.04** . . .
>
> (2) [General] The court shall grant summary judgment if,
>
> (a) the court is satisfied that there is no genuine issue requiring a trial with respect to a claim or defence; or
>
> (b) the parties agree to have all or part of the claim determined by a summary judgment and the court is satisfied that it is appropriate to grant summary judgment.
>
> (2.1) [Powers] In determining under clause (2) (a) whether there is a genuine issue requiring a trial, the court shall consider the evidence submitted by the parties and, if the determination is being made by a judge, the judge may exercise any of the following powers for the purpose, unless it is in the interest of justice for such powers to be exercised only at a trial:
>
> 1. Weighing the evidence.
>
> 2. Evaluating the credibility of a deponent.
>
> 3. Drawing any reasonable inference from the evidence.
>
> (2.2) [Oral Evidence (Mini-Trial)] A judge may, for the purposes of exercising any of the powers set out in subrule (2.1), order that oral evidence be presented by one or more parties, with or without time limits on its presentation.

[43] The Ontario amendments changed the test for summary judgment from asking whether the case presents "a genuine issue <u>for</u> trial" to asking whether there is a "genuine issue <u>requiring</u> a trial". The new rule, with its enhanced fact-finding powers, demonstrates that a trial is not the default procedure. Further, it eliminated the presumption of substantial indemnity costs against a party that brought an

[8] The full text of Rule 20 is attached as an Appendix.

unsuccessful motion for summary judgment, in order to avoid deterring the use of the procedure.

[44] The new powers in Rules 20.04(2.1) and (2.2) expand the number of cases in which there will be no genuine issue requiring a trial by permitting motion judges to weigh evidence, evaluate credibility and draw reasonable inferences.[9]

[45] These new fact-finding powers are discretionary and are presumptively available; they may be exercised *unless* it is in the interest of justice for them to be exercised only at a trial; Rule 20.04(2.1). Thus, the amendments are designed to transform Rule 20 from a means to weed out unmeritorious claims to a significant alternative model of adjudication.

[46] I will first consider when summary judgment can be granted on the basis that there is "no genuine issue requiring a trial" (Rule 20.04(2)(a)). Second, I will discuss when it is against the "interest of justice" for the new fact-finding powers in Rule 20.04(2.1) to be used on a summary judgment motion. Third, I will consider the power to call oral evidence and, finally, I will lay out the process to be followed on a motion for summary judgment.

(1) <u>When is There no Genuine Issue Requiring a Trial?</u>

[9] As fully canvassed by the Court of Appeal, the powers in Rule 20.04(2.1) were designed specifically to overrule a number of long-standing appellate decisions that had dramatically restricted the use of the rule; *Aguonie v. Galion Solid Waste Material Inc.* (1998), 38 O.R. (3d) 161 (C.A.); *Dawson v. Rexcraft Storage and Warehouse Inc.* (1998), 164 D.L.R. (4th) 257 (Ont. C.A.).

[47] Summary judgment motions must be granted whenever there is no genuine issue requiring a trial (Rule 20.04(2)(a)). In outlining how to determine whether there is such an issue, I focus on the goals and principles that underlie whether to grant motions for summary judgment. Such an approach allows the application of the rule to evolve organically, lest categories of cases be taken as rules or preconditions which may hinder the system's transformation by discouraging the use of summary judgment.

[48] The Court of Appeal did not explicitly focus upon when there is a genuine issue requiring a trial. However, in considering whether it is against the interest of justice to use the new fact-finding powers, the court suggested that summary judgment would most often be appropriate when cases were document driven, with few witnesses and limited contentious factual issues, or when the record could be supplemented by oral evidence on discrete points. These are helpful observations but, as the court itself recognized, should not be taken as delineating firm categories of cases where summary judgment is and is not appropriate. For example, while this case is complex, with a voluminous record, the Court of Appeal ultimately agreed that there was no genuine issue requiring a trial.

[49] There will be no genuine issue requiring a trial when the judge is able to reach a fair and just determination on the merits on a motion for summary judgment. This will be the case when the process (1) allows the judge to make the necessary

findings of fact, (2) allows the judge to apply the law to the facts, and (3) is a proportionate, more expeditious and less expensive means to achieve a just result.

[50] These principles are interconnected and all speak to whether summary judgment will provide a fair and just adjudication. When a summary judgment motion allows the judge to find the necessary facts and resolve the dispute, proceeding to trial would generally not be proportionate, timely or cost effective. Similarly, a process that does not give a judge confidence in her conclusions can never be the proportionate way to resolve a dispute. It bears reiterating that the standard for fairness is not whether the procedure is as exhaustive as a trial, but whether it gives the judge confidence that she can find the necessary facts and apply the relevant legal principles so as to resolve the dispute.

[51] Often, concerns about credibility or clarification of the evidence can be addressed by calling oral evidence on the motion itself. However, there may be cases where, given the nature of the issues and the evidence required, the judge cannot make the necessary findings of fact, or apply the legal principles to reach a just and fair determination.

(2) The Interest of Justice

[52] The enhanced fact-finding powers granted to motion judges in Rule 20.04(2.1) may be employed on a motion for summary judgment unless it is in the

"interest of justice" for them to be exercised only at trial. The "interest of justice" is not defined in the Rules.

[53] To determine whether the interest of justice allowed the motion judge to use her new powers, the Court of Appeal required a motion judge to ask herself, "can the full appreciation of the evidence and issues that is required to make dispositive findings be achieved by way of summary judgment, or can this full appreciation only be achieved by way of a trial?" (para. 50).

[54] The Court of Appeal identified the benefits of a trial that contribute to this full appreciation of the evidence: the narrative that counsel can build through trial, the ability of witnesses to speak in their own words, and the assistance of counsel in sifting through the evidence (para. 54).

[55] The respondents, as well as the interveners, the Canadian Bar Association, the Attorney General of Ontario and the Advocates' Society, submit that the Court of Appeal's emphasis on the virtues of the traditional trial is misplaced and unduly restrictive. Further, some of these interveners submit that this approach may result in the creation of categories of cases inappropriate for summary judgment, and this will limit the development of the summary judgment vehicle.

[56] While I agree that a motion judge must have an appreciation of the evidence necessary to make dispositive findings, such an appreciation is not only available at trial. Focussing on how much and what kind of evidence could be

adduced at a trial, as opposed to whether a trial is "requir[ed]" as the Rule directs, is likely to lead to the bar being set too high. The interest of justice cannot be limited to the advantageous features of a conventional trial, and must account for proportionality, timeliness and affordability. Otherwise, the adjudication permitted with the new powers — and the purpose of the amendments — would be frustrated.

[57] On a summary judgment motion, the evidence need not be equivalent to that at trial, but must be such that the judge is confident that she can fairly resolve the dispute. A documentary record, particularly when supplemented by the new fact-finding tools, including ordering oral testimony, is often sufficient to resolve material issues fairly and justly. The powers provided in Rules 20.04(2.1) and 20.04(2.2) can provide an equally valid, if less extensive, manner of fact finding.

[58] This inquiry into the interest of justice is, by its nature, comparative. Proportionality is assessed in relation to the full trial. It may require the motion judge to assess the relative efficiencies of proceeding by way of summary judgment, as opposed to trial. This would involve a comparison of, among other things, the cost and speed of both procedures. (Although summary judgment may be expensive and time consuming, as in this case, a trial may be even more expensive and slower.) It may also involve a comparison of the evidence that will be available at trial and on the motion as well as the opportunity to fairly evaluate it. (Even if the evidence available on the motion is limited, there may be no reason to think better evidence would be available at trial.)

[59] In practice, whether it is against the "interest of justice" to use the new fact-finding powers will often coincide with whether there is a "genuine issue requiring a trial". It is logical that, when the use of the new powers would enable a judge to fairly and justly adjudicate a claim, it will generally not be against the interest of justice to do so. What is fair and just turns on the nature of the issues, the nature and strength of the evidence and what is the proportional procedure.

[60] The "interest of justice" inquiry goes further, and also considers the consequences of the motion in the context of the litigation as a whole. For example, if some of the claims against some of the parties will proceed to trial in any event, it may not be in the interest of justice to use the new fact-finding powers to grant summary judgment against a single defendant. Such partial summary judgment may run the risk of duplicative proceedings or inconsistent findings of fact and therefore the use of the powers may not be in the interest of justice. On the other hand, the resolution of an important claim against a key party could significantly advance access to justice, and be the most proportionate, timely and cost effective approach.

(3) <u>The Power to Hear Oral Evidence</u>

[61] Under Rule 20.04(2.2), the motion judge is given the power to hear oral evidence to assist her in making findings under Rule 20.04(2.1). The decision to allow oral evidence rests with the motion judge since, as the Court of Appeal noted, "it is the motion judge, not counsel, who maintains control over the extent of the evidence to be led and the issues to which the evidence is to be directed" (para. 60).

[62] The Court of Appeal suggested the motion judge should only exercise this power when

> (1) Oral evidence can be obtained from a small number of witnesses and gathered in a manageable period of time; (2) Any issue to be dealt with by presenting oral evidence is likely to have a significant impact on whether the summary judgment motion is granted; and (3) Any such issue is narrow and discrete — *i.e.*, the issue can be separately decided and is not enmeshed with other issues on the motion. [para. 103]

This is useful guidance to ensure that the hearing of oral evidence does not become unmanageable; however, as the Court of Appeal recognized, these are not absolute rules.

[63] This power should be employed when it allows the judge to reach a fair and just adjudication on the merits and it is the proportionate course of action. While this is more likely to be the case when the oral evidence required is limited, there will be cases where extensive oral evidence can be heard on the motion for summary judgment, avoiding the need for a longer, more complex trial and without compromising the fairness of the procedure.

[64] Where a party seeks to lead oral evidence, it should be prepared to demonstrate why such evidence would assist the motion judge in weighing the evidence, assessing credibility, or drawing inferences and to provide a "will say" statement or other description of the proposed evidence so that the judge will have a basis for setting the scope of the oral evidence.

[65] Thus, the power to call oral evidence should be used to promote the fair and just resolution of the dispute in light of principles of proportionality, timeliness and affordability. In tailoring the nature and extent of oral evidence that will be heard, the motion judge should be guided by these principles, and remember that the process is not a full trial on the merits but is designed to determine if there is a genuine issue requiring a trial.

(4) The Roadmap/Approach to a Motion for Summary Judgment

[66] On a motion for summary judgment under Rule 20.04, the judge should first determine if there is a genuine issue requiring trial based only on the evidence before her, *without* using the new fact-finding powers. There will be no genuine issue requiring a trial if the summary judgment process provides her with the evidence required to fairly and justly adjudicate the dispute and is a timely, affordable and proportionate procedure, under Rule 20.04(2)(a). If there appears to be a genuine issue requiring a trial, she should then determine if the need for a trial can be avoided by using the new powers under Rules 20.04(2.1) and (2.2). She may, at her discretion, use those powers, provided that their use is not against the interest of justice. Their use will not be against the interest of justice if they will lead to a fair and just result and will serve the goals of timeliness, affordability and proportionality in light of the litigation as a whole.

[67] Inquiring first as to whether the use of the powers under Rule 20.04(2.1) will allow the dispute to be resolved by way of summary judgment, before asking

whether the interest of justice requires that those powers be exercised only at trial, emphasizes that these powers are presumptively available, rather than exceptional, in line with the goal of proportionate, cost-effective and timely dispute resolution. As well, by first determining the consequences of using the new powers, the benefit of their use is clearer. This will assist in determining whether it is in the interest of justice that they be exercised only at trial.

[68] While summary judgment *must* be granted if there is no genuine issue requiring a trial,[10] the decision to use either the expanded fact-finding powers or to call oral evidence is discretionary.[11] The discretionary nature of this power gives the judge some flexibility in deciding the appropriate course of action. This discretion can act as a safety valve in cases where the use of such powers would clearly be inappropriate. There is always the risk that clearly unmeritorious motions for summary judgment could be abused and used tactically to add time and expense. In such cases, the motion judge may choose to decline to exercise her discretion to use those powers and dismiss the motion for summary judgment, without engaging in the full inquiry delineated above.

C. *Tools to Maximize the Efficiency of a Summary Judgment Motion*

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[10] Rule 20.04(2): "The court shall grant summary judgment if, (a) the court is satisfied that there is no genuine issue requiring a trial . . .".

[11] Rule 20.04(2.1): "In determining . . . whether there is a genuine issue requiring a trial . . . if the determination is being made by a judge, the judge may exercise any of the following powers . . . 1. Weighing the evidence. 2. Evaluating the credibility of a deponent. 3. Drawing any reasonable inference from the evidence." Rule 20.04(2.2): "A judge may . . . order that oral evidence be presented . . .".

(1) Controlling the Scope of a Summary Judgment Motion

[69] The *Ontario Rules* and a superior court's inherent jurisdiction permit a motion judge to be involved early in the life of a motion, in order to control the size of the record, and to remain active in the event the motion does not resolve the entire action.

[70] The Rules provide for early judicial involvement, through Rule 1.05, which allows for a motion for directions, to manage the time and cost of the summary judgment motion. This allows a judge to provide directions with regard to the timelines for filing affidavits, the length of cross-examination, and the nature and amount of evidence that will be filed. However, motion judges must also be cautious not to impose administrative measures that add an unnecessary layer of cost.

[71] Not all motions for summary judgment will require a motion for directions. However, failure to bring such a motion where it was evident that the record would be complex or voluminous may be considered when dealing with costs consequences under Rule 20.06(a). In line with the principle of proportionality, the judge hearing the motion for directions should generally be seized of the summary judgment motion itself, ensuring the knowledge she has developed about the case does not go to waste.

[72] I agree with the Court of Appeal (at paras. 58 and 258) that a motion for directions also provides the responding party with the opportunity to seek an order to

stay or dismiss a premature or improper motion for summary judgment. This may be appropriate to challenge lengthy, complex motions, particularly on the basis that they would not sufficiently advance the litigation, or serve the principles of proportionality, timeliness and affordability.

[73] A motion for summary judgment will not always be the most proportionate way to dispose of an action. For example, an early date may be available for a short trial, or the parties may be prepared to proceed with a summary trial. Counsel should always be mindful of the most proportionate procedure for their client and the case.

(2) Salvaging a Failed Summary Judgment Motion

[74] Failed, or even partially successful, summary judgment motions add — sometimes astronomically — to costs and delay. However, this risk can be attenuated by a judge who makes use of the trial management powers provided in Rule 20.05 and the court's inherent jurisdiction.

[75] Rule 20.05(1) and (2) provides in part:

> **20.05** (1) Where summary judgment is refused or is granted only in part, the court may make an order specifying what material facts are not in dispute and defining the issues to be tried, and order that the action proceed to trial expeditiously.
>
> (2) If an action is ordered to proceed to trial under subrule (1), the court may give such directions or impose such terms as are just . . .

[76] Rules 20.05(2)(a) through (p) outline a number of specific trial management orders that may be appropriate. The court may: set a schedule; provide a restricted discovery plan; set a trial date; require payment into court of the claim; or order security for costs. The court may order that: the parties deliver a concise summary of their opening statement; the parties deliver a written summary of the anticipated evidence of a witness; any oral examination of a witness at trial will be subject to a time limit or; the evidence of a witness be given in whole or in part by affidavit.

[77] These powers allow the judge to use the insight she gained from hearing the summary judgment motion to craft a trial procedure that will resolve the dispute in a way that is sensitive to the complexity and importance of the issue, the amount involved in the case, and the effort expended on the failed motion. The motion judge should look to the summary trial as a model, particularly where affidavits filed could serve as the evidence of a witness, subject to time-limited examinations and cross-examinations. Although the Rules did not adopt the Osborne Report's recommendation of a summary trial model, this model already exists under the simplified rules or on consent. In my view, the summary trial model would also be available further to the broad powers granted a judge under Rule 20.05(2).

[78] Where a motion judge dismisses a motion for summary judgment, in the absence of compelling reasons to the contrary, she should also seize herself of the

matter as the trial judge. I agree with the Osborne Report that the involvement of a single judicial officer throughout

> saves judicial time since parties will not have to get a different judge up to speed each time an issue arises in the case. It may also have a calming effect on the conduct of litigious parties and counsel, as they will come to predict how the judicial official assigned to the case might rule on a given issue. [p. 88]

[79] While such an approach may complicate scheduling, to the extent that current scheduling practices prevent summary judgment motions being used in an efficient and cost effective manner, the courts should be prepared to change their practices in order to facilitate access to justice.

D. *Standard of Review*

[80] The Court of Appeal concluded that determining the appropriate test for summary judgment — whether there is a genuine issue requiring a trial — is a legal question, reviewable on a correctness standard, while any factual determinations made by the motions judge will attract deference.

[81] In my view, absent an error of law, the exercise of powers under the new summary judgment rule attracts deference. When the motion judge exercises her new fact-finding powers under Rule 20.04(2.1) and determines whether there is a genuine issue requiring a trial, this is a question of mixed fact and law. Where there is no extricable error in principle, findings of mixed fact and law, should not be overturned,

absent palpable and overriding error, *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235, at para. 36.

[82] Similarly, the question of whether it is in the "interest of justice" for the motion judge to exercise the new fact-finding powers provided by Rule 20.04(2.1) depends on the relative evidence available at the summary judgment motion and at trial, the nature, size, complexity and cost of the dispute and other contextual factors. Such a decision is also a question of mixed fact and law which attracts deference.

[83] Provided that it is not against the "interest of justice", a motion judge's decision to exercise the new powers is discretionary. Thus, unless the motion judge misdirected herself, or came to a decision that is so clearly wrong that it resulted in an injustice, her decision should not be disturbed.

[84] Of course, where the motion judge applies an incorrect principle of law, or errs with regard to a purely legal question, such as the elements that must be proved for the plaintiff to make out her cause of action, the decision will be reviewed on a correctness standard (*Housen v. Nikolaisen*, at para. 8).

E. *Did the Motion Judge Err by Granting Summary Judgment?*

[85] The motion judge granted summary judgment in favour of the Mauldin Group. While the Court of Appeal found that the action should not have been decided by summary judgment, it nevertheless dismissed the appeal. Hryniak argues

this constituted "prospective overruling" but, in light of my conclusion that the motion judge was entitled to proceed by summary judgment, I need not consider these submissions further. For the reasons that follow, I am satisfied that the motion judge did not err in granting summary judgment.

(1) <u>The Tort of Civil Fraud</u>

[86] The action underlying this motion for summary judgment was one for civil fraud brought against Hryniak, Peebles, and Cassels Brock.

[87] As discussed in the companion *Bruno Appliance* appeal, the tort of civil fraud has four elements, which must be proven on a balance of probabilities: (1) a false representation by the defendant; (2) some level of knowledge of the falsehood of the representation on the part of the defendant (whether knowledge or recklessness); (3) the false representation caused the plaintiff to act; (4) the plaintiff's actions resulted in a loss.

(2) <u>Was There a Genuine Issue Requiring a Trial?</u>

[88] In granting summary judgment to the Mauldin Group against Hryniak, the motion judge did not explicitly address the correct test for civil fraud but, like the Court of Appeal, I am satisfied that his findings support that result.

[89] The first element of civil fraud is a false representation by the defendant. The Court of Appeal agreed with the motion judge that "[u]nquestionably, the Mauldin group was induced to invest with Hryniak because of what Hryniak said to Fred Mauldin" at the meeting of June 19, 2001 (at para. 158), and this was not disputed in the appellant's factum.

[90] The motion judge found the requisite knowledge or recklessness as to the falsehood of the representation, the second element of civil fraud, based on Hryniak's lack of effort to ensure that the funds would be properly invested and failure to verify that the eventual end-point of the funds, New Savings Bank, was secure. The motion judge also rejected the defence that the funds were stolen, noting Hryniak's feeble efforts to recover the funds, waiting some 15 months to report the apparent theft of US$10.2 million.

[91] The motion judge also found an intention on the part of Hryniak that the Mauldin Group would act on his false representations, the third requirement of civil fraud. Hryniak secured a US$76,000 loan for Fred Mauldin and conducted a "test trade", actions which, in the motion judge's view, were "undertaken . . . for the purpose of dissuading the Mauldin group from demanding the return of its investment" (para. 113). Moreover, the motion judge detailed Hryniak's central role in the web of deception that caused the Mauldin Group to invest its funds and that dissuaded them from seeking their return for some time after they had been stolen.

[92] The final requirement of civil fraud, loss, is clearly present. The Mauldin Group invested US$1.2 million and, but for a small return of US$9,600 in February 2002, lost its investment.

[93] The motion judge found no credible evidence to support Hryniak's claim that he was a legitimate trader, and the outcome was therefore clear, so the motion judge concluded there was no issue requiring a trial. He made no palpable and overriding error in granting summary judgment.

(3) Did the Interest of Justice Preclude the Motion Judge from Using his Powers Under Rule 20.04?

[94] The motion judge did not err in exercising his fact-finding powers under Rule 20.04(2.1). He was prepared to sift through the detailed record, and was of the view that sufficient evidence had been presented on all relevant points to allow him to draw the inferences necessary to make dispositive findings under Rule 20. Further, while the amount involved is significant, the issues raised by Hryniak's defence were fairly straightforward. As the Court of Appeal noted, at root, the question turned on whether Hryniak had a legitimate trading program that went awry when the funds were stolen, or whether his program was a sham from the outset (para. 159). The plaintiffs are a group of elderly American investors and, at the return date of the motion, had been deprived of their funds for nearly a decade. The record was sufficient to make a fair and just determination and a timely resolution of the matter

was called for. While the motion was complex and expensive, going to trial would have cost even more and taken even longer.

[95] Despite the fact that the Mauldin group's claims against Peebles and Cassels Brock had to proceed to trial, there is little reason to believe that granting summary judgment against Hryniak would have a prejudicial impact on the trial of the remaining issues. While the extent of the other defendants' involvement in the fraud requires a trial, that matter is not predetermined by the conclusion that Hryniak clearly was a perpetrator of the fraud. The motion judge's findings speak specifically to Hryniak's involvement and neither rely upon, nor are inconsistent with, the liability of others. His findings were clearly supported by the evidence. It was neither against the interest of justice for the motion judge to use his fact-finding powers nor was his discretionary decision to do so tainted with error.

V. Conclusion

[96] Accordingly, I would dismiss the appeal, with costs to the respondents.

APPENDIX

Rules of Civil Procedure, R.R.O. 1990, Reg. 194

RULE 20 SUMMARY JUDGMENT

20.01 [Where Available] (1) [To Plaintiff] A plaintiff may, after the defendant has delivered a statement of defence or served a notice of motion, move with supporting affidavit material or other evidence for summary judgment on all or part of the claim in the statement of claim.

(2) The plaintiff may move, without notice, for leave to serve a notice of motion for summary judgment together with the statement of claim, and leave may be given where special urgency is shown, subject to such directions as are just.

(3) [To Defendant] A defendant may, after delivering a statement of defence, move with supporting affidavit material or other evidence for summary judgment dismissing all or part of the claim in the statement of claim.

20.02 [Evidence on Motion] (1) An affidavit for use on a motion for summary judgment may be made on information and belief as provided in subrule 39.01 (4), but, on the hearing of the motion, the court may, if appropriate, draw an adverse inference from the failure of a party to provide the evidence of any person having personal knowledge of contested facts.

(2) In response to affidavit material or other evidence supporting a motion for summary judgment, a responding party may not rest solely on the allegations or denials in the party's pleadings, but must set out, in affidavit material or other evidence, specific facts showing that there is a genuine issue requiring a trial.

20.03 [Factums Required] (1) On a motion for summary judgment, each party shall serve on every other party to the motion a factum consisting of a concise argument stating the facts and law relied on by the party.

(2) The moving party's factum shall be served and filed with proof of service in the court office where the motion is to be heard at least seven days before the hearing.

(3) The responding party's factum shall be served and filed with proof of service in the court office where the motion is to be heard at least four days before the hearing.

(4) Revoked.

20.04 [Disposition of Motion] (1) [General] Revoked.

(2) The court shall grant summary judgment if,
(a) the court is satisfied that there is no genuine issue requiring a trial with respect to a claim or defence; or
(b) the parties agree to have all or part of the claim determined by a summary judgment and the court is satisfied that it is appropriate to grant summary judgment.

(2.1) [Powers] In determining under clause (2) (a) whether there is a genuine issue requiring a trial, the court shall consider the evidence submitted by the parties and, if the determination is being made by a judge, the judge may exercise any of the following powers for the purpose, unless it is in the interest of justice for such powers to be exercised only at a trial:
1. Weighing the evidence.
2. Evaluating the credibility of a deponent.
3. Drawing any reasonable inference from the evidence.

(2.2) [Oral Evidence (Mini-Trial)] A judge may, for the purposes of exercising any of the powers set out in subrule (2.1), order that oral evidence be presented by one or more parties, with or without time limits on its presentation.

(3) Where the court is satisfied that the only genuine issue is the amount to which the moving party is entitled, the court may order a trial of that issue or grant judgment with a reference to determine the amount.

(4) [Only Genuine Issue Is Question Of Law] Where the court is satisfied that the only genuine issue is a question of law, the court may determine the question and grant judgment accordingly, but where the motion is made to a master, it shall be adjourned to be heard by a judge.

(5) [Only Claim Is For An Accounting] Where the plaintiff is the moving party and claims an accounting and the defendant fails to satisfy the court that there is a preliminary issue to be tried, the court may grant judgment on the claim with a reference to take the accounts.

20.05 [Where A Trial Is Necessary] (1) [Powers of Court] Where summary judgment is refused or is granted only in part, the court may make an order specifying what material facts are not in dispute and defining the issues to be tried, and order that the action proceed to trial expeditiously.

(2) [Directions And Terms] If an action is ordered to proceed to trial under subrule (1), the court may give such directions or impose such terms as are just, including an order,

(a) that each party deliver, within a specified time, an affidavit of documents in accordance with the court's directions;
(b) that any motions be brought within a specified time;
(c) that a statement setting out what material facts are not in dispute be filed within a specified time;
(d) that examinations for discovery be conducted in accordance with a discovery plan established by the court, which may set a schedule for examinations and impose such limits on the right of discovery as are just, including a limit on the scope of discovery to matters not covered by the affidavits or any other evidence filed on the motion and any cross-examinations on them;
(e) that a discovery plan agreed to by the parties under Rule 29.1 (discovery plan) be amended;
(f) that the affidavits or any other evidence filed on the motion and any cross-examinations on them may be used at trial in the same manner as an examination for discovery;
(g) that any examination of a person under Rule 36 (taking evidence before trial) be subject to a time limit;
(h) that a party deliver, within a specified time, a written summary of the anticipated evidence of a witness;
(i) that any oral examination of a witness at trial be subject to a time limit;
(j) that the evidence of a witness be given in whole or in part by affidavit;
(k) that any experts engaged by or on behalf of the parties in relation to the action meet on a without prejudice basis in order to identify the issues on which the experts agree and the issues on which they do not agree, to attempt to clarify and resolve any issues that are the subject of disagreement and to prepare a joint statement setting out the areas of agreement and any areas of disagreement and the reasons for it if, in the opinion of the court, the cost or time savings or other benefits that may be achieved from the meeting are proportionate to the amounts at stake or the importance of the issues involved in the case and,
    (i) there is a reasonable prospect for agreement on some or all of the issues, or
    (ii) the rationale for opposing expert opinions is unknown and clarification on areas of disagreement would assist the parties or the court;
(l) that each of the parties deliver a concise summary of his or her opening statement;
(m) that the parties appear before the court by a specified date, at which appearance the court may make any order that may be made under this subrule;

(n) that the action be set down for trial on a particular date or on a particular trial list, subject to the direction of the regional senior judge;
(o) for payment into court of all or part of the claim; and
(p) for security for costs.

(3) [Specified Facts] At the trial, any facts specified under subrule (1) or clause (2) (c) shall be deemed to be established unless the trial judge orders otherwise to prevent injustice.

(4) [Order re Affidavit Evidence] In deciding whether to make an order under clause (2) (j), the fact that an adverse party may reasonably require the attendance of the deponent at trial for cross-examination is a relevant consideration.

(5) [Order re Experts, Costs] If an order is made under clause (2) (k), each party shall bear his or her own costs.

(6) [Failure To Comply With Order] Where a party fails to comply with an order under clause (2) (o) for payment into court or under clause (2) (p) for security for costs, the court on motion of the opposite party may dismiss the action, strike out the statement of defence or make such other order as is just.

(7) Where on a motion under subrule (6) the statement of defence is struck out, the defendant shall be deemed to be noted in default.

20.06 [Costs Sanctions For Improper Use Of Rule] The court may fix and order payment of the costs of a motion for summary judgment by a party on a substantial indemnity basis if,

(a) the party acted unreasonably by making or responding to the motion; or
(b) the party acted in bad faith for the purpose of delay.

20.07 [Effect Of Summary Judgment] A plaintiff who obtains summary judgment may proceed against the same defendant for any other relief.

20.08 [Stay Of Execution] Where it appears that the enforcement of a summary judgment ought to be stayed pending the determination of any other issue in the action or a counterclaim, crossclaim or third party claim, the court may so order on such terms as are just.

20.09 [Application To Counterclaims, Crossclaims And Third Party Claim] Rules 20.01 to 20.08 apply, with necessary modifications, to counterclaims, crossclaims and third party claims.

Appeal dismissed with costs.

Solicitors for the appellant: McCarthy Tétrault, Toronto.

Solicitors for the respondents: Heydary Hamilton, Toronto.

Solicitors for the intervener the Ontario Trial Lawyers Association: Allan Rouben, Toronto; SBMB Law, Richmond Hill, Ontario.

Solicitors for the intervener the Canadian Bar Association: Evans Sweeny Bordin, Hamilton; Sotos, Toronto.

Tab 2

CanLII

Dunn v. Chubb Insurance Company of Canada, 2009 ONCA 538 (CanLII)

Date:	2009-07-02
Docket:	C50079; C50141
Parallel citations:	97 OR (3d) 701
URL:	http://canlii.ca/t/24684
Citation:	Dunn v. Chubb Insurance Company of Canada, 2009 ONCA 538 (CanLII), <http://canlii.ca/t/24684> retrieved on 2014-01-31
Print:	PDF Format
Noteup:	Search for decisions citing this decision
Reflex Record	Related decisions, legislation cited and decisions cited

Dunn v. Chubb Insurance Company of Canada et al.
Beatty v. Chubb Insurance Company of Canada et al.
[Indexed as: Dunn v. Chubb Insurance Co. of Canada]

97 O.R. (3d) 701

Court of Appeal for Ontario,
O'Connor A.C.J.O., Lang and Watt JJ.A.
July 2, 2009

Insurance -- Interpretation and construction -- Application judge dismissing application by insured for declaration that insurer was obligated to pay 90 or 100 per cent of defence costs -- Insured appealing -- Appeal allowed -- Clause relating to allocation of defence costs in directors and officers liability insurance policy being ambiguous -- Evidence before court insufficient to assist it in resolving ambiguity -- New hearing of application directed to give parties opportunity to call evidence regarding factual matrix of agreement and evidence that would inform contra proferentem issue.

During the policy period of a directors and officers liability policy (the "2001 Policy"), the appellants participated in conduct that became the subject of civil proceedings commenced in 2001 and 2002 (the "2001 Proceedings"). The respondent [page702] insurer acknowledged that the 2001 Proceedings triggered coverage under the 2001 Policy. In 2004 and subsequent years, further proceedings were brought against the appellants, including civil proceedings and proceedings by the Ontario Securities

Commission and the United States Securities and Exchange Commission (the "Hybrid Proceedings"). All of those proceedings included allegations against the appellants by reason of their conduct in 2001 (the "2001 Conduct") and their conduct in 2003 and 2004 (the "2003 Conduct"). The respondent accepted that it was responsible for 100 per cent of the defence costs incurred by the appellants in the Hybrid Proceedings to the extent that those proceedings related to the 2001 Conduct, but took the position that it was not responsible for the appellants' defence costs in the Hybrid Proceedings to the extent that those costs related exclusively to the appellants 2003 Conduct. As a result, the respondent was paying 50 per cent of the defence costs for the Hybrid Proceedings. An application by the appellants for a declaration that the respondent was responsible to pay either 90 or 100 per cent of the defence costs relating to the Hybrid Proceedings was dismissed. The appellants appealed.

Held, the appeal should be allowed.

The insurance policy, as it related to the allocation of defence costs, was ambiguous. It was impossible to resolve the ambiguity on the factual record before the court. There was virtually no evidence about the context or the factual matrix within which the 2001 Policy was agreed to. While both sides urged that "commercial realities" supported their interpretation, there was little in the record to assist the court in assessing the relative commercial practicality of the approaches advocated by each party. It was undesirable to resolve the ambiguity without providing the parties an opportunity to call evidence regarding the factual matrix of the agreement, as well as extrinsic evidence that would inform the contra proferentem issue. For that reason, a new hearing was required on that issue only.

APPEAL from judgment of C.L. Campbell J., 2009 CanLII 7083 (ON SC), [2009] O.J. No. 720, 2009 CanLII 7083 (S.C.J.) dismissing an application for a declaration that the insurer was obligated to pay 90 or 100 per cent of the appellants' defence costs. [page704]

Cases referred to Boliden Ltd. v. Liberty Mutual Insurance Co., 2008 ONCA 418 (CanLII), [2008] O.J. No. 2079, 2008 ONCA 418, 62 C.C.L.I. (4th) 56; Boucher v. Public Accounts Council for the Province of Ontario 2004 CanLII 14579 (ON CA), (2004), 71 O.R. (3d) 291, [2004] O.J. No. 2634, 188 O.A.C. 201, 48 C.P.C. (5th) 56, 132 A.C.W.S. (3d) 15 (C.A.); Brisette Estate v. Westbury Life Insurance Co., 1992 CanLII 32 (SCC), [1992] 3 S.C.R. 87, [1992] S.C.J. No. 86, 96 D.L.R. (4th) 609, 142 N.R. 104, J.E. 92-1622, 58 O.A.C. 10, 13 C.C.L.I. (2d) 1, 47 E.T.R. 109, [1992] I.L.R. Â1-2888 at 2051, 36 A.C.W.S. (3d) 449; Canadian Crude Separators Ltd. v. W.A. (Wes) Jacobson, 1998 ABQB 590 (CanLII), [1998] A.J. No. 787, 1998 ABQB 590, 66 Alta. L.R. (3d) 312, 226 A.R. 171, 81 A.C.W.S. (3d) 466; Canadian National Railway Co. v. Royal and Sun Alliance Insurance Co. of Canada, 2008 SCC 66 (CanLII), [2008] 3 S.C.R. 453, [2008] S.C.J. No. 67, 2008 SCC 66, EYB 2008-150740, J.E. 2008-2205, 299 D.L.R. (4th) 1, 170 A.C.W.S. (3d) 623, 381 N.R. 332, [2009] I.L.R. I-4755, 243 O.A.C. 340, 68 C.C.L.I. (4th) 1, revg 2007 ONCA 209 (CanLII), (2007), 85 O.R. (3d) 186, [2007] O.J. No. 1077, 2007 ONCA 209, 222 O.A.C. 129, 48 C.C.L.I. (4th) 161, 59 C.L.R. (3d) 169, [2007] I.L.R. I-4591, 156 A.C.W.S. (3d) 207, revg [2004] O.J. No. 4086, [2004] O.T.C. 851, 15 C.C.L.I. (4th) 1, 134 A.C.W.S. (3d) 319 (S.C.J.); Canadian Premier Holdings Ltd. v. Winterthur Canada Financial Corp., 2000 CanLII 5724 (ON CA), [2000] O.J. No. 1619, 132 O.A.C. 172, 96 A.C.W.S. (3d) 595 (C.A.); Chubb

Custom Ins. Co. v. Prudential Ins. Co. of America, 948 A.2d 1285, 195 N.J. 231 (2008); Consolidated-Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co., 1979 CanLII 10 (SCC), [1980] 1 S.C.R. 888, [1979] S.C.J. No. 133, 112 D.L.R. (3d) 49, 32 N.R. 488, [1980] I.L.R. Â1-1176 at 595, 1 A.C.W.S. (2d) 169; Eagle Leasing Corp. v. Hartford Fire Ins. Co., 540 F.2d 1257 (5th Cir. 1976); Eli Lilly & Co. v. Novopharm Ltd., 1998 CanLII 791 (SCC), [1998] 2 S.C.R. 129, [1998] S.C.J. No. 59, 161 D.L.R. (4th) 1, 227 N.R. 201, J.E. 98-1562, 80 C.P.R. (3d) 321, 80 A.C.W.S. (3d) 871; [page703] F.D.I.C. v. Ins. Co. of North America, 105 F.3d 778 (1st Cir. 1997); Fletcher v. Manitoba Public Insurance Co., 1990 CanLII 59 (SCC), [1990] 3 S.C.R. 191, [1990] S.C.J. No. 121, 74 D.L.R. (4th) 636, 116 N.R. 1, J.E. 90-1652, 71 Man. R. (2d) 81, 44 O.A.C. 81, 1 C.C.L.I. (2d) 1, 5 C.C.L.T. (2d) 1, [1990] I.L.R. Â1-2672 at 10547, 30 M.V.R. (2d) 260, 23 A.C.W.S. (3d) 1248; Fountain Powerboat Industries, Inc. v. Reliance Ins. Co., 119 F.Supp.2d 552 (E.D.N.C. 2000); Fraser River Pile & Dredge Ltd. v. Can-Dive Services Ltd., 1999 CanLII 654 (SCC), [1999] 3 S.C.R. 108, [1999] S.C.J. No. 48, 176 D.L.R. (4th) 257, 245 N.R. 88, [1999] 9 W.W.R. 380, 127 B.C.A.C. 287, 67 B.C.L.R. (3d) 213, 50 B.L.R. (2d) 169, 11 C.C.L.I. (3d) 1, 47 C.C.L.T. (2d) 1, [1999] I.L.R. I-3717, 90 A.C.W.S. (3d) 786; Hanis v. Teevan 2008 ONCA 678 (CanLII), (2008), 92 O.R. (3d) 594, [2008] O.J. No. 3909, 2008 ONCA 678, 69 C.C.E.L. (3d) 86, 241 O.A.C. 303, [2008] I.L.R. I-4748, 67 C.C.L.I. (4th) 196; Hanis v. University of Western Ontario, 2008 ONCA 793 (CanLII), [2008] O.J. No. 4706, 2008 ONCA 793, 70 C.C.E.L. (3d) 18, 67 C.C.L.I. (4th) 210; Hillis Oil & Sales v. Wynn's Canada, 1986 CanLII 44 (SCC), [1986] 1 S.C.R. 57, [1986] S.C.J. No. 9, 25 D.L.R. (4th) 649, 65 N.R. 23, J.E. 86-281, 71 N.S.R. (2d) 353, 36 A.C.W.S. (2d) 3; Hi-Tech Group Inc. v. Sears Canada Inc. 2001 CanLII 24049 (ON CA), (2001), 52 O.R. (3d) 97, [2001] O.J. No. 33, 141 O.A.C. 56, 11 B.L.R. (3d) 197, 4 C.P.C. (5th) 35, 102 A.C.W.S. (3d) 79 (C.A.); Indemnity Insurance Co. of North America v. Excel Cleaning Service, 1954 CanLII 9 (SCC), [1954] S.C.R. 169, [1954] S.C.J. No. 11, [1954] 2 D.L.R. 721, [1954] I.L.R. Â1-143 at 590; Jesuit Fathers of Upper Canada v. Guardian Insurance Co. of Canada, 2006 SCC 21 (CanLII), [2006] 1 S.C.R. 744, [2006] S.C.J. No. 21, 2006 SCC 21, 267 D.L.R. (4th) 1, 348 N.R. 307, J.E. 2006-1123, 211 O.A.C. 363, [2006] R.R.A. 523, 36 C.C.L.I. (4th) 161, [2006] I.L.R. I-4512, 147 A.C.W.S. (3d) 1058, EYB 2006-105962; Kentucky Fried Chicken v. Scott's Food Services Inc., 1998 CanLII 4427 (ON CA), [1998] O.J. No. 4368, 114 O.A.C. 357, 41 B.L.R. (2d) 42, 83 A.C.W.S. (3d) 382 (C.A.); L auren International, Inc. v. Reichert, 2008 ONCA 382 (CanLII), [2008] O.J. No. 1891, 2008 ONCA 382, 237 O.A.C. 94, 167 A.C.W.S. (3d) 174, 45 B.L.R. (4th) 172, 70 C.P.R. (4th) 377; M. (E.) v. Reed, [2003] O.J. No. 1791, 49 C.C.L.I. (3d) 57, [2003] I.L.R. I-4191, 122 A.C.W.S. (3d) 929 (C.A.); McClelland & Stewart Ltd. v. Mutual Life Assurance Co. of Canada, 1981 CanLII 53 (SCC), [1981] 2 S.C.R. 6, [1981] S.C.J. No. 60, 125 D.L.R. (3d) 257 at 258, 37 N.R. 190, [1981] I.L.R. Â1-1393 at 321, 9 A.C.W.S. (2d) 264; Non-Marine Underwriters, Lloyd's of London v. Scalera, 2000 SCC 24 (CanLII), [2000] 1 S.C.R. 551, [2000] S.C.J. No. 26, 2000 SCC 24, 185 D.L.R. (4th) 1, 253 N.R. 1, [2000] 5 W.W.R. 465, J.E. 2000-935, 135 B.C.A.C. 161, 75 B.C.L.R. (3d) 1, 18 C.C.L.I. (3d) 1, 50 C.C.L.T. (2d) 1, [2000] I.L.R. I-3810, 96 A.C.W.S. (3d) 479; Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co., 1993 CanLII 150 (SCC), [1993] 1 S.C.R. 252, [1993] S.C.J. No. 10, 99 D.L.R. (4th) 741, 147 N.R. 44, [1993] 2 W.W.R. 433, J.E. 93-230, 83 Man. R. (2d) 81, 13 C.C.L.I . (2d) 161, 6 C.L.R. (2d) 161, [1993] I.L.R. Â1-2914 at 2206, 37 A.C.W.S. (3d) 1267; Showmart Management Ltd. v. 853436 Ontario Ltd. (c.o.b. Features Cafe), [1998] O.J. No. 1645, 64 O.T.C. 187, 18 R.P.R. (3d) 128, 79 A.C.W.S. (3d) 155 (Gen. Div.); SimEx Inc. v.

IMAX Corp., 2005 CanLII 46629 (ON CA), [2005] O.J. No. 5389, 206 O.A.C. 3, 11 B.L.R. (4th) 214, 144 A.C.W.S. (3d) 256 (C.A.); Six Flags, Inc. v. Westchester Surplus Lines Ins. Co., 565 F.3d 948 (5th Cir. 2009); Stevenson v. Reliance Petroleum Ltd., 1956 CanLII 27 (SCC), [1956] S.C.R. 936, [1956] S.C.J. No. 68, 5 D.L.R. (2d) 673, [1956] I.L.R. Â1-238 at 127; United Brotherhood of Carpenters and Joiners of America, Local 579 v. Bradco Construction Ltd., 1993 CanLII 88 (SCC), [1993] 2 S.C.R. 316, [1993] S.C.J. No. 56, 102 D.L.R. (4th) 402, 153 N.R. 81, J.E. 93-1086, 106 Nfld. & P.E.I.R. 140, 12 Admin. L.R. (2d) 165, 93 CLLC Â14,033 at 12213, 40 A.C.W.S. (3d) 282; Ventas, Inc. v. Sunrise Living Real Estate Investment Trust 2007 ONCA 205 (CanLII), (2007), 85 O.R. (3d) 254, [2007] O.J. No. 10 . 83, 2007 ONCA 205 (CanLII), 2007 ONCA 205, 222 O.A.C. 102, 29 B.L.R. (4th) 312, 56 R.P.R. (4th) 163, 156 A.C.W.S. (3d) 95

Thomas G. Heintzman, Q.C., and Junior Sirivar, for appellant Frank Andrew Dunn.

Bonnie A. Tough and Jennifer Lynch, for appellant Douglas Beatty.

Gary H. Luftspring and Sam R. Sasso, for respondent Chubb Insurance Company of Canada.

Richard H. Krempulec, Q.C., for respondent American Home Assurance Company.

BY THE COURT: -- Overview

[1] These two appeals, heard together, concern the interpretation of provisions in a directors and officers liability insurance policy regarding the allocation of Defence Costs, a defined term in the policy, in proceedings brought against persons insured under the policy. The appellants challenge the decision of Campbell J. (the "application judge"), which dismissed their application for a declaration that the insurer is obligated to pay either 90 or 100 per cent of their Defence Costs. The Defence Costs relate to proceedings brought after the expiry of the policy period and allege conduct occurring both prior to and after the end of the policy period.

[2] At the request of the appellants, these appeals were expedited, and counsel have requested that we deliver our reasons expeditiously.

[3] We have concluded that the insurance policy, as it relates to the allocation of Defence Costs, is ambiguous. The conclusion we have reached results from a submission first made in oral argument on this appeal. Were it not for that submission, we would have dismissed the appeal for the reasons set out below.

[4] However, the current state of the record provides little help in resolving the ambiguity. Moreover, the parties assert different facts, most of which are not in evidence, in arguing for and against the application of the doctrine of contra proferentem. In our view, it is desirable that this important case be decided on a more complete record.

[5] In the result, we have concluded that the preferable course is to order a new hearing of the application. We find this conclusion unfortunate because we are well aware of the urgency from the appellants' point of view of having the issues raised on this appeal resolved one way or the other. However, the delay is necessary to provide the parties with the opportunity to introduce evidence and provide argument that would assist with the resolution of the ambiguity. [page705]

[6] In order to narrow the future proceedings, we have decided all of the issues other than the one giving rise to the ambiguity. We expect that the parties will co-operate with one another in order to achieve a speedy resolution of the outstanding issue. Background

[7] The appellants are Frank Andrew Dunn and Douglas Beatty. Although we recognize that there are a number of insurers listed as respondents, for the purpose of the discussion in these reasons, we refer to the insurers simply as "Chubb" or the "insurers".

[8] The insurance policy in issue (the "2001 Policy") was one of many issued by Chubb to Northern Telecom Limited (now Nortel Networks Corporation). It covered the Policy Period from 1999 to 2001 (the "Policy Period"). The 2001 Policy is a variant of a "claims made" policy.

[9] During the Policy Period, the appellants participated in certain conduct that became the subject of civil proceedings commenced in 2001 and 2002 (the "2001 Proceedings"). Chubb acknowledges that the 2001 Proceedings triggered coverage under the 2001 Policy.

[10] In 2004 and subsequent years, further proceedings were brought against the appellants. These proceedings include civil cases as well as regulatory proceedings by the Ontario Securities Commission and the United States Securities and Exchange Commission. All of these proceedings include allegations against the appellants by reason of their conduct in 2001 (the "2001 Conduct") as well as their conduct in 2003 to 2004 (the "2003 Conduct"). Counsel refer to these 2004 and subsequent civil and regulatory proceedings as the Hybrid Proceedings. All of the Hybrid Proceedings were commenced after the expiration of the Policy Period.

[11] Chubb acknowledges that the 2001 Conduct pleaded in the Hybrid Proceedings triggers coverage under the 2001 Policy because a claim was made regarding the appellants' 2001 Conduct during the Policy Period. Thus, Chubb accepts that it is responsible for 100 per cent of the Defence Costs incurred by the appellants in the Hybrid Proceedings to the extent that those proceedings relate to the 2001 Conduct. However, Chubb takes the position that it is not responsible for the appellants' Defence Costs in the Hybrid Proceedings to the extent that those costs relate exclusively to the appellants' 2003 Conduct. As a result of taking the above position, Chubb has been paying 50 per cent of the appellants' Defence Costs for the Hybrid Proceedings. [page706]

[12] The application judge dismissed the appellants' application for a declaration that Chubb is responsible to pay either 90 or 100 per cent of the Defence Costs relating to the Hybrid Proceedings. Issues

[13] On this appeal, the appellants advance three arguments.

[14] First, they argue that the application judge erred in failing to give effect to the allocation provisions contained in two endorsements to the 2001 Policy, which provide a specific allocation for Defence Costs in the case of claims that include both covered and uncovered matters. The appellants submit that the endorsements are clear on their face and entitle them to either 100 per cent of their Defence Costs for the Hybrid Proceedings (assuming the claims are based on, arising from or in consequence of a "Securities Transaction"), or 90 per cent otherwise.

[15] Second, they argue that the application judge erred in failing to find that the particulars of the 2003 Conduct alleged in the Hybrid Proceedings were "Interrelated Wrongful Acts" with the 2001 Conduct and, as such, were all covered under the terms of the 2001 Policy.

> [16] Third, in the alternative to their first and second arguments, the appellants submit that the application judge erred in holding that the appellants had the burden of proving that a greater proportion than 50 per cent of the Defence Costs was appropriate for coverage under the 2001 Policy. Analysis 1. The allocation provisions issue

[17] Chubb's responsibility for Defence Costs relating to the 2003 Conduct in the Hybrid Proceedings turns on the interpretation of Endorsements 3 and 10 of the 2001 Policy.

[18] Both endorsements became effective on the same date and replaced s. 12 of the 2001 Policy. Section 12 was entitled "Allocation". It provided that if both "Loss covered and loss not covered" were incurred, "because a Claim against the Insured Persons includes both covered and uncovered matters", the parties would use best efforts to agree upon a fair and proper allocation between "covered Loss and uncovered loss" (emphasis in original). Section 12 further provided that if the parties could not agree on an allocation, Chubb would advance Defence Costs that it believed to be covered until a different allocation was negotiated, arbitrated or judicially determined. [page707]

[19] Endorsements 3 and 10 replaced the allocation scheme set out in s. 12 of the 2001 Policy. Both endorsements provide for a fixed percentage allocation of Defence Costs for claims that include both covered and uncovered matters. Endorsement 10 allocates 100 per cent of Defence Costs to covered loss in the case of a claim based on, arising from or in consequence of a "Securities Transaction", as that term is defined in s. 2 of Endorsement 10. Endorsement 3 allocates 90 per cent of Defence Costs to covered matters in the case of claims that do not fall within the definition of a "Securities Transaction".

(a) Ambiguity in Endorsement 3

[20] The relevant part of Endorsement 3 reads as follows:

> If both Loss covered by this coverage section and Loss not covered by this coverage section are incurred, either because a Claim against an Insured Person includes both covered and uncovered matters or because a Claim is made against both an Insured Person and others, including the Insured Organization, the Insureds and the Company shall allocate such amounts as

> follows:
> (a) with respect to Defence Costs, to create certainty in determining a fair and proper allocation of Defence Costs, 90 % of all Defence Costs which must otherwise be allocated as described above shall be allocated to covered Loss and shall be advanced by the Company on a current basis . . . . (Emphasis in original)

[21] The interpretation of Endorsement 3 and its application to the Hybrid Proceedings depends in part on the meaning of the term "Loss". Indeed, Chubb acknowledges that, but for the definition of "Loss" in the 2001 Policy, Endorsement 3 would require Chubb to pay 90 per cent of the appellants' Defence Costs of the Hybrid Proceedings, including those aspects of the proceedings that relate to the 2003 Conduct.

[22] The relevant part of the definition of "Loss" in the 2001 Policy reads as follows:

> [T]he total amount which any Insured Person becomes legally obligated to pay on account of each Claim and for all Claims in each Policy Period and the Extended Reporting Period, if exercised, made against them for Wrongful Acts for which coverage applies, including, but not limited to, damages, judgments, settlements, costs and Defence Costs. (Emphasis in original)

[23] Chubb argues that this definition limits the application of Endorsement 3 to claims made during the Policy Period and does not, therefore, cover claims arising from the 2003 Conduct. Chubb sets out its argument in its factum as follows:
[page708]

> The 90% Allocation Provision is inapplicable to the Hybrid Proceedings because it applies only to Claims first made during the 2001 Policy Period that give rise to Loss covered by the 2001 Policy and loss not covered by the 2001 Policy. None of the Hybrid Proceedings were Claims first made during that policy period.
>
> By its terms, the 90% Allocation Provision applies only "[i]f both Loss covered by this coverage section and Loss not covered by this coverage section are incurred . . . ." Loss is defined to include only those amounts which the Insured is legally obligated to pay "on account of each Claim and for all Claims in each Policy Period and the Extended Reporting Period, if exercised." [See Note 1 below] Amounts incurred defending the Hybrid Proceedings are not amounts Dunn and Beatty are obligated to pay "on account of" a Claim in the 2001 Policy Period because the Hybrid Proceedings are not Claims made during the 2001 Policy Period. Accordingly, the 90% Allocation Provision simply has no application to defence costs incurred in the Hybrid Proceedings. (Italics in original; underlining added)

[24] The appellants respond by arguing that the application of the definition of "Loss" to Endorsement 3 would render Endorsement 3 meaningless. The definition of "Loss" in the 2001 Policy includes only amounts that an insured person becomes legally obligated to pay "for which coverage applies" (emphasis added). Endorsement 3 specifically provides for the allocation of costs in situations where there is a "Loss" for which there is no coverage. Indeed, the whole purpose of Endorsement 3 is to allocate Defence Costs between covered and uncovered losses. Thus, interpreting the contract as Chubb

suggests would mean that there could be no "Loss not covered" and therefore no allocation. The appellants submit that this interpretation would negate the overall purpose of the allocation provision, a result that could not have reflected the intention of the parties. [See Note 2 below]

[25] Chubb acknowledges the difficulty in interpretation that is posed when applying the definition of "Loss" in the 2001 Policy to Endorsement 3. However, it submits that the difficulty could be resolved by removing the words "for which coverage applies" from the definition of "Loss" when interpreting Endorsement 3. Indeed, this is the only solution that Chubb proposes to the interpretation dilemma. Effectively, Chubb is asking the court to amend the definition of "Loss" in the 2001 Policy. [page709]

[26] Chubb points out that the interpretation urged by the appellants would require ignoring a defined term in the 2001 Policy. In this respect, it is interesting to note that the previous allocation provision -- s. 12 of the 2001 Policy -- referred to "Loss covered by this coverage section and loss not covered by this coverage section" and provided an allocation scheme for "covered Loss and uncovered loss" (emphasis in original). Thus, in the original 2001 Policy, the word "loss", as it related to uncovered losses, was neither bolded nor capitalized. Hence, one could read into the term "Loss" in Endorsement 3 some support, if any is needed, for the position that the parties intended the definition of "Loss" to be relied upon when interpreting the allocation provisions.

[27] Chubb argues that the only way the definition makes sense is if it is amended as set out above. The commercial reality, according to Chubb, is that once the parties moved to a fixed allocation for covered and uncovered matters, it made sense to limit the allocation to claims made during the Policy Period. Otherwise, the allocation provision would be open-ended and would cover Defence Costs for claims against an insured brought years after the Policy Period had expired.

> [28] Thus, the parties' positions lead to one of two possible results:
> -- interpret Endorsement 3 without reference to the definition of "Loss" because to do so would render Endorsement 3 meaningless. This would require ignoring the definition of the term "Loss" in Endorsement 3 (the appellants' position); or
> -- interpret Endorsement 3 by referring to the definition of "Loss" but delete from the definition the phrase "for which coverage applies" (Chubb's position).

[29] The result would be either that the appellants are entitled to the 90 per cent allocation under Endorsement 3, [See Note 3 below] or that Endorsement 3 does not apply to that portion of the Hybrid Proceedings relating to the 2003 Conduct because the claims relating to that conduct were not made during the Policy Period as required by the definition of "Loss" in the 2001 Policy. [page710]

[30] In short, we conclude that the meaning of Endorsement 3 when read in conjunction with the definition of "Loss" is ambiguous.

[31] In our view, it is impossible to resolve the ambiguity in this case on the factual record before us. In order to explain our position, it is necessary to review some of the basic principles of contractual interpretation.

[32] The primary goal of contractual interpretation is to give effect to the intentions of the parties. As Estey J. explained in Consolidated-Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co., 1979 CanLII 10 (SCC), [1980] 1 S.C.R. 888, [1979] S.C.J. No. 133, at p. 901 S.C.R., "the normal rules of construction lead a court to search for an interpretation which, from the whole of the contract, would appear to promote or advance the true intent of the parties at the time of entry into the contract".

[33] Where a contract is clear and unambiguous on its face, it is unnecessary to consider extrinsic evidence in order to interpret its terms: Eli Lilly & Co. v. Novopharm Ltd., 1998 CanLII 791 (SCC), [1998] 2 S.C.R. 129, [1998] S.C.J. No. 59, at para. 55; Fraser River Pile & Dredge Ltd. v. Can-Dive Services Ltd., 1999 CanLII 654 (SCC), [1999] 3 S.C.R. 108, [1999] S.C.J. No. 48, at para. 32. Thus, it has been said that courts should give effect to clear and unambiguous language in an insurance policy, having regard to the contract as a whole: Non-Marine Underwriters, Lloyd's of London v. Scalera, 2000 SCC 24 (CanLII), [2000] 1 S.C.R. 551, [2000] S.C.J. No. 26, at para. 71; Brisette Estate v. Westbury Life Insurance Co., 1992 CanLII 32 (SCC), [1992] 3 S.C.R. 87, [1992] S.C.J. No. 86, at p. 92 S.C.R. That being said, the terms of an insurance policy, like all contractual terms, must be examined in light of the surrounding circumstances -- or what is sometimes called the "factual matrix" -- in order to determine the intent of the parties and the scope of t heir understanding: Jesuit Fathers of Upper Canada v. Guardian Insurance Co. of Canada, 2006 SCC 21 (CanLII), [2006] 1 S.C.R. 744, [2006] S.C.J. No. 21, at para. 27.

[34] A contractual provision is ambiguous if it is reasonably susceptible of more than one meaning: Hi-Tech Group Inc. v. Sears Canada Inc. 2001 CanLII 24049 (ON CA), (2001), 52 O.R. (3d) 97, [2001] O.J. No. 33 (C.A.), at para. 18. Extrinsic or parol evidence may be admitted to assist in resolving an ambiguity: United Brotherhood of Carpenters and Joiners of America, Local 579 v. Bradco Construction Ltd., 1993 CanLII 88 (SCC), [1993] 2 S.C.R. 316, [1993] S.C.J. No. 56, at p. 342 S.C.R.; Eli Lilly, at para. 55. For example, extrinsic evidence regarding the negotiations leading up to an agreement may be admitted if the contract is ambiguous, but not if the language of the contract is clear: [page711] see Canadian Premier Holdings Ltd. v. Winterthur Canada Financial Corp., 2000 CanLII 5724 (ON CA), [2000] O.J. No. 1619, 132 O.A.C. 172 (C.A.), at para. 15; SimEx Inc. v. IMAX Corp., [2005] O.J. No. 5389, 206 O.A.C. 3 (C.A.), at para. 23. [See Note 4 below]

[35] Further, where an insurance policy is ambiguous, the court should adopt the interpretation that gives effect to the reasonable expectations or intentions of the parties: Non- Marine Underwriters, at para. 71; Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co., 1993 CanLII 150 (SCC), [1993] 1 S.C.R. 252, [1993] S.C.J. No. 10, at p. 269 S.C.R. As Estey J. explained in Consolidated-Bathurst, at pp. 901-902 S.C.R.:

> [L]iteral meaning should not be applied where to do so would bring about an unrealistic result or a result which would not be contemplated in the commercial atmosphere in which the insurance was contracted. Where words may bear two constructions, the more reasonable one, that which produces a fair result, must certainly be taken as the interpretation which would promote the intention of the parties. Similarly, an interpretation which defeats the intentions of the parties and their objective in entering into the commercial transaction in the first place should be discarded in favour of an

> interpretation of the policy which promotes a sensible commercial result. It is trite to observe that an interpretation of an ambiguous contractual provision which would render the endeavour on the part of the insured to obtain insurance protection nugatory, should be avoided. Said another way, the courts should be loath to support a construction which would either enable the insurer to pocket the premiu m without risk or the insured to achieve a recovery which could neither be sensibly sought nor anticipated at the time of the contract. (Emphasis added)

[36] Finally, if all other rules of construction are inadequate, the doctrine of contra proferentem may be applicable to resolve an ambiguity against the party who drafted the contract. Contra proferentem is a rule of last resort and will only apply "when all other rules of construction fail": Canadian National Railway Co. v. Royal and Sun Alliance Insurance Co. of Canada, 2008 SCC 66 (CanLII), [2008] 3 S.C.R. 453, [2008] S.C.J. No. 67, at para. 33, citing Stevenson v. Reliance Petroleum Ltd., 1956 CanLII 27 (SCC), [1956] S.C.R. 936, [1956] S.C.J. No. 68, at p. 953 S.C.R. [page712]

[37] Without being critical, there is little evidence in the record to assist the court in resolving the interpretation dilemma identified on this appeal. There is virtually no evidence about the context or the factual matrix within which the 2001 Policy or the endorsements were agreed to. While both sides have urged that "commercial realities" support their interpretation, there is little in the record, by way of either facts or argument, to assist the court in assessing the relative commercial practicality of the approaches advocated by each party. [See Note 5 below] Indeed, we can think of benefits and problems with both interpretations depending from whose vantage point the situation is considered.

[38] We do not know whether there is further evidence available that would assist in resolving the ambiguity. However, we do know that the parties take differing positions as to whether the doctrine of contra proferentem is available to assist with the resolution of the ambiguity. Significantly, the difference in the parties' positions results primarily from the different facts that the parties assert relating to the negotiations and the terms of the insurance contract.

[39] The appellants accept that the parties appear to have negotiated the removal of the previous allocation clauses and replaced them with Endorsements 3 and 10. They also accept that there may have been negotiations with respect to the premiums to be paid for the new arrangements. However, the appellants go on to assert that there is no suggestion that Nortel or anyone on behalf of Nortel negotiated any of the contractual language in the body of the standard insurance policy, including the definition of "Loss". Nor is there any evidence that the parties negotiated the specific language used in Endorsements 3 and 10. Thus, the appellants' position is that there may have been negotiations, but those negotiations were limited to the issues of percentages and premiums. The appellants assert that the 2001 Policy is a standard policy, as are each of Endorsements 3 and 10. As such, they argue that the 2001 Policy is a contract of adhesion. They rely on case law, [See Note 6 below] [page713] which, in their submission, stands f or the proposition that the doctrine of contra proferentem applies to contracts of adhesion and that the ambiguity should be resolved against the insurers.

[40] Chubb takes the opposite position. It says that the appellants' arguments on the facts relating to the scope of the negotiations are inappropriate because there is no evidence

about those negotiations. Chubb relies on Canadian [See Note 7 below] and American [See Note 8 below] authorities for the proposition that contra proferentem should not be applied against an insurer where the insured has participated in the negotiations of endorsements to an insurance policy. Chubb also relies upon the passage from the Supreme Court of Canada's decision in Canadian National Railway, at para. 33. There, the court spoke of the doctrine being inapplicable where the entire policy had been negotiated between sophisticated parties and pointed out the difference between a manuscript (or fully negotiated) policy and a policy of adhesion.

[41] The difficulty in both parties' submissions is the lack of evidence necessary to resolve this point. There is virtually no evidence about the negotiations, if any, leading to Endorsements 3 and 10; the definition of Loss in the 2001 Policy or other relevant terms; what matters were covered in the negotiations; the parties involved; or any other information that would assist in determining whether the resulting contract is a policy of adhesion or a manuscript policy.

[42] Whether or not there is further evidence to assist with resolving the ambiguity, it seems obvious that the doctrine of contra proferentem will play an important role in the resolution of the interpretive issue arising from the allocation provisions [page714] in Endorsement 3. Clearly, this is an important issue for these parties. It is also an important issue for other cases where large and sophisticated parties contract for insurance coverage.

[43] In our view, it is undesirable to resolve the ambiguity in this case without providing the parties an opportunity to call evidence regarding the factual matrix of the agreement, as well as extrinsic evidence and evidence that would inform the contra proferentem issue. It is for that reason that we have decided that there must be a new hearing on this issue only.

[44] We wish to stress that the remedy in this case is unusual. As noted, it arises from a submission that was advanced for the first time in oral argument on this appeal and from the parties' different interpretation of facts that were not in evidence. In our view, it would be inappropriate to decide this issue in the absence of a complete factual record that would enable the parties to develop the relevant facts and arguments.
(b) Endorsement 10

[45] The appellants also argue that Chubb is required to pay 100 per cent of their Defence Costs pursuant to Endorsement 10, which as discussed above, provides for a 100 per cent reimbursement for Defence Costs for claims based on, arising from or in consequence of a "Securities Transaction". Section 7 of Endorsement 10 reads as follows:

> The first paragraph of subsection 12, Allocation, is deleted in its entirety and the following is inserted:
> (a) If a Claim based on, arising from or in consequence of a Securities Transaction results in both Loss covered by this coverage section and Loss not covered by this coverage section, because such Claim includes both covered and uncovered matters or is made against both covered and uncovered parties, the Insureds and the

> Company shall allocate such amount to Loss as follows:
> (i) 100% of such amount constitute defense costs shall be allocated to covered Loss; and
> (ii) 100% of such amount other than defense costs shall be allocated to covered Loss. (Emphasis in original)

[46] "Securities Transaction" is defined in s. 2 of Endorsement 10 to mean "the purchase or sale of, or offer to purchase or sell, any securities issued by any Insured Organization" (emphasis in original).

[47] In our view, the allocation process described in Endorsement 10 does not apply to the Hybrid Proceedings. We agree with Chubb's submission that the Hybrid Proceedings are not [page715] "based on, arising from, or in consequence of" the purchase or sale of Nortel securities. Rather, as Chubb argues, the Hybrid Proceedings are based on the appellants' alleged improper accounting treatment of Nortel's revenues and reserves.
(c) Other issues

[48] The appellants also relied on ss. 8 and 10 of the 2001 Policy to counter Chubb's argument that the definition of "Loss" limits Endorsement 3 to allocating losses for covered and uncovered matters to claims made during the Policy Period. In effect, the appellants argue that the 2001 Conduct and the 2003 Conduct are "Interrelated Wrongful Acts" (s. 8) or claims arising from the same circumstances (s. 10). As such, they argue that the Hybrid Proceedings include only claims made during the Policy Period. That being the case, the appellants argue that the definition of "Loss" does not operate to exclude the claims in the Hybrid Proceedings relating to the 2003 Conduct from the operation of Endorsement 3.

[49] We do not accept this argument. For the reasons we set out below in dealing with the appellants' second ground of appeal, we are of the view that the 2001 Conduct and the 2003 Conduct are not "Interrelated Wrongful Acts" and did not arise out of the same circumstances. In our view, they are two separate and distinct sets of conduct.

[50] Finally, before leaving the allocation issue, we point out that an exchange took place between the court and counsel during oral argument with respect to the definition of "Loss". The panel observed that the following sentence appears at the end of the definition of "Loss", as it is reproduced in Appendix A to the application judge's reasons:

> Loss does not include any amount allocated to uncovered loss pursuant to subsection 12, Allocation. (Emphasis in original)

[51] After oral argument, the court's senior legal officer wrote to counsel advising that it appeared that this part of the definition of "Loss" was added by Endorsement 10. [See Note 9 below] Counsel were asked [page716] whether or not they had any submissions as to the applicability of the above sentence to the interpretation of the definition of "Loss" as it applied to Endorsement 3. For different reasons, counsel said that it did not. As a result, we have not taken into consideration the amendment to the definition of "Loss" found in Endorsement 10.

[52] We raise this point at this stage to say that we thought it might be argued that the amendment to the definition of "Loss" forms part of the entire 2001 Policy. If that were the case, it also might be argued that the definition of "Loss", as amended, is consistent with an approach that when Defence Costs are being allocated between covered and uncovered losses, the definition of "Loss" in the 2001 Policy should not be applied to uncovered losses. If that were the case, uncovered losses would not be limited by the requirement in the definition of "Loss" that they be on account of claims made in the Policy Period.

> [53] We do not raise this point at this time to suggest that the amendment to the definition of "Loss" in Endorsement 10 should determine the issue or even that it is relevant to the resolution of the ambiguity. We do so only so that the parties and the court hearing the reapplication may consider whether or not there is any assistance to be gleaned from that amendment. 2. Interrelated wrongful acts

[54] On this ground of appeal, the appellants argue that the 2003 Conduct that is pleaded in the Hybrid Proceedings is covered by the 2001 Policy on two bases.

[55] First, they argue that the 2003 Conduct is the same as, or is interrelated to, the 2001 Conduct on the basis of s. 8 of the 2001 Policy. Section 8 provides coverage for "all Loss arising out of the same Wrongful Act and all Interrelated Wrongful Acts" (emphasis in original). "Wrongful Act" is broadly defined to include the type of conduct at issue in the Hybrid Proceedings, including misleading statements. "Interrelated Wrongful Act" is defined to mean "all causally connected Wrongful Acts" (emphasis in original).

[56] Second, the appellants argue that the 2003 Conduct is conduct that was "subsequently arising from" the 2001 Conduct within the meaning of s. 10 of the 2001 Policy. Section 10 [page717] provides for coverage where a claim after the Policy Period arises from circumstances about which the insured gave notice during the Policy Period.

[57] In essence, these arguments are both based on the premise that the 2003 Conduct arose out of, was causally connected to or was the same as the 2001 Conduct. In support, the appellants point to various broad-based allegations in the Hybrid Proceedings, including the Ontario Securities Commission's allegation that the appellants displayed a "culture of non-compliance" throughout the whole period.

[58] Broad language can usually be chosen to describe a wide variety of allegations of misconduct. However, in our view, a reading of the allegations in the Hybrid Proceedings shows that the 2003 Conduct is different in nature, in kind and in time from the 2001 Conduct alleged in the same proceedings.

[59] The allegations of the 2003 Conduct relate to different acts of non-compliance than the 2001 Conduct and to acts that took place at different time frames and in different ways. The allegations are specific in describing the different acts. For example, the Securities and Exchange Commission proceedings allege that the appellants were involved in two fraudulent accounting schemes, which are explained as comprising a Revenue Recognition scheme based on the 2001 Conduct and a different Provisioning scheme based on the 2003 Conduct. The distinction between the parameters of the

conduct and the two time frames is further illustrated by recent criminal charges which involve allegations restricted to the 2003 Conduct.

[60] Accordingly, we reject this ground of appeal. 3. Larger costs issue

[61] On this ground of appeal, the appellants challenge the application judge's finding that "in the absence of evidence to the contrary", it was reasonable for Chubb to pay them 50 per cent of the Defence Costs of the Hybrid Proceedings in relation to the 2001 Conduct covered under the 2001 Policy. The application judge made this finding because the appellants did not call evidence that the 2001 Conduct consumed more than 50 per cent of the costs of the Hybrid Proceedings.

[62] The appellants argue that the application judge erred in failing to apply the decision of this court in Hanis v. Teevan 2008 ONCA 678 (CanLII), (2008), 92 O.R. (3d) 594, [2008] O.J. No. 3909 (C.A.). They submit, based on Hanis, that Chubb is obliged to pay any defence costs reasonably related to the defence of the 2001 covered [page718] claims, even if those costs also relate to the defence of any 2003 uncovered claims.

[63] This argument is consistent with Hanis, where Doherty J.A. stated, at para. 2, "the insurer is required to pay all reasonable costs associated with the defence of those claims even if those costs further the defence of uncovered claims". However, Doherty J.A. continued to explain, at para. 2, that the insurer "is not obliged to pay costs related solely to the defence of uncovered claims".

[64] In our view, on the state of the current record, and for our reasons relating to the Interrelated Wrongful Act argument, this case appears to be one where the Defence Costs can be separated into costs relating to the 2001 Conduct and costs relating to the 2003 Conduct. This does not appear to be a case where the same costs are being incurred for both covered and uncovered claims: see Hanis, at paras. 25, 42.

[65] Finally, the appellants argue that the onus was on Chubb to establish which Defence Costs relate to the covered claims and which relate to the uncovered claims. On this issue, we agree with the observation of Doherty J.A. in Hanis, at para. 43, that there does not appear to be "any compelling reason to depart from the general rule that the party claiming damages bears the ultimate or legal burden of proof on that issue, including proving the quantum of damages suffered".

[66] The application judge resolved this issue by observing that Chubb, in the absence of evidence to the contrary, had allocated 50 per cent of the Defence Costs to the Policy Period. He left it open to the appellants to demonstrate, to the satisfaction of Chubb or the court, that a greater percentage was appropriate and stated in his reasons that his order could be amended accordingly. We are of the view that in the event that the appellants are ultimately unsuccessful on the allocation provisions issue, the approach taken by the application judge is appropriate.

[67] Thus, we reject this ground of appeal. Disposition

[68] In the result, we allow the appeal and direct a new hearing of the application to be limited in accordance with these reasons. Given the result, we make no order as to the costs of this appeal and leave that issue to the judge rehearing the application. However,

to assist with respect to the amount of the costs to be awarded with respect to the appeal, we fix the costs as follows. [page719]

[69] If the appellants are eventually successful, we would have awarded costs on a partial indemnity basis. The appellants argued in their costs submissions that the insured "is entitled to all his or her costs on a substantial (or full) indemnity basis in an action against an insurer who denies coverage". Substantial indemnity costs may be appropriate in cases where the issue on appeal is whether the insurer had a duty to defend: see M. (E.) v. Reed, [2003] O.J. No. 1791, 49 C.C.L.I. (3d) 57 (C.A.). However, where the issue on appeal involves the allocation of costs between the insurer and the insured, as in this case, costs are awarded on a partial indemnity basis:
see Hanis v. University of Western Ontario, 2008 ONCA 793 (CanLII), [2008] O.J. No. 4706, 2008 ONCA 793; Boliden Ltd. v. Liberty Mutual Insurance Co., 2008 ONCA 418 (CanLII), [2008] O.J. No. 2079, 2008 ONCA 418.

[70] That said, the amount claimed must also be fair and reasonable having regard to the nature of the appeal: see Boucher v. Public Accounts Council for the Province of Ontario 2004 CanLII 14579 (ON CA), (2004), 71 O.R. (3d) 291, [2004] O.J. No. 2634 (C.A.). We would fix the costs for the appellant, Dunn, in the amount of $35,000 and for the appellant, Beatty, in the amount of $15,000. Both amounts are inclusive of disbursements and GST. If an award is to be made in favour of Chubb, we would fix Chubb's costs on a partial indemnity basis in the amount of $35,000, inclusive of disbursements and GST.

Appeal allowed.

Notes

Note 1: The Extended Reporting Period was not exercised and, therefore, is irrelevant.

Note 2: It is important to point out that it does not appear that this issue was addressed before the application judge.

Note 3: Assuming that the claims are not based on, arising from or in consequence of a "Securities Transaction".

Note 4: Regardless of ambiguity, however, as noted above, courts may have regard to the context or the factual matrix. This court has said that commercial contracts are to be interpreted "with regard to objective evidence of the factual matrix underlying the negotiation of the contract, but without reference to the subjective intention of the parties": see Ventas, Inc. v. Sunrise Senior Living Real Estate Investment Trust 2007 ONCA 205 (CanLII), (2007), 85 O.R. (3d) 254, [2007] O.J. No. 1083 (C.A.), at para. 24, citing Eli Lilly, at para. 54, and Kentucky Fried Chicken v. Scott's Food Services Inc., [1998] O.J. No. 4368, 114 O.A.C. 357 (C.A.), at paras. 25-27.

Note 5: Having said this, we note that the application of a standard of commercial reasonableness does not necessarily require the consideration of any evidence, extrinsic or otherwise: see Lauren International, Inc. v. Reichert, 2008 ONCA 382 (CanLII),

[2008] O.J. No. 1891, 237 O.A.C. 94 (C.A.), at para. 23, leave to appeal to S.C.C. refused [2008] S.C.C.A. No. 327.

Note 6: Indemnity Insurance Co. of North America v. Excel Cleaning Service, 1954 CanLII 9 (SCC), [1954] S.C.R. 169, [1954] S.C.J. No. 11; Consolidated-Bathurst; Fletcher v. Manitoba Public Insurance Co., 1990 CanLII 59 (SCC), [1990] 3 S.C.R. 191, [1990] S.C.J. No. 121; Canadian National Railway Co. v. Royal and SunAlliance Insurance Co. of Canada, [2004] O.J. No. 4086, 15 C.C.L.I. (4th) 1 (S.C.J.), revd 2007 ONCA 209 (CanLII), (2007), 85 O.R. (3d) 186, [2007] O.J. No. 1077 (C.A.), revd 2008 SCC 66 (CanLII), [2008] 3 S.C.R. 453, [2008] S.C.J. No. 67.

Note 7: Hillis Oil & Sales v. Wynn's Canada, 1986 CanLII 44 (SCC), [1986] 1 S.C.R. 57, [1986] S.C.J. No. 9; McClelland & Stewart Ltd. v. Mutual Life Assurance Co. of Canada, 1981 CanLII 53 (SCC), [1981] 2 S.C.R. 6, [1981] S.C.J. No. 60; Showmart Management Ltd. v. 853436 Ontario Ltd. (c.o.b. Features Cafe), [1998] O.J. No. 1645, 18 R.P.R. (3d) 128 (Gen. Div.); Canadian Crude Separators Ltd. v. W.A. (Wes) Jacobson, [1998] A.J. No. 787, 226 A.R. 171 (Q.B.).

Note 8: Chubb Custom Ins. Co. v. Prudential Ins. Co. of America, 948 A.2d 1285, 195 N.J. 231 (2008); Six Flags, Inc. v. Westchester Surplus Lines Ins. Co., 565 F.3d 948 (5th Cir. 2009); F.D.I.C. v. Ins. Co. of North America, 105 F.3d 778 (1st Cir. 1997); Eagle Leasing Corp. v. Hartford Fire Ins. Co., 540 F.2d 1257 (5th Cir. 1976); Fountain Powerboat Industries, Inc. v. Reliance Ins. Co., 119 F.Supp.2d 552 (E.D.N.C. 2000).

Note 9: Section 2(c) of Endorsement 10 provides that the definition of Loss is amended by adding the following:

> Loss does not include any amount allocated to uncovered loss pursuant to subsection 12, Allocation. For purposes of coverage under Insuring Clause 3, Loss includes punitive or exemplary damages which any Insured Organization becomes legally obligated to pay, provided the punitive or exemplary damages are otherwise covered under Insuring Clause 3 and are insurable under the law pursuant to which this coverage section is construed.

Tab 3

CITATION: Thomas Cook Canada Inc. v. Skyservice Airlines Inc., 2011 ONSC 5756
COURT FILE NO.: CV-10-8647-00CL
DATE: 20111003

2011 ONSC 5756 (CanLII)

SUPERIOR COURT OF JUSTICE – ONTARIO
COMMERCIAL COURT

IN THE MATTER OF the receivership of Skyservice Airlines Inc.

RE: **THOMAS COOK CANADA INC.**

Applicant

- AND -

SKYSERVICE AIRLINES INC.

Respondent

BEFORE: Newbould J.

COUNSEL: Geoff R. Hall, for the receiver FTI Consulting Canada Inc.

Julie Rosenthal, for Skyservice Investments Inc. and Ron Patmore, in his capacity as Minority Shareholder Representative

HEARD: September 27, 2011

ENDORSEMENT

[1] Skyservice Airlines Inc. ("Skyservice") is in receivership. Prior to the receivership a predecessor of Skyservice was acquired from its then shareholders under a series of corporate transactions which resulted in Skyservice being formed and being entitled to the rights of the purchaser. Those rights are contained in an Arrangement Agreement.

[2] The Arrangement Agreement provided that certain portions of the purchase price were to be held back and placed into escrow. The release of the various holdback amounts were to depend on whether certain financial thresholds were met following the closing of the agreement, which occurred in October 2007. If the thresholds were met, then the holdbacks were to be released to the former shareholders. If the thresholds were not met, then the holdbacks were to be released to the purchaser.

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[3] The relevant thresholds relate to the amount contributed to Skyservice's EBITDA by one of its customers, a tour operator known as Conquest Vacations Inc. Broadly speaking, if Conquest contributed $2 million to Skyservice's EBITDA either during the six months running November 1, 2007 to April 30, 2008, or during the eighteen months running November 1, 2007 to April 30, 2009, then the full $2 million being held in escrow would be released to the former shareholders at the end of the applicable 6 or 18 month periods. If Conquest contributed $1 million but less than $2 million to Skyservice's EBITDA, $1 million would be released to the former shareholders at the end of the applicable period.

Nature of dispute

[4] A dispute arose between the former shareholders and Skyservice regarding the amount contributed by Conquest to Skyservice's EBITDA. This dispute arose before the receiver of Skyservice was appointed. It has not been settled. The interpretation of a provision of the Arrangement Agreement dealing with the method of calculating the EBITDA has been brought into question by the receiver.

[5] The Arrangement Agreement provided for two different mechanisms that were to govern how Conquest's contribution to Skyservice's EBITDA was to be determined. One mechanism was to apply if Skyservice maintained April 30 as its financial year-end (as it had been prior to the closing of the Arrangement Agreement). The other mechanism was to apply if Skyservice did not maintain April 30 as its financial year-end. The two mechanisms are set out in the following clause of the Arrangement Agreement:

> 2.11(e)(viii)
>
> I. the parties agree that the applicable EBITDA contributed by [Conquest's] programs for the applicable period shall be determined based on the audited financial statements of [Skyservice] for such period (excluding interest earned on cash balances as provided in clause (vii) above). If the financial year of Skyservice does not end on April 30th, then the parties agree, acting reasonably, to determine the applicable EBITDA on the basis of internally generated financial statements for the applicable periods and which are reviewed by Skyservice's auditors. Such determinations shall be final and binding on the Parties. ...

[6] Following the acquisition of the business, Skyservice changed the financial year end from April 30. The clause therefore directed the EBITDA to be determined as follows:

> ... then the parties agree, acting reasonably, to determine the applicable EBITDA on the basis of internally generated financial statements for the applicable periods and which are reviewed by [Skyservice's] auditors.

[7] Following the first six-month period ending April 30, 2008, Skyservice authorized the release of $1 million to the former shareholders. Although no explanation was given at that time for the amount of the payment, it indicated that Conquest had contributed at least $1 million but less than $2 million to Skyservice's EBITDA as of April 30, 2008. A few weeks before the April 30 2008 date, Mr. Ciampi of Skyservice had informed a representative of the former shareholders that Conquest had by the end of February 2008 contributed approximately $1.6 million to Skyservice's EBITDA. Based on that information the former shareholders had expected that the $2 million threshold would be reached by April 30, 2008 as the months of March and April had historically been the two biggest months for Conquest's business. Requests over several months from the former shareholders for an explanation went unanswered until March 5, 2009 when Skyservice asserted that Conquest had contributed $1,930,941 to Skyservice's EBITDA for the six months ending April 30, 2008, some $69,000 less than the $2 million threshold.

[8] Because of problems relating to the calculation of the EBITDA contributed by conquest for the period ending April 30, 2009, that figure has never been determined. KPMG, Skyservice's auditor, were engaged to review the interim financial statements. The results of their review have

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not been released by KPMG because of its demand for a release from liability from the former shareholders before doing so, which the former shareholders have refused.

[9] A dispute has arisen as to the importance to be given to KPMG's review. The receiver takes the position that the clause is ambiguous and that no literal reading will lead to a clear result. The receiver asserts that the correct interpretation using accepted principles of interpretation requires the EBITDA to be determined by Skyservice's auditor KPMG. The former shareholders contend that the provision is not ambiguous and that on a proper construction of the provision the EBITDA is to be determined by the agreement of the parties acting reasonably after the auditors have reviewed the internally generated financial statements. What is at issue is whether the remaining $1 million plus interest held in escrow is to be released to the former shareholders or retained by the receiver of Skyservice.

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Principles of interpretation

[10] The principles governing the interpretation of a commercial contract were recently stated in *Ventas, Inc. v. Sunrise Senior Living Real Estate Investment Trust*, 85 O.R. (3d) 254 (C.A.) by Blair J.A. as follows:

> [24] Counsel accept that the application judge correctly outlined the principles of contractual interpretation applicable in the circumstances of this case. I agree. Broadly stated -- without reproducing in full the relevant passages from her reasons (paras. 29-34) in full -- she held that a commercial contract is to be interpreted,
>
> > (a) 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;
> >
> > (b) by determining the intention of the parties in accordance with the language they have used in the written document and based upon the "cardinal presumption" that they have intended what they have said;
> >
> > (c) with regard to objective evidence of the factual matrix underlying the negotiation of the contract, but without reference to the subjective intention of the parties; and (to the extent there is any ambiguity in the contract),

> (d) in a fashion that accords with sound commercial principles and good business sense, and that avoid a commercial absurdity.

[11] This passage was adopted in *Bell Canada v. The Plan Group* (2009), 96 OR (3d) 81 (CA), which also stated:

> ...each word in an agreement is not to be "placed under the interpretative microscope in isolation and given a meaning without regard to the entire document and the nature of the relationship created by the agreement." Courts should not strain to dissect a written agreement into isolated components and then interpret them in a way that – while apparently logical at one level – does not make sense given the overall wording of the document and the relationship of the parties.

[12] In the test for interpreting commercial contracts set out in *Ventas*, the fourth test that the contract is to be interpreted in a fashion that accords with sound commercial principles and good business sense that avoids a commercial absurdity is preceded by a statement in parentheses "to the extent there is any ambiguity in the contract". This suggests that it is only if there is an ambiguity that a commercial contract is to be interpreted in a fashion that accords with sound commercial principles and good business sense and avoids a commercial absurdity. Mr. Hall in his factum states, and I agree with him, that there is some reason to believe that ambiguity may not be a precondition to the consideration of sound commercial principles and that until *Ventas*, a consistent line of authorities held that sound commercial principles should be considered and did not set any precondition of ambiguity. See *Scanlon v. Castlepoint Development Corporation* (1992), 11 OR (3d) 744 (C.A.) at 770 and *Kentucky Fried Chicken v. Scott's Food Services Inc.* (1998), 41 B.L.R. (2d) (C.A.) at para. 27 in which it was stated by Gouge J.A.:

> Where, as here, the document to be construed is a negotiated commercial document, the court should avoid an interpretation that would result in a commercial absurdity. Rather, the document should be construed in accordance with sound commercial principles and good business sense. Care must be taken, however, to do this objectively rather than from the perspective of one contracting party or the other, since what might make good business sense to one party would not necessarily do so for the other.

[13] Mr. Hall says, however, that as there is an ambiguity, whether the words in parentheses in *Ventas* have restricted the use of commercial principles to construe commercial contracts only

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where there is ambiguity is moot. In my view, I rather doubt that *Ventas* intended to make any change in the settled principles for interpreting a commercial contract and I prefer to rely upon the statement of Gouge J.A. in *Kentucky Fried Chicken v. Scott's Food Services Inc.* and use those principles whether or not there is an ambiguity in the clause in question.

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[14] As to the consideration of interpreting the contract with regard to objective evidence of the factual matrix underlying the negotiation of the contract, what the surrounding circumstances are that are to be considered will vary from case to case. In *Kentucky Fried Chicken v. Scott's Food Services Inc,* Goudge J.A. stated:

> 25....While the task of interpretation must begin with the words of the document and their ordinary meaning, the general context that gave birth to the document or its "factual matrix" will also provide the court with useful assistance. In the famous passage in *Reardon Smith Line Ltd. v. Yngvar Hansen-Tangen*, [1976] 1 W.L.R. 989 at 995-96 (H.L.) Lord Wilberforce said this:
>
>> No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of what is legitimate to have regard to is usually described as "the surrounding circumstances" but this phrase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.
>
> 26 The scope of the surrounding circumstances to be considered will vary from case to case but generally will encompass those factors which assist the court "... to search for an interpretation which, from the whole of the contract, would appear to promote or advance the true intent of the parties at the time of entry into the contract." *Consolidated Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co.*, [1980] 1 S.C.R. 888 at 901.

[15] The receiver also relies upon the principle of contract interpretation that where a contract is ambiguous, evidence of the parties' subsequent conduct is admissible as an aid to contractual interpretation. This principle is described in *Montreal Trust Co. of Canada v. Birmingham Lodge Ltd.* (1995), 24 O.R. (3d) 97 (C.A.) at 108. The receiver looks to the subsequent conduct of the parties as confirmatory of its interpretation of the clause in question. The former shareholders

say that if there is an ambiguity and subsequent conduct may be considered, that subsequent conduct assists their interpretation.

Factual matrix

[16] As can be seen, the clause in question clearly directs the determination of EBITDA to be based on audited statements if the year-end did not change after the acquisition from the former shareholders. It does not state that for the situation in which the year-end did change. There is evidence, which can be considered part of the factual matrix, which relates to the reason for the different treatment depending on whether the year-end changed. It is contained in the affidavit of Ronald Patmore, one of the former shareholders. He was involved in the negotiations of the Arrangement Agreement with Mr. Ciampi who represented the purchasers.

[17] The determination of Conquest's contribution to Skyservice's EBITDA was complicated by certain aspects of Skyservice's internal accounting. Skyservice's practice was to set aside over the course of the year internal reserves from money earned through its operations in order to protect itself in the event of various contingencies. At the end of each financial year-end, these internal reserves were reviewed to determine whether they were reasonable. Typically these reserves proved to have been overly conservative and were reversed, the effect of which was to decrease the company's expenses and thus increase its EBITDA. This review process was undertaken at year-end in order to prepare the company's financial statements which were then audited by the company's auditors.

[18] Although the auditors did not undertake a substantive review of the reasonableness of the company's internal reserves, because, among other things, they lacked the necessary knowledge to do so, they did compare those reserves to those shown in the year-end financial statements of previous years. Any material change would lead to questions being asked by the auditors and, depending upon the answers to those questions, the possibility of further audits procedures. Mr. Patmore explained in his affidavit:

> Although the nature of internal reserves is such that they are not particularly amenable to substantive review by a company's auditors, at the financial year-end, the auditors can (and, to the best of my knowledge, do) compare the internal

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> reserves for the year in question to those that were shown on the previous year's audited financial statements. Any material change in the reserves will lead to questions being asked of management as to the justification for the increase or decrease in the reserves and, if needed, further audit procedures. All of the foregoing imposed a fiscal discipline on the preparation of the year-end financial statements... which discipline was specific to the preparation of the year-end statements and which did not apply to the preparation of interim financial statements. Thus, the perhaps natural tendency of a purchaser to determine that the EBITDA thresholds had not been met (and, thereby secure release of the EBITDA tranche to the purchaser) would be counterbalanced by factors such as those discussed above, i.e. the year-end review process, the desire to maximize profits at year-end, and the ability of the auditors to compare year-end internal reserves to those shown on the audited financial statements from previous years.

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[19] Mr. Patmore stated that the determination of whether the April 30 EBITDA thresholds had been reached would be more complicated if, after the closing of the Arrangement Agreement, the company changed its financial year-end. If the financial year-end were no longer April 30, then the former shareholders would no longer have the full and complete picture of the contribution to the EBITDA made by Conquest that would be produced at year-end as a result of the factors that would be taken into account at year-end.

[20] Thus, in the event that the year-end changed, without some provision in the Arrangement Agreement, the former shareholders, who would no longer be involved in the management of the company nor have access to the internally generated interim financial statements, would be in a disadvantageous position when it came to the calculation of the EBITDA contribution made by Conquest for the six-month period ending April 30, 2008 and the further period ending April 30, 2009.

Analysis

[21] For ease of reference, the clause in question provides:

> The parties agree that the applicable EBITDA contributed by [Conquest's] programs for the applicable period shall be determined based on the audited financial statements of [Skyservice] for such period ... If the financial year of [Skyservice] does not end on April 30th, then the parties agree, acting reasonably, to determine the applicable EBITDA on the basis of internally generated financial

> statements for the applicable periods and which are reviewed by [Skyservice's] auditors. Such determinations shall be final and binding on the Parties. ...

[22] The receiver contends that the last sentence, which states that the determinations shall be final and binding on the parties, is inconsistent with the earlier statement that the parties agree, acting reasonably, to determine the applicable EBITDA. Thus there is said to be an ambiguity. It is said that businesspeople prefer certainty and dislike litigation and it would make no commercial sense to say that the parties had to agree between themselves as to the applicable EBITDA as that would only be inviting litigation. The receiver says that the phrase in the clause dealing with the internally generated financial statements which states "which are reviewed by Skyservice's auditors" should be interpreted to mean "which are to be reviewed and determined by Skyservice's auditors". Otherwise, contends the receiver, the last sentence stating that the determination is final and binding on the parties would be meaningless.

[23] One difficulty with this interpretation is that the clause expressly states that the parties, acting reasonably, are to determine the applicable EBITDA, and not that the auditors are to determine it.

[24] The receiver also contends that the clause gave the former shareholders the right to have an input as to what KPMG was to do, which the receiver says later occurred, but were not given the right after KPMG had done its review to say that they had to agree on the EBITDA calculation. What happened after the Amalgamation Agreement took place cannot be considered part of the factual matrix and would only be admissible if there were an ambiguity. In any event, a difficulty with this contention of the receiver is that the clause does not state what the receiver asserts, i.e. does not state that the former shareholders, or Skyservice for that matter, are to have input into what KPMG is to do and are to have no other input, and ignores the express provision that the parties are to determine the applicable EBITDA.

[25] The former shareholders contend that there is no ambiguity and that the last sentence of the clause that states that the determination shall be final and binding on the parties is not inconsistent with the provision that the parties themselves are to determine the EBITDA in the event of a year-end change. They contend that a purpose of the final and binding provision

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would be that if there were a determination after the first six months that there had been an EBITDA contribution by Conquest of $1 million, that determination could not be changed in the following year when considering whether a further $1 million contribution had been made by Conquest. The same comment could be made after a determination of the EBITDA as of April 30, 2009. It would not be open in subsequent years for Skyservice to attempt to make adjustments to the prior year's financial statements for whatever reason, as sometimes occurs, or for the former shareholders to attempt to cause that to be done. Once the money in escrow had been released either to the former shareholders or to Skyservice after a determination of the EBITDA contribution by Conquest, that would be the end of the matter.

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[26] In my view the contention of the former shareholders is correct and that properly interpreted, there is no ambiguity in the clause. There was on an objective basis commercial reason for the difference in the method of determining the EBITDA contribution by Conquest depending on whether the year-end was changed. As a commercial matter, it makes sense to give the former shareholders some assurances regarding the EBITDA calculations that would not be available if the year-end changed and there were no audit undertaken by the auditors as at year-end.

[27] The clause does not state that the auditors are to determine the EBITDA. At most it says that the statements are reviewed by the auditor. The distinction between an accountant providing an audited opinion and undertaking a review engagement is well known. A review engagement is a less detailed engagement that does not result in an audited opinion, and there is no commercial reason to suppose that the former shareholders would agree to have the determination of the EBITDA done on the basis of something less reliable than a full year-end audit by KPMG. I accept the position of the former shareholders that the financial statements as reviewed by KPMG would be used by the parties in their determination of the EBITDA figure.

[28] If the contention of the receiver were accepted, it would mean that the determination of the EBITDA calculation would be made on the basis of internal financial statements prepared by Skyservice without any input from the former shareholders and on the basis of a review by

KPMG, again without any input from the former shareholders. Taken the circumstances existing at the time the agreement was made, this would not appear to be commercially reasonable.

[29] There is no reason to assume that the parties by agreeing to be reasonable were inviting litigation and thus conclude that they could not have intended to require their agreement to the EBITDA calculation.[1]

[30] Thus in my view the clause is not ambiguous and it is possible to interpret it without taking into account any extrinsic evidence. The interpretation that I put on the clause is that it requires the parties, acting reasonably, to jointly determine the Conquest EBITDA figures on the basis of the internally generated financial statements that have been reviewed by Skyservice's auditors.

[31] If there were an ambiguity, a review of what occurred after the Arrangement Agreement was made does not, in my view, lead to the interpretation of the clause contended for by the receiver.

[32] By early May 2009, after it was clear that there was a dispute between the parties regarding the EBITDA calculation, the parties through their solicitors agreed that the internally generated financial statements were to be reviewed by KPMG. A draft engagement letter to be signed by Skyservice and KPMG was prepared by KPMG. A copy was provided by Skyservice to the former shareholders who made a number of changes to the draft, some but not all of which were accepted by KPMG in the next draft. One of the changes proposed by the former shareholders that was not accepted by KPMG was that KPMG was to test various expenses for reasonableness. For some reason unexplained in the evidence, the engagement letter was signed by KPMG but not by Skyservice.

[33] Although the engagement letter was not signed by Skyservice, KPMG undertook a review of the Skyservice internally generated financial statements. The former shareholders had no input in this process.

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[1] I raised with counsel the question of whether the clause could be considered to be an unenforceable agreement to agree. Counsel advised that they were not taking that position and thus it has not been considered.

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[34] In early September the former shareholders learned that KPMG was about to complete its work. They were asked to sign a release in favour of KPMG in order for KPMG to release its report. Ms. Duff-Caron, a solicitor for the former shareholders, requested Skyservice to forward the financial statements for the periods November 1, 2007 to April 30, 2008 and from May 1, 2008 to April 30, 2009 which KPMG had reviewed. She also advised that the former shareholders were not prepared to sign any indemnification in favour of KPMG.

[35] On October 9, 2009 Ms. Duff-Caron wrote to Skyservice and referred to information from Skyservice that KPMG's report was nearing completion. She said that the parties should therefore begin the process contemplated by the clause in question by arranging a meeting to review the internally generated financial statements in order to agree on the applicable EBITDA. On October 16, 2009 Skyservice wrote to Ms. Duff-Caron and reiterated that once a release had been signed by the former shareholders in favour of KPMG, the report would be provided to them along with the internally generated financial statements and that Skyservice would then be prepared to meet to consider any comments or concerns the former shareholders had with respect to the KPMG report, the financial statements or the EBITDA determinations flowing therefrom.

[36] The receiver contends that by requesting a meeting in October 2009 to negotiate the applicable EBITDA, the former shareholders changed their position. The receiver does not assert that the former shareholders had previously agreed that the applicable EBITDA would be determined by KPMG but says that their previous conduct in making suggested changes to the draft KPMG engagement letter was consistent with KPMG having the final word. The receiver says that the former shareholders only changed their position once they had some indication that the KPMG report would not be favourable to their position. I think it a fair inference that by the time of Ms. Duff-Caron's letter of October 9, 2009, the former shareholders had some word that the KPMG report would not assist their position.

[37] I do not accept this position of the receiver that there was a change of position on the part of the former shareholders or that they had agreed at any time after the Arrangement Agreement that KPMG would be the party determining the applicable EBITDA. There is no evidence that the former shareholders so agreed and there is evidence that they understood to the contrary.

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[38] On May 28, 2009, before the first draft KPMG engagement letter was prepared by KPMG, a representative of KPMG e-mailed Skyservice, whose solicitor forwarded it to the solicitors for the former shareholders on June 2, 2009. The KPMG e-mail stated:

> Based on my review of the agreement, it appears that the EBITDA contributed by Conquest's programs for the period from November 1, 2007 to April 30, 2009 shall be determined based on the audited financial statements of Skyservice for the period ended April 30th, unless the financial year end of Skyservice does not end on April 30th, in which case, the parties involved would determine the applicable EBITDA on the basis of internally generated financial statements which are reviewed by Skyservice's auditors. (Underlining added)

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[39] It is thus clear from this e-mail that KPMG understood that the parties would determine the applicable EBITDA rather than KPMG. In passing this e-mail on to the solicitor for the former shareholders, there was no indication that Skyservice thought that KPMG's understanding was incorrect. Thus from the outset before the first KPMG draft engagement letter was circulated, the former shareholders had no reason to question that they and Skyservice would determine the applicable EBITDA rather than KPMG. It is not at all clear that Skyservice later had any different view. The letter from Skyservice of October 16, 2009 to Ms. Duff-Caron said that once an indemnity had been provided by the former shareholders in favour of KPMG, the KPMG report along with the internally generated financial statements would be made available and a meeting could then be held to discuss any concerns regarding the KPMG report, the financial statements or the EBITDA determinations flowing therefrom. This was not a statement that there was no purpose to the meeting because the KPMG report would be the final word.

[40] In summary, even if it were permissible to review evidence of post-agreement conduct of the parties as an aid to the interpretation of the contractual clause in question, in my view that evidence would not assist the receiver. The evidence is more confirmatory of the position taken by the former shareholders as to the meaning of the clause.

Further relief requested by the receiver

[41] In the event that the receiver's interpretation of the clause is not accepted, the receiver requests an order that no claim can be brought against KPMG if the KPMG report is released. The receiver relies upon the inherent jurisdiction of the Court to make such an order.

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[42] In my view I have no jurisdiction to make such an order. Inherent jurisdiction embodies the authority of the courts to control their own process and to administer justice in a regular, orderly and effective manner. While courts in CCAA proceedings and in receivership proceedings make orders establishing a claims bar date which prevents claims from being made by creditors after that date, orders are not made extinguishing claims. In the context of a CCAA proceeding, Blair J.A. stated in *Re: Stelco Inc.* (2005), 75 O.R. (3d) 5 the following in making clear that inherent jurisdiction is not limitless:

> [34] Inherent jurisdiction is a power derived "from the very nature of the court as a superior court of law", permitting the court "to maintain its authority and to prevent its process being obstructed and abused". It embodies the authority of the judiciary to control its own process and the lawyers and other officials connected with the court and its process, in order "to uphold, to protect and to fulfill the judicial function of administering justice according to law in a regular, orderly and effective manner". See I.H. Jacob, "The Inherent Jurisdiction of the Court" (1970) 23 Current Legal Problems 27-28. In Halsbury's Laws of England, 4th ed. (London: LexisNexis UK, 1973 --), vol. 37, at para. 14, the concept is described as follows:
>
>> In sum, it may be said that the inherent jurisdiction of the court is a virile and viable doctrine, and has been defined as being the reserve or fund of powers, a residual source of powers, which the court may draw upon as necessary whenever it is just or equitable to do so, in particularly to ensure the observation of the due process of law, to prevent improper vexation or oppression, to do justice between the parties and to secure a fair trial between them.

[43] In *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 45 C.B.R. (5th) 163 (Ont. C.A.) a plan of compromise and arrangement involving the independently sponsored ABCP market in Canada included provisions releasing third parties from claims that did not involve fraud. The plan was approved by the court. The provision for the third-party releases was not approved under any inherent jurisdiction of the court, but rather under the provisions of the CCAA construed in light of the purpose, objects and scheme of that Act.

[44] Even if I had jurisdiction to make the order sought by the receiver, I would decline to do so. If anything, I would be inclined if KPMG were a party to this motion to order that KPMG deliver the report without obtaining any release from the former shareholders.

[45] The engagement letter prepared by KPMG and signed by it, and apparently acted on by KPMG in doing its work even though Skyservice did not sign it, provided for a release by Skyservice of any claim against KPMG in excess of the fees charged by KPMG. Although KPMG knew that the purpose of its work was to assist in the settlement of a dispute between Skyservice and the former shareholders, it did request any release at that time from the former shareholders. It was only after it had completed its work that KPMG demanded a release from the former shareholders. Although the engagement letter was not signed by Skyservice, it knew that KPMG was acting under it and it is likely that there was a contract between Skyservice and KPMG that required KPMG to deliver its report without any release from the former shareholders.

[46] The former shareholders have not seen the KPMG report or the internal financial statements of Skyservice and have no knowledge of the details of the work performed by KPMG. They have no means of knowing whether they might have any complaint against KPMG arising out of the work done by it.

Conclusion

[47] On the motion of the receiver and cross-motion of the former shareholders for the determination of the proper interpretation of section 2.11 (e)(viii)1 of the Arrangement Agreement, it is declared that the section requires the former shareholders and Skyservice, acting reasonably, to determine the amount contributed by Conquest to Skyservice's EBITDA on the basis of the internally generated financial statements that have been reviewed by Skyservice's auditors and that any report of Skyservice's auditors is not binding on Skyservice or the former shareholders.

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[48] The motion by the receiver for an order barring the former shareholders from commencing any action against KPMG arising from any work performed by KPMG in connection with the Conquest EBITDA figures is dismissed.

[49] The former shareholders are entitled to their costs. If costs cannot be agreed brief written submissions of the former shareholders along with a proper cost outline may be made within 10 days and brief written submissions of the receiver in response may be made within a further 10 days.

Newbould J.

DATE: October 3, 2011

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Tab 4

CanLII

Montreal Trust Co. of Canada v. Birmingham Lodge Ltd., 1995 CanLII 438 (ON CA)

Date: 1995-06-02

Docket: c18926

Parallel citations: 24 OR (3d) 97; 125 DLR (4th) 193; 21 BLR (2d) 165; 82 OAC 25; OJ No 1609

URL: http://canlii.ca/t/1g2m2

Citation: Montreal Trust Co. of Canada v. Birmingham Lodge Ltd., 1995 CanLII 438 (ON CA), <http://canlii.ca/t/1g2m2> retrieved on 2014-01-31

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Montreal Trust Company of Canada v. Birmingham Lodge Limited et al.
[Indexed as: Montreal Trust Co. of Canada v. Birmingham Lodge Ltd.]

24 O.R. (3d) 97
[1995] O.J. No. 1609
File No. C18926

Court of Appeal for Ontario,
Brooke, Robins and Laskin JJ.A.
June 2, 1995

Contracts -- Interpretation -- Two reasonable interpretations -- Subsequent conduct after signing agreement may be considered in interpreting agreement.

Guarantee and suretyship -- Interpretation -- Guarantor agreeing to remain liable despite variation of terms of loan, if variation made between lender and successor of borrower -- Distinction between successor and assign -- Guarantor not agreeing to be bound by variation made between lender and assign of borrower -- Guarantor discharged where variation made by assign and not successor of borrower.

Guarantee and suretyship -- Interpretation -- Guarantor agreeing that as between guarantor and lender, the guarantor to be considered as primarily liable -- Classification of nature of liability by parties not determinative -- Review of entire guarantee and subsequent conduct establishing that parties intended that guarantor's liability to be as a guarantor and not as one primary liability -- Guarantor discharged by material variation of terms of loan agreement.

In 1986, the appellants guaranteed payment of a $1,325,000 debenture granted by the corporation of which they were officers, directors, and shareholders to the respondent as lender. In the debenture, the appellants were described as the "Guarantors"; their guarantee of payment was binding upon "their heirs, executors, administrators and assigns"; and the guarantee was made to the lender's "successors and assigns". The guarantee stated that, as between the "Guarantors and the Lender the Guarantors shall be considered as primarily liable". The Guarantee stated that:

. . . nor any variation in or departure from the provisions of this Debenture nor any other dealings between the Corporation or any successor and Lender including any variation or increase of the interest rate, nor any release of the Corporation or any other thing whatsoever whereby the Guarantors as sureties only would or might have been released shall in any way modify, alter, vary or in any way prejudice the Lender or affect the liability of the Guarantors in any way under this covenant . . .

Following the execution of the debenture, the mortgaged property was sold with the appellants' consent and then without their consent. The terms of the mortgage were varied three times without the appellants' consent. The variations were by renewal agreements with the purchaser of the mortgaged property, two of which renewals increased the interest rate and the third which lowered it. The debenture went into default, and, in an action to enforce the guarantee, the respondent moved for summary judgment. The appellants' defence was that they had been discharged because the terms of the debenture had been varied without their consent. They argued that the provision in the debenture allowing variations applied to variations with a successor of the borrower but not to variations made with an "assign" of the borrower. The motions court judge held there was no distinction between successor and assign and granted judgment. The judgment was appealed.

Held, the appeal should be allowed with costs.

There is a distinction between successors and assigns. A purchaser of the mortgaged assets is one to whom an assignment is made, not someone who takes title through legal succession. The debenture used the phrase "successors and assigns" in several provisions, but in the provision permitting variations, the word "assigns" was conspicuously absent. The interpretation of the guarantee was that the appellants agreed that their liability as guarantors would be unaffected if the respondent and a successor of the Corporation extended the term of the mortgage or increased the interest rate. They did not agree, however, that their liability would be unaffected if the respondent and an assign of the Corporation varied these terms without their consent. The appellants did not contract out of the rule by which they would be discharged for material variations made without their consent.

The respondent's argument that the appellants were nevertheless liable as principal debtors did not succeed. The language labelling a party as primarily liable is not determinative. The court must examine the entire document to ascertain the parties' intention. If the court is uncertain about the correct interpretation, it may resort to extrinsic evidence, including the parties' subsequent conduct. In the immediate case, the parties intended the appellants to be guarantors. They were referred to as guarantors throughout the debenture. They signed the debenture as guarantors. Their subsequent conduct resolved any doubt. The subsequent documentation referred to the appellants as guarantors. All three renewal offers and both sale agreements called for the appellants' consent, which indicated that the respondent recognized that without such consent the appellants as guarantors would no longer be liable.

APPEAL from a summary judgment enforcing a guarantee.

Cases referred to Arthur Andersen Inc. v. Toronto-Dominion Bank 1994 CanLII 729 (ON CA), (1994), 17 O.R. (3d) 363, 14 B.L.R. (2d) 1 (C.A.) [leave to appeal to S.C.C. refused (1994), 19 O.R. (3d) xvi, 16 B.L.R. (2d) 254n]; Bank of Montreal v. University of Saskatchewan (1953), 9 W.W.R. (N.S.) 193 (Sask. Q.B.); Brown Brothers Motor Lease Canada Ltd. v. Ganapathi (1982), 139 D.L.R. (2d) 227, 18 B.L.R. 229 (B.C.S.C.); Canadian National Railways v. Canadian Pacific Ltd. 1979 CanLII 2132 (ON SC), (1979), 105 D.L.R. (3d) 170, [1979] 6 W.W.R. 96 (S.C.C.), affg 95 D.L.R. (3d) 242, [1979] 1 W.W.R. 358 (B.C.C.A.); Communities Economic Development Fund v. Canadian Pickles Corp., 1991 CanLII 48 (SCC), [1991] 3 S.C.R. 388, 85 D.L.R. (4th) 88, 76 Man. R. (2d) 1, 131 N.R. 81, 10 W.A.C. 1, [1992] 1 W.W.R. 193, 8 C.B.R. (3d) 121; First City Trust Co. v. 122637 Developments Ltd. (1989), 8 R.P.R. (2d) 155, 79 Sask. R. 175 (Q.B.); Heald v. O'Connor, [1971] 1 W.L.R. 497, [1971] 2 All E.R. 1105, 115 Sol. Jo. 244 (Q.B.D.); Holme v. Brunskill (1878), 3 Q.B.D. 495, 47 L.J.Q.B. 610, 38 L.T. 838, 42 J.P. 757 (C.A.); Manulife Bank of Canada v. Conlin 1994 CanLII 1357 (ON CA), (1994), 20 O.R. (3d) 499, 120 D.L.R. (4th) 234, 17 B.L.R. (2d) 143, 41 R.P.R. (2d) 283 (C.A.), leave to appeal to S.C.C. granted May 4, 1995; Morguard Trust Co. v. Heritage Horizons Ltd. 1987 CanLII 2836 (BC SC), (1987), 36 B.L.R. 16, 44 R.P.R. 135 (B.C.S.C.); National Trust Co. v. Mead, 1990 CanLII 73 (SCC), [1990] 2 S.C.R. 410, 71 D.L.R. (4th) 488, 87 Sask. R. 161, 112 N.R. 1, 1990 CanLII 73 (SCC), [1990] 5 W.W.R. 459, 12 R.P.R. (2d) 165; Walter E. Heller Financial Corp. v. Timber Rock Enterprises Ltd. 1982 CanLII 747 (BC SC), (1982), 40 B.C.L.R. 85 (S.C.) Statutes referred to Limitation of Civil Rights Act, R.S.S. 1978, c. L-16 Mortgages Act, R.S.O. 1990, c. M.40, s. 20(2) Authorities referred to Black's Law Dictionary, 6th ed. (1990), pp. 118, 1431 Waddams, The Law of Contracts, 3rd ed. (1993), para. 323

Andrew M. Robinson, for appellant, Norman N. Warner.

No one appearing for appellant, Paul Martin.

Howard Swartz and Natalie Marconi, for respondent.

The judgment of the court was delivered by

LASKIN J.A.: -- The appellants, Norman Warner and Paul Martin, guaranteed payment of any money owing on a mortgage between the lender, Wellington Trust Company, now the respondent Montreal Trust Company of Canada, and the borrower, Birmingham

Lodge Ltd. (the "Corporation"). The terms of the mortgage were subsequently varied without the appellants' consent. The issue on this appeal is whether these variations released the appellants from liability. This issue has been litigated in this court many times. Like the previous cases, this appeal turns on the intention of the parties and the interpretation of the guarantee. The motions court judge found the appellants liable and granted summary judgment against them. This is an appeal from his judgment.

A. The Facts

The Corporation owned a residential retirement home and apartment complex in Mount Forest, Ontario. The appellants Warner and Martin were the officers, directors and shareholders of the Corporation.

Under the terms of a registered debenture dated January 13, 1986, Wellington Trust Company loaned the Corporation $1,325,000 for three years at an interest rate of 12 per cent per annum. The Corporation agreed to make monthly payments and to pay the balance of the loan on February 1, 1989. On default in payment the loan would immediately become due and payable at the option of the respondent.

The loan was secured by a first mortgage on the Corporation's property and chattels and the Corporation agreed that it would not sell, assign or transfer the property without the written approval of the respondent. The appellants agreed to guarantee the Corporation's mortgage payments. Article 10.1 of the debenture provides for the appellants' guarantee. It states that variations in the terms of the mortgage made by the Corporation or any successor do not affect the appellants' liability. The relevant parts of art. 10.1 are as follows:

> 10.1 IN CONSIDERATION of the premises and of the Lender advancing the said money to the Corporation, PAUL MARTIN and NORMAN M. WARNER (the "Guarantors") do hereby absolutely and unconditionally jointly and severally guarantee to the Lender, its successors and assigns, the due and punctual payment by the Corporation of all principal monies, interest and other monies owing on the security of this Debenture, and the Guarantors for themselves, their heirs, executors, administrators and assigns, covenant with the Lender that if the Corporation shall at any time make default in the punctual payment of any monies payable hereunder, they will pay all such monies to the Lender without any demand being required to be made.
>
> AND IT IS HEREBY EXPRESSED that although as between the Guarantors and the Corporation, the Guarantors are only sureties for the payment by the Corporation of the monies hereby guaranteed, yet as between the Guarantors and the Lender the Guarantors shall be considered as primarily liable therefor and that no release or releases of any portion or portions of the Secured Property, and no indulgence shown by the Lender in respect of any default by the Corporation or any successor which may arise under this Debenture, and that no extension or extensions granted by the Lender to the Corporation or any successor for payment of the monies hereby secured or for the doing, observing or performing of any covenant, agreement, matter or thing herein contained, to be done, observed or performed by the Corporation or any successor nor any variation in or departure from the provisions of this Debenture nor any other dealings between the Corporation or any successor and Lender including any variation or increase of the interest rate, nor any release of the Corporation or any other thing whatsoever whereby

> the Guarantors as sureties only would or might have been released shall in any way modify, alter, vary or in any way prejudice the Lender or affect the liability of the Guarantors in any way under this covenant, which shall continue and be binding on the Guarantors, and as well after as before default and after as before maturity of this Debenture, until the said monies are fully paid and satisfied. In the event of an increase in the interest rate, the liability of the Guarantors would continue to include the increased interest rate for which the Guarantors would be considered as primarily liable therefor. And it is hereby further expressly declared that the Lender shall not be bound to exhaust its recourse against the Corporation or the Secured Property before being entitled to payment from the Guarantors of the amount hereby guaranteed by the Guarantors.
>
> . . . . .
>
> ALL COVENANTS, liabilities and obligations entered into or imposed hereunder upon the Guarantors shall be equally binding upon their heirs, executors, administrators and assigns.
>
> THE LENDER may vary any agreement or arrangement with the Guarantors and grant extensions of time to or otherwise deal with them, their heirs, executors, administrators and assigns, without any consent on the part of the Corporation.

(Emphasis added)

The appellants rely on the repeated use of the phrase "the Corporation or any successor" in the second clause of art. 10.1 (the "no prejudice clause"). They argue that they did not agree to remain liable on their guarantee for variations in the terms of the mortgage made by the respondent and an assign of the Corporation.

Following the execution of the debenture, the mortgaged property was transferred twice and the terms of the mortgage were varied three times. The material facts concerning these five transactions are as follows:

(i) By an agreement dated November 1986, the Corporation sold the property and chattels to 672069 Ontario Inc.
("672069"). The respondent consented to the sale. 672069 assumed liability for the mortgage debt "as principal debtor and not as surety". The appellants, described as "original guarantors", were parties to this agreement. They agreed that the covenant in their original guarantee would remain in effect "notwithstanding the entering into of this agreement". Compleat Health Corporation
("Compleat"), described as the "new guarantor", also agreed to guarantee the debt. The Corporation and each appellant signed this agreement.

(ii) By an agreement dated February 1, 1989, 672069, the respondent and Compleat agreed to renew the mortgage for one year from March 1, 1989, to February 1, 1990, at a new interest rate of 12.75 per cent per annum. The respondent offered this renewal on condition "that the consent of all existing guarantors shall be obtained to the renewal of the mortgage". The appellants -- again described as original guarantors -- were shown as parties to the renewal agreement but they did not consent to the renewal and they did not sign the agreement.

(iii) On April 4, 1990, the respondent wrote to Compleat offering to renew the mortgage for another year at a rate of 13.25 per cent per annum. The respondent's offer to renew was conditional on "receipt of acceptance of renewal offer signed by all mortgagors and guarantors". Compleat and 672069 accepted the offer and the mortgage was renewed. Neither the Corporation nor the appellants, however, signed the offer. The Corporation was dissolved on August 14, 1989; and the appellants said that they had no knowledge of this or any other transaction involving the mortgage loan after the Corporation sold the property in 1986.

(iv) By an assumption agreement dated August 1990, Vanguard Leisure Lodges Limited ("Vanguard") acquired the property and chattels from 672069. The respondent approved the sale and the parties agreed that Vanguard would become the principal debtor and that 672069 and Compleat would continue to be responsible jointly and severally with Vanguard for the loan secured under the debenture. The agreement as drafted provided for its execution by the Corporation, and by the appellants (who are again referred to as original guarantors), but neither the Corporation nor the appellants signed the agreement. Instead, a line was drawn through their names and a line was also drawn through the clause in the agreement that recited that the appellants' covenants were to "remain in full force and effect".

(v) On March 25, 1991, the respondent wrote to Vanguard offering to renew the mortgage for another year, this time at an interest rate of 11.5 per cent per annum. Again the offer to renew was conditional on "receipt and acceptance of renewal offer signed by all Mortgagors and Guarantors". Although Vanguard accepted the offer, again, neither the Corporation nor the appellants signed it.

In summary, the appellants consented to the sale to 672069 in 1986. They did not consent to the subsequent sale to Vanguard and they did not consent to the two renewal agreements that increased the interest rate, or, for that matter, to the last renewal agreement that lowered the rate.

The debenture went into default on January 1, 1992. The respondent appointed a receiver-manager to operate the retirement home on January 31, 1992. It issued a notice of sale under mortgage in February 1992 and served the notice on the appellants. The respondent commenced this action on April 6, 1992, and brought its motion for summary judgment on April 12, 1992. The motions court judge granted judgment for the respondent for $1,440,931.13, the amount owing on the mortgage, and ordered the appellants to deliver possession of the property to the respondent.

The appellants submit that they were relieved from liability on their covenant on the following four grounds:

(i) The terms of the mortgage were varied without their consent.

(ii) This court's judgment in Manulife Bank of Canada v. Conlin 1994 CanLII 1357 (ON CA), (1994), 20 O.R. (3d) 499, 120 D.L.R. (4th) 234 (C.A.), leave to appeal to the Supreme Court of Canada granted May 4, 1995.

(iii) Section 20(2) of the Mortgages Act, R.S.O. 1990, c. M.40.

(iv) Novation.

Counsel agreed that we could deal with the first three submissions by summary judgment. I propose to address only the appellants' first submission because in my opinion it is decisive of this appeal.

B. Did the Variations in the Terms of the Mortgage Release the Appellants from Liability?

The legal principles governing the liability of a guarantor are well-established. Robins J.A. set them out succinctly in his dissenting judgment in Manulife Bank of Canada v. Conlin, supra, at pp. 502-03:

> The general rule is that the surety will be discharged if the principal contract which he guaranteed is varied or altered without his consent in a material way not necessarily beneficial to him. The scope of this rule, which has become known as the rule in Holme v. Brunskill, was stated in that case (1878), 3 Q.B.D. 495 at pp. 505-06, 47 L.J.Q.B. 610 (C.A.), as follows:
>
>> The true rule . . . is, that if there is any agreement between the principals with reference to the contract guaranteed, the surety ought to be consulted, and that if he has not consented to the alteration, although in cases where it is without inquiry evident that the alteration is unsubstantial, or that it cannot be otherwise than beneficial to the surety, the surety may not be discharged; yet, that if it is not self-evident that the alteration is unsubstantial, or one which cannot be prejudicial to the surety, the Court will . . . hold that in such a case the surety himself must be the sole judge whether or not he will consent to remain liable notwithstanding the alteration, and that if he has not so consented he will be discharged.

It follows that a change in the interest rate payable on a guaranteed obligation may discharge the surety from liability as may an extension of time within which the principal obligor is to pay or perform the guaranteed obligation. Changes of this nature have been held to materially alter the basis on which a surety agreed to become liable under a guarantee and therefore to release him from liability: see Holland-Canada Mortgage Co. v. Hutchings, 1936 CanLII 20 (SCC), [1936] S.C.R. 165, [1936] 2 D.L.R. 481.

However, a guarantor will not be released if such changes are provided for under the terms of the guarantee or are otherwise within the contemplation of the contract. It is open to parties to a guarantee to make their own arrangements modifying or excluding the rights and defences to which a surety is entitled in law or in equity. This was made clear by the Supreme Court of Canada in Bank of Montreal v. Bauer, 1980 CanLII 12 (SCC), [1980] 2 S.C.R. 102 at p. 107, 110 D.L.R. (3d) 424. Whether in any given case involving changes of the type we are concerned with here the creditor can be said to have effectively reserved its rights against the guarantor or, conversely, whether the guarantor can be said to have contracted out of the defences afforded him by the law is essentially a matter of interpretation. The determination of whether the changes were in fact authorized or contemplated will depend on the construction to be given the contract and the intention of the parties as evidenced by the transaction viewed as a whole: see

> Communities Economic Development Fund v. Canadian Pickles Corp., 1991 CanLII 48 (SCC), [1991] 3 S.C.R. 388, 85 D.L.R. (4th) 88 . . .

In this case the appellants agreed that if the Corporation or a successor varied the interest rate or extended the time for payment, they would remain liable on their guarantee. They submit, however, that they did not agree to remain liable if an assign of the Corporation varied the terms of the mortgage without their consent. They argue that when 672069 entered into the renewal agreements of February 1, 1989, and April 4, 1990, with the respondent, it did so as an assign of the Corporation, not a successor. Since each renewal agreement extended the time for payment and increased the interest rate, the appellants submit that they are released from liability. The motions court judge dismissed this argument holding that "the distinction between 'successor' and 'assign' is spurious". I respectfully disagree. There is a valid distinction between the two terms. Wilson J. discussed this distinction in National Trust Co. v. Mead, 1990 CanLII 73 (SCC), [1990] 2 S.C.R. 410 at p. 423, 71 D.L.R. (4th) 488 at pp. 497-98:

> Turning to s. 40(2) of the Act, the provision states that if a corporation waives its protection, that waiver binds all successors and assigns "notwithstanding anything in this Act." When used in reference to corporations, a "successor" generally denotes another corporation which, through merger, amalgamation or some other type of legal succession, assumes the burdens and becomes vested with the rights of the first corporation. . . .
>
> The word "assign" has, of course, a broader meaning. An "assign" is anyone to whom an assignment is made and presumably, but for the specific reference to "successors", would include both individuals and corporations. As between mortgagors, an assignment would be an agreement between the original mortgagor and his purchaser by which the latter would assume the mortgage debt in exchange for valuable consideration.

The definition of "successor" and "assign" that Wilson J. used are taken from Black's Law Dictionary (see, e.g., 6th ed. (1990), at pp. 118 and 1431.) She used them to assist her in interpreting a section of the Saskatchewan Limitation of Civil Rights Act, R.S.S. 1978, c. L-16. I think that they also assist in construing the appellants' guarantee.

672069 purchased the Corporation's property and chattels. The respondent submits that a purchaser of the assets of the Corporation is a successor of the Corporation. But these definitions suggest otherwise. A purchaser is "anyone to whom an assignment is made", not someone who takes title through legal succession. Therefore 672069 was an assign of the Corporation, not a successor.

In art. 10.1 the appellants agreed that their liability as guarantors would be unaffected if the respondent and a successor of the Corporation extended the term of the mortgage or increased the interest rate. They did not agree, however, that their liability would be unaffected if the respondent and an assign of the Corporation varied these terms without their consent. Undoubtedly the parties intended to make this distinction because the appellants were officers, directors and shareholders of the Corporation. The usual phrase "successors and assigns" appears in several places in the debenture, including in the opening clause of art. 10.1 in reference to the lender. But in the no prejudice clause, which refers to the appellants' liability if the terms of the mortgage are varied, the phrase

"the Corporation or any successor" is used and it is used four times. The word assign is conspicuously absent. The appellants did not contract out of the rule in Holme v. Brunskill (1878), 3 Q.B.D. 495, 47 L.J.Q.B. 610 (C.A.), for material variations made without their consent by the respondent and an assign of the Corporation. In my opinion, this is the only reasonable interpretation of art. 10.1. I therefore conclude that the renewal agreement of February 1, 1989, which was an agreement between the respondent and an assign of the Corporation, and which materially varied the terms of the mortgage, released the appellants from liability as guarantors.

The respondent advances two other arguments to support the judgment under appeal. It submits that even if the appellants are not liable as guarantors, they are still liable as primary debtors. The no prejudice clause of art. 10.1 does state that "as between the Guarantors and the Lender the Guarantors shall be considered as primarily liable therefor". As Robins J.A. noted in Manulife Bank of Canada v. Conlin, supra, lenders often include a provision in their guarantee documents purporting to make guarantors liable as principal debtors. Lenders often have considerable leverage in the negotiation of guarantee arrangements and, not surprisingly, strive to cast a wide net to prevent guarantors escaping liability because of some unforeseen event. Nevertheless, a provision such as "the guarantors shall be considered as primarily liable" does not automatically convert a contract of guarantee into a contract of indemnity. In Communities Economic Development Fund v. Canadian Pickles Corp., 1991 CanLII 48 (SCC), [1991] 3 S.C.R. 388 at pp. 413-14, 85 D.L.R. (4th) 88 at p. 106, Iacobucci J. wrote:

> Contracts of guarantee are sometimes distinguished from contracts of indemnity. In a contract of indemnity, the indemnifier assumes a primary obligation to repay the debt, and is liable regardless of the liability of the principal debtor. An indemnifier will accordingly be liable even if the principal debt is void or otherwise unenforceable. The distinction between contracts of guarantee and of indemnity ought not to be overemphasized. The resolution of a given case will turn on the correct interpretation of the contract and of the intention of the parties; attempts to label the contract as one of guarantee or of indemnity may be less than helpful.

Iacobucci J. referred with approval to the English decision of Heald v. O'Connor, [1971] 1 W.L.R. 497, [1971] 2 All E.R. 1105 (Q.B.D.). In that case the clause in question provided "that the liability hereunder of the guarantor shall be as a primary obligor and not merely as surety and shall not be impaired or discharged by reason of any time or other indulgence granted by the registered holder". Despite this language, Fisher J. wrote at p. 503:

> In the present case, the instrument was given pursuant to clause 7 of the agreement which calls for a personal guarantee. The word "guarantee" is used in it time and again. The obligation is to pay the principal moneys to become due under the debenture if and whenever the company makes default. The statement of claim refers to it as a guarantee and pleads the company's default and the consequent liability of the guarantor. The only straw for the plaintiff to clutch is the phrase "as a primary obligor and not merely as a surety" but that, in my judgment, is merely part of the common form of provision to avoid the consequences of giving time or indulgence to the principal debtor and cannot convert what is in reality a guarantee into an indemnity.

Two British Columbia judgments have taken the same view of a similar clause in a guarantee document. In Brown Brothers Motor Lease Canada Ltd. v. Ganapathi 1982 CanLII 289 (BC SC), (1982), 18 B.L.R. 229 at pp. 235-36, 139 D.L.R. (3d) 227 (S.C.), Locke J. stated:

> The clause has given me much trouble but I adopt the view of Wilde C.J. and say that even the very specific words "I shall be and shall be deemed to be a principal debtor and not a surety . . ." were not intended to alter the basic intention of the parties, i.e., that Ganapathi was intended to be a guarantor alone.
>
> Among other reasons, if he was ever intended to be the principal debtor, I do not see why he was not so named as a co-debtor in the body of the agreement, nor do I see the need for any guarantee at all. . . .
>
> . . . . .
>
> I think the overriding intention was always that Ganapathi be merely a guarantor. Once an overriding intention or circumstance is found, in my view the principle expressed by Davey J.A. (later C.J.B.C.) in Sawley Agency Ltd v. Ginter flex, (1966), 57 W.W.R. 561, 58 D.L.R. (2d) 757 applies, in words approved by the Supreme Court of Canada 1967 CanLII 75 (SCC), [1967] S.C.R. 451, 60 W.W.R. 701, 62 D.L.R. (2d) 768n. When interpreting an ambiguous clause he said [at p. 563 W.W.R.]:
>
> > . . . That circumstance, in my opinion, dominates the clause and controls its meaning. . . .
>
> In the result, I think the circumstance of guarantee dominates and was intended to dominate this entire document, and in particular cl. 25, and the clause should be so construed.

(Emphasis in original)

And in Walter E. Heller Financial Corp. v. Timber Rock Enterprises Ltd. 1982 CanLII 747 (BC SC), (1982), 40 B.C.L.R. 85 (S.C.), Mackoff J. concluded that a provision in which the defendants "covenant with the mortgagee as principal debtors and not as sureties" conflicted with "the rest of the clause constituting the defendants as guarantors". He held that the defendants were guarantors, not principals. In his view (p. 89):

> If the defendants were intended to be principal debtors it would have been very simple to name them as such in the agreement rather than to refer to them as guarantors throughout.

Other cases have produced the opposite result. For example, in Morguard Trust Co. v. Heritage Horizons Ltd. 1987 CanLII 2836 (BC SC), (1987), 36 B.L.R. 16, 44 R.P.R. 135 (B.C.S.C.), Boyd L.J.S.C. held that a clause in a mortgage in which the guarantor "joins in all covenants with the mortgagee severally as well as jointly" and agrees that he "shall be and be deemed to be a principal debtor and not merely a surety" made the guarantor

primarily liable. Justice Boyd distinguished the Walter E. Heller case because of the different language in each mortgage document. He concluded at p. 27 that:

> . . . in construing the document, it is not sufficient to simply identify contradictory wording and to construe the document as against the interests of the creditor. Rather, the Court's inquiry is always aimed at giving effect to that part of the document which is calculated to carry into effect the real intention of the parties.

See also First City Trust Co. v. 122637 Developments Ltd. (1989), 8 R.P.R. (2d) 155 at pp. 166-67, 79 Sask. R. 175 (Q.B.).

All these cases turn on the specific language of the document being considered. The mere inclusion of a phrase such as "the guarantors shall be considered as primarily liable" is not determinative. The court should examine the entire document to ascertain the parties' intention. If the court is uncertain about the correct interpretation it may resort to extrinsic evidence to assist it.

In this case I would not give effect to the respondent's submission that the appellants are liable as principal debtors. In my view the parties intended that the appellants would be liable only as guarantors. They are referred to as guarantors throughout the debenture. They signed the debenture as guarantors. I therefore construe art. 10.1 of the debenture as a contract of guarantee.

Moreover, I think that the respondent's subsequent conduct resolves any doubt about the extent of the appellants' liability under art. 10.1. Subsequent conduct may be used to interpret a written agreement because "it may be helpful in showing what meaning the parties attached to the document after its execution, and this in turn may suggest that they took the same view at the earlier date": S.M. Waddams, The Law of Contracts, 3rd ed. (1993), at para. 323. Often, as Thomson J. wrote in Bank of Montreal v. University of Saskatchewan (1953), 9 W.W.R. (N.S.) 193 at p. 199 (Sask. Q.B.): "there is no better way of determining what the parties intended than to look to what they did under it".

Lambert J.A. discussed the relevance of subsequent conduct in Canadian National Railways v. Canadian Pacific Ltd., Iflex, [1979] 1 W.W.R. 358 at p. 372, 95 D.L.R. (3d) 242 (B.C.C.A.), affirmed 1979 CanLII 2132 (ON SC), (1979), 105 D.L.R. (3d) 170, [1979] 6 W.W.R. 96 (S.C.C.):

> In Canada the rule with respect to subsequent conduct is that, if, after considering the agreement itself, including the particular words used in their immediate context and in the context of the agreement as a whole, there remain two reasonable alternative interpretations, then certain additional evidence may be both admitted and taken to have legal relevance if that additional evidence will help to determine which of the two reasonable alternative interpretations is the correct one. It certainly makes no difference to the law in this respect if the continuing existence of two reasonable alternative interpretations after an examination of the agreement as a whole is described as doubt or an ambiguity or as uncertainty or as difficulty of construction.

See also Arthur Andersen Inc. v. Toronto-Dominion Bank 1994 CanLII 729 (ON CA), (1994), 17 O.R. (3d) 363 at p. 372, 14 B.L.R. (2d) 1 (C.A.).

In each of its mortgage renewal offers the respondent referred to the appellants only as guarantors, not as primary debtors. Even in its statement of claim in this litigation the respondent sued the appellants as guarantors. It did not allege in its pleading that the appellants were liable as principal debtors.

All three renewal offers and both sale agreements call for the appellants' consent. Eventually the respondent agreed to the sale to Vanguard and to each renewal without obtaining the appellants' consent. Nevertheless I infer that in making the appellants' consent a term of each transaction, the respondent recognized that without such consent the appellants would no longer be liable. Had the appellants been liable as primary debtors under art. 10.1, their consent to the subsequent transactions affecting the property would have been unnecessary. Had the appellants been liable as guarantors under the no prejudice clause, their consent would also have been unnecessary.

The conduct of the respondent after the debenture was executed is entirely consistent with interpreting art. 10.1 as a guarantee, not an indemnity and with limiting the appellants' liability for material variations made without their consent to those made by the respondent and a successor of the Corporation.

The respondent also relies on art. 10.6 of the debenture, which provides:

> 10.6 Everything contained herein shall enure to the benefit of and be binding upon the respective, heirs, executors, administrators, successors and assigns of the Lender, and the Corporation.

This provision -- which parenthetically uses the phrase "successors and assigns" again in reference to the lender -- does not affect the appellants' liability. In my view it does not assist the respondent.

I would allow the appeal, set aside the judgment below and in its place grant judgment dismissing the action against the appellants Warner and Martin. Both appellants are entitled to their party and party costs of the motion and the appellant Warner is entitled to his costs of this appeal. Finally, I wish to record my appreciation to counsel for a well -argued appeal.

Appeal allowed.

Tab 5

Allen-Vanguard Corporation (Re), 2011 ONSC 5017 (CanLII)

Date:	2011-08-25
Docket:	CV-09-00008502-00CL
URL:	http://canlii.ca/t/fn0h5
Citation:	Allen-Vanguard Corporation (Re), 2011 ONSC 5017 (CanLII), <http://canlii.ca/t/fn0h5> retrieved on 2014-01-31
Print:	PDF Format
Noteup:	Search for decisions citing this decision
Reflex Record	Related decisions, legislation cited and decisions cited

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Citation: Allen-Vanguard Corporation (Re), 2011 ONSC 5017
Court File No. CV-09-00008502-00CL
Date: 20110825

ONTARIO
SUPERIOR COURT OF JUSTICE
(Commercial List)

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF ARRANGEMENT AND REORGANIZATION OF **ALLEN-VANGUARD CORPORATION** UNDER THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED AND SECTION 186 OF THE *ONTARIO BUSINESS CORPORATIONS ACT.*, R.S.O. 1990, c.B.16, AS AMENDED

Applicants

Ronald G. Slaght, Q.C., Eli S. Lederman for the Directors and Officers of Allen-Vanguard Corporation
C. Scott Ritchie, Michael G. Robb, Daniel E.H. Bach for class action plaintiffs
Alan L.W. D'Silva, Daniel S. Murdoch for Underwriters

Heard: November 16, 2010

C. CAMPBELL J.:

REASONS FOR DECISION

[1] Two motions were heard together: the first by former directors and officers of Allen-Vanguard to enforce the terms of a Sanction Order, which the directors and officers say release them as well as Allen-Vanguard from all claims except those specifically provided for insection 5.1 (2) of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (the "CCAA.") In addition, the former directors assert that the claims of the Plaintiffs in two proposed Class Actions are not sustainable against them in law under s. 5 .1 (2) of the CCAA.

[2] The second motion by the Underwriters of Allen-Vanguard seeks to dismiss or stay the action brought against the Underwriters by shareholders in a proposed Class Action.

[3] A cross-motion brought by Plaintiffs in the two proposed Class Actions seeks, if required, variation of the terms contained in the Sanction Order granted December 16, 2009, to permit the Class Actions to proceed.

[4] By way of an endorsement dated February 9, 2011,the Court sought further information from the parties with respect to the factual circumstances that surrounded the agreement that was embodied in the terms of the Sanction Order. That information has been provided and will be referred to later in these Reasons.

[5] The claims that the directors who are the moving parties seek to effectively enjoin are those brought in two Class Actions (hereinafter the "Laneville action" and the "Love action"), wherein former shareholders seek damages against directors, officers and Underwriters based on alleged misrepresentation to shareholders by the Defendants about the effect on Allen-Vanguard of its purchase of another company in 2007.

Background

[6] As of December 2009, Allen-Vanguard was insolvent. An Application was made on December 9 for an Initial Order under the CCAA, appointment of a Monitor and a Plan Filing and Meeting Order. The effect of the Initial Order among other matters stayed the existing Class proceeding.

[7] The circumstances that surrounded the Plan Filing/Meeting Order, the Court was advised, were necessary to avoid a bankruptcy. The subsequent vote on December 9, 2010 was approved in favour of the Plan by 100% of affected creditors.

[8] The circumstances that surrounded the December 9, 2010 Application and Order were a variation on a CCAA process that has come to be known as a "pre-packaged" Application. The secured creditors agreed to a restructuring of their secured debt in circumstances involving a going concern sale of assets where, had a bankruptcy ensued, there would have been no recovery for creditors or shareholders beyond very incomplete recovery for those secured creditors.

[9] The First Report of the then proposed Monitor, Deloiite and Touche, in support of the Initial Order, outlined the transaction that had been proposed to all creditors as early as September 2009, posted on SEDAR and to which (apart from the question of releases) no party was opposed on December 9.

[10] The Plan provided for the Secured Lenders foregoing a portion of their existing debt and fees, converting the remainder of the existing debt into a multi-year restructured term loan with terms more favourable to the Company and a new revolving credit facility.

[11] The Court accepted the opinion of Deloitte & Touche that without the proposed transaction, the Company would likely not be able to meet its financial obligations as they became due and would likely be unable to carry on the business beyond the very short-term, which would then necessitate liquidation.

[12] The conclusion by Deloitte & Touche, accepted by the Court, was that the restructuring process in the Plan maximized the value of the Company for the benefit of all stakeholders and represented the best offer from that process.

[13] The alternative faced by the Company was that of a forced liquidation, which as estimated by the Monitor would result in a shortfall to secured lenders in excess of $100 million.

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The Laneville Action

[14] The proposed Class Action Plaintiff in the Laneville action issued on October 9, 2009 a Statement of Claim dated November 26, 2009, which sought appointment on behalf of a Representative Plaintiff and for a class of Allen-Vanguard shareholders who allege that Allen-Vanguard Corporation and its directors and officers are liable for various misrepresentations, negligence and oppression.

[15] The Statement of Claim detailed a transaction that occurred in 2007 for which the Class Plaintiffs claim the directors and officers failed to properly value and account for in the financial statements of Allen-Vanguard, when Allen-Vanguard purchased all of the shares of a private corporation called Mid-Eng Systems Inc.

[16] In addition, the Class Plaintiff claims damages for negligent misrepresentation not only under the common law but as well under s. 138.3 of the *Ontario Securities Act* in connection with the same transaction.

[17] The only creditor objection to the Plan taken at the time of the Initial Order was from counsel for the Proposed Class Plaintiff in the Laneville action, who sought an adjournment of the vote based on the wording of the proposed release terms.

[18] The adjournment of the vote was not granted given the financial fragility of Allen-Vanguard, and the sanction hearing, which was to deal with the wording of the proposed release terms, was set for December 16, 2009.

[19] The Second Report of the Monitor, dated December 10, 2010, advised the Court of the terms of the release and injunctions that had been negotiated, the terms of which were put forward for approval on an unopposed basis. No objection was taken at the sanction hearing by counsel for the Class Plaintiff and no amendment to the Release portion of the Sanction Order sought. Whatever had been negotiated between the parties came before the Court on an unopposed basis. Counsel for the

Class Action Plaintiffs and for the Defendant directors had input into and agreed to the wording.

[20] The Court has been advised that by agreement of counsel, the wording of the Release was negotiated by the parties with the recognition that there would likely remain an issue on which the Court would have to rule. That issue is now the subject of the first motion and the cross motion. I have been advised as a result of the inquiry of February 9, 2011 and what is now obvious as a result of the recent correspondence (including an affidavit sworn June 30, 2011 and objected to) is that Plaintiffs' counsel in the Laneville action and counsel for the directors had quite different views in respect of the kinds of claims that could be included in s. 5.1(2).

[21] As I now understand it, counsel for the Allen-Vanguard Corporation made no representation or agreement that the claims in the Laneville action were within those permitted by s. 5.1(2) of the CCAA.

[22] Counsel for the Plaintiff in the Laneville action believe that the language in the Sanction Order preserves the claims in both the Laneville action and the Love action, including the claims against the Underwriters. It is submitted by the Plaintiff that the jurisprudence in respect of s. 5.1(2) permits not only claims against directors but as well officers to the extent there is insurance coverage, and that the Plaintiffs' position is consistent with the jurisprudence under s. 5.1(2).

[23] Counsel for the Directors and for Underwriters submit that counsel for the Plaintiff knew or ought to have known at the time they agreed to the language of the Plan of Arrangement and the draft Sanction Order that the claims asserted against the Directors and Officers of Allen-Vanguard might nevertheless fail to meet one of the exceptions set out in s. 5.1(2) of the CCAA.

[24] In the result, the issue of what was or was not agreed to as part of the Sanction Order comes down to the question of whether or not the wording of s. 5.1 (2) of the CCAA, read in context of statutory interpretation, is sufficient to permit continuance of claims in the Laneville and Love actions.

[25] As reported by the Monitor in the First Report, the Plan contemplated two releases: a General Release and an Equity Claims Release, both of which had been contemplated in the proposed Plan. Neither the Equity Claims Release nor the General Release was intended to release or deal with or affect in any respect claims under ss. 5.1(1), (2) and (3) of the CCAA, which read:

> 5.1 (1) a compromise or arrangement made in respect of a debtor company may include in its terms provision for the compromise of claims against directors of the company that arose before the commencement of proceedings under this Act and that relate to the obligations of the company where the directors are by law liable in their capacity as directors for the payment of such obligations.
>
> 5.1 (2) A provision for the compromise of claims against directors may not include claims that
>
> (a) relate to contractual rights of one or more creditors; or
>
> (b) are based on allegations of misrepresentations made by directors to creditors or of wrongful or oppressed conduct of directors.
>
> 5.1 (3) the court may declare that a claim against directors shall not be compromised if it is satisfied that the compromise would not be fair and reasonable in the circumstances.

[26] The Monitor in its Second Report remarked as follows:

28. The injunctions provided in the Plan are limited by section 5.1 (2) of the CCAA. The injunctions barring any person from commencing, continuing or pursuing any proceeding on or after the Effective Time for a claim that such person may have against the Company or any current or former officer of the Company of the type referred to in subsection 5.1 (2) of the CCAA... but permit any such subsection 5.1 (2) claim to proceed against a current or former director of the company except that any such claim against a current or former director of the company is permitted recourse, and sole recourse, to the Company's insurance policies in respect of its current and former directors. The estimated value of any coverage under such insurance is $30 million as per the Luxton Affidavit.

29. The Monitor is aware of at least one group of stakeholders affected and by the Supplemental Injunction, being a group of current and former shareholders of the Company that have served a Notice of Action and Statement of Claim on the Company seeking approximately $80 million in damages from the Company and its directors and officers, as further described in the monitors First Report. As stated above the terms of the Supplemental Injunction would permit this claim to survive against the current and former directors of the Company with recourse limited to the Companies insurance as referenced above."

[27] The Releases and Sanctions are contained in the language of the Sanction Order. A summary of the provisions with paragraph references to the Sanction Order is as follows:

22. Releases are essential to the Plan

23. All Persons give full release to each of the Released Parties including contribution and indemnity but directors not released in respect of any claim of the kind referred to in section 5 . 1 (2) of the CCAA.

24. Release of Applicant and current and former directors provided that nothing therein releases a director or current or former officer in respect of any claim of the kind referred to in section 5 .1 (2) of the CCAA.

25. All Persons enjoined and estopped from commencing or continuing actions with the exception of any claim against the directors of the kind referred to in section 5 .1 (2) of the CCAA..

26. Injunction and bar with respect to section 5 .1 (2) against the applicant... and that the sole recourse for any claims against a current or former director or officer of the Applicant Limited to any recoveries from the Applicants insurance policies in respect of current or former directors and officers

27. Laneville Action dismissed as against the Applicant without prejudice to discovery rights against representative of the Applicant.

The Love Action

[28] On February 8, 2010, after the Sanction Order had been made, another Proposed Representative Plaintiff, Gordon Love, commenced a second action and is represented by the same counsel as in the Laneville action. The Statement of Claim, dated March 10, 2010 against the directors and officers of Allen-Vanguard Corporation, includes claims against Cannacord Financial Ltd (and others collectively referred to as "Underwriters.")

[29] An Amended Statement of Claim dated August 10, 2010 asserts in the Love action claims for negligence against directors, officers and Underwriters, all arising out of the transaction and alleged failure to properly disclose the transaction in the

financial statements and transaction referred to in paragraph 15 above in respect of a 2007 acquisition.

Issues

1. Do the Laneville action and the Love action and their proposed class claims fall within those claims non-exempt under s. 5.1(2) of the CCAA?
2. Does the language of the Release contained in the Sanction Order apart from s. 5.1(2) permit either the Laneville or Love actions, including that against Underwriters, to continue?
3. Is there any basis on which the Court could or should vary the terms of the Release section of the Sanction Order?

[30] Having reviewed the language of the Releases contained in the Sanction Order, I am satisfied that the only basis that the release language permits claims as against the directors is if they are those contemplated in s. 5.1(2) of the CCAA not to be released.

[31] The object of the CCAA is to facilitate the restructuring of an insolvent corporation. In order to effect restructuring, a compromise of creditors' claims is almost inevitably an essential ingredient of a Plan under the CCAA.

[32] The Plan, to be effective and to obtain Court approval, requires consensus and agreement by various classes of creditors. Many of the issues that arise before a Plan is approved by the Court involve a contestation between creditor groups as to how they should be classified and what extent of what group approval should be appropriately required. No motion was brought to seek to lift the stay in respect of actions provided for in the Initial Order.

[33] In this case, no creditor came forward to oppose approval of the Plan, including the terms of the release language as set out in the Sanction Order. The effect of a Sanction Order is to create a contract between creditors. (See *Canadian Red Cross Society* (2002), 35. C.B.R. (4th) 43 (Ont. S.C.J.).

[34] The most significant feature of the CCAA Applications that have come before the Court in the last two or three years is that the negotiation has taken place to achieve consensus among creditors often before the Initial Order under the statute.

[35] One can rightly understand the reluctance on the part of a provider of interim financing to continue to do so on an indefinite basis, when the approval process may be dragged out for days, weeks or months.

[36] All secured creditors whose security continues to deteriorate during the period of negotiation will seek an early determination of the consensus necessary for approval of a Plan; otherwise, liquidation may be preferable.

[37] Such consensus requires agreement among many stakeholders, including not just creditors but as well current and former directors and officers, many of whose continued cooperation is necessary and integral to a Plan's success.

[38] To avoid the inequity that would result from creditor claims that were outstanding as against directors at the time of a CCAA application, s. 5.1(2) was amended in 1997 to its present form. As Hart J. noted in *Re-Liberty Oil & Gas Ltd.* 2002 ABQB 949 (CanLII), 2002 ABQB 949 at paragraph 4, before the enactment of

this section, the legislation provided for compromises of claims only against the petitioning company. The new section extends relief against directors of the petitioning company subject to exceptions.

[39] It is appropriate to approach statutory interpretation with the assumption that meaning is to be accorded to each of the words used in the provision within the overall purpose of the CCAA. The absence of other words can also be purposeful.

[40] The CCAA has been said to be a skeletal statute designed to give flexibility and expediency in the ability of the company, with the concurrence of its creditors, to accomplish a restructuring of its debt in the avoidance of liquidation or bankruptcy, and does not contain a comprehensive code that lays out all that is permitted or barred. (See *ATB Financial v. Metcalfe & Mansfield Alternative Investments11 Corp.*, 2008 ONCA 587 (CanLII), 2008 ONCA 587 per Blair J.A para. 44.)

[41] Since the hearing in this matter, the Supreme Court of Canada has rendered a decision in *Century Services Inc. v. Canada (Attorney General)* 2010 SCC 60 (CanLII), 2010 SCC 60, which endorses the broad principles of the CCAA and the discretion granted to the Court to effect a restructuring if possible or an orderly liquidation.

[42] The case involved a contest between the deemed trust provisions of the *Excise Tax Act* and the CCAA. Madam Justice Deschamps, speaking for the majority, noted the need for clarity of the underlying purpose with respect to the CCAA.

[43] Paragraphs 12 to 14, 17, 58-59 and 63 of that decision read as follows:

> 12. Insolvency is the factual situation that arises when a debtor is unable to pay creditors (see generally, R. J. Wood, *Bankruptcy and Insolvency Law* (2009), at p. 16). Certain legal proceedings become available upon insolvency, which typically allow a debtor to obtain a court order staying its creditors' enforcement actions and attempt to obtain a binding compromise with creditors to adjust the payment conditions to something more realistic. Alternatively, the debtor's assets may be liquidated and debts paid from the proceeds according to statutory priority rules. The former is usually referred to as reorganization or restructuring while the latter is termed liquidation.
>
> 13. Canadian commercial insolvency law is not codified in one exhaustive statute. Instead, Parliament has enacted multiple insolvency statutes, the main one being the *BIA*. The *BIA* offers a self-contained legal regime providing for both reorganization and liquidation. Although bankruptcy legislation has a long history, the *BIA*itself is a fairly recent statute — it was enacted in 1992. It is characterized by a rules-based approach to proceedings. The *BIA* is available to insolvent debtors owing $1000 or more, regardless of whether they are natural or legal persons. It contains mechanisms for debtors to make proposals to their creditors for the adjustment of debts. If a proposal fails, the *BIA* contains a bridge to bankruptcy whereby the debtor's assets are liquidated and the proceeds paid to creditors in accordance with the statutory scheme of distribution.
>
> 14. Access to the *CCAA* is more restrictive. A debtor must be a company with liabilities in excess of $5 million. Unlike the *BIA*, the *CCAA* contains no provisions for liquidation of a debtor's assets if reorganization fails. There are three ways of exiting *CCAA* proceedings. The best outcome is achieved when the stay of proceedings provides the debtor with some breathing space during which solvency is restored and the *CCAA* process terminates without reorganization being needed. The second most desirable outcome occurs when the debtor's compromise or arrangement is accepted by its creditors and the reorganized company emerges from the *CCAA*proceedings as a going concern. Lastly, if the

compromise or arrangement fails, either the company or its creditors usually seek to have the debtor's assets liquidated under the applicable provisions of the *BIA* or to place the debtor into receivership. As discussed in greater detail below, the key difference between the reorganization regimes under the *BIA* and the *CCAA* is that the latter offers a more flexible mechanism with greater judicial discretion, making it more responsive to complex reorganizations.

...

17. Parliament understood when adopting the *CCAA*that liquidation of an insolvent company was harmful for most of those it affected — notably creditors and employees — and that a workout which allowed the company to survive was optimal (Sarra, *Creditor Rights*, at pp. 13-15).

...

58. *CCAA* decisions are often based on discretionary grants of jurisdiction. The incremental exercise of judicial discretion in commercial courts under conditions one practitioner aptly describes as "the hothouse of real-time litigation" has been the primary method by which the *CCAA* has been adapted and has evolved to meet contemporary business and social needs (see Jones, at p. 484).

59. Judicial discretion must of course be exercised in furtherance of the *CCAA*'s purposes. The remedial purpose I referred to in the historical overview of the Act is recognized over and over again in the jurisprudence. To cite one early example:

> The legislation is remedial in the purest sense in that it provides a means whereby the devastating social and economic effects of bankruptcy or creditor initiated termination of ongoing business operations can be avoided while a court-supervised attempt to reorganize the financial affairs of the debtor company is made.
> *Elan Corp. v. Comiskey* reflex, reflex, (1990), 41 O.A.C. 282, at para. 57, *per* Doherty J.A., dissenting.)

...

63. Judicial innovation during *CCAA* proceedings has not been without controversy. At least two questions it raises are directly relevant to the case at bar: (1) what are the sources of a court's authority during *CCAA* proceedings? (2) what are the limits of this authority?

[44] I have quoted from the above decision at length to stress the nature of the discretion that is inherent in the CCAA statute to allow the Court to fashion a structure or process to best benefit stakeholders. Consistent with that purpose and as a matter of statutory interpretation, it is appropriate to look at the interpretation of s. 5.1(1) and (2) of the CCAA. Section 5.1 (1) deals with "obligations of the company where the directors are by law liable in their capacity as directors for the payment of such obligations."

[45] A Plan can therefore provide for the compromise of claims against directors where a director may in law be liable for the payment of a company's obligation with the exceptions set out in s. 5.1(2).

[46] In my view, the best that can be said of s. 5 is that it is not as clearly drafted as it might have been.

[47] It is noteworthy that in the first line of s. 5.1(2), the only claims that may not be excluded in a compromise are those against "directors." Claims that can be excluded in a compromise include those against "officers" and the "company" itself. Why is this the case? One reason undoubtedly is the personal liability that directors face under both Federal and Provincial legislation, or the personal undertaking of a director to a creditor such as a personal guarantee. (See *C.I.T. Financial v Lambert*2005 BCSC 1779 (CanLII), 2005 BCSC 1779.)

[48] By way of example, s. 131 (1) of the OBCA provides that directors are made personally liable for unpaid wages of the corporation's employees to a maximum of six months. Reading through s. 5.1 (1)and (2), there is nothing in the wording that would prevent the compromise of such claims against officers or the company itself, but not as against directors. The CCAA does not contain a definition of the word "creditor" but does of the terms "secured creditor," "unsecured creditor" and "shareholder." It would seem that for the purposes of the CCAA and in particular s. 5.1 (2), a creditor would include both a secured creditor and an unsecured creditor, but would not include a shareholder.

[49] Section 5.1(2) refers only to creditors and not shareholders as prospective claimants, whether in contract, tort or statutory oppression.

[50] In this case, the claims by the Class Action Plaintiffs are on behalf of shareholders against directors, since the effect of the CCAA stayed the action against the company Allen-Vanguard. The claims arise with respect to a 2007 transaction and the pre-filing financial statements, but the claims do not involve officers or the company, only directors.

[51] While framed in negligence, the claims in these actions seek to involve the remedy of oppression under the OBCA to enlist the broad scope of remedy possible under that statute. However, it is only in respect of unpaid obligations of the company and other contract-type claims where the law imposes liability on the Defendant directors that invokes the exception in s. 5.1 (2). It is noteworthy that the word "negligence" does not appear in the section at all.

[52] In their essence, the claims in the two actions allege a failure on the part of the directors in 2007 and the company to enter into a provident transaction and the transaction represented a misrepresentation to shareholders of the value of the transaction causing a reduction in shareholder value. Such claims are not of the same kind as those contemplated in section 5.1 (1). They do not relate to "obligations of the company where the directors are by law liable."

[53] The claims relate to transactions that were well in advance of the Initial CCAA Order. In *Re Canadian Airlines Corp.* 2000 ABQB 442 (CanLII), 2000 ABQB 442 (leave refused to ABCA and to SCC), it was held that claims against the directors should only be released if they arose prior to the date of the CCAA proceeding.

[54] I agree that the oppression remedy is expansive in scope and empowers the Court to make determinations and orders that can have a direct and even a radical impact on the internal management and status of a corporation, including even an order winding up the corporation. (See *820099 Ontario Inc. v. Harold E. Ballard Ltd.* flex, (1991), 3 B.L.R. (2nd) 113 (Ont. Div. Ct.) and *Incorporated Broadcasters Ltd. v. CanWest Global*2001 CanLII 28395 (ON SC), 2001 CanLII 28395 (ON S.C.) at paragraphs 101-105.) Oppression as it occurs within s. 5.1(2) of the CCAA must be read within the context of the section itself.

[55] The claims in the Love and Laneville actions are in negligence and no other remedy is sought apart from a claim for damages and access to whatever insurance may be available to respond to claims against directors and officers. There is nothing before the Court to suggest that the insurers, assuming there is a valid policy, are aware of the restriction on remedy.

[56] I see no basis from the pleadings in this action for which it would be appropriate to consider the scope of relief that might otherwise apply under the oppression remedy section of the OBCA. Counsel for the Plaintiffs in the Proposed Class Actions cannot bolster their position by limiting recovery to the applicable Directors and Officers Insurance, when there is no basis for the claim at all, either under the language of the Release or the meaning to be accorded to s. 5.1 (2).

[57] In *BCE Inc. v. 1976 Debentureholders*,2008 SCC 69 (CanLII), [2008] 3 S.C.R. 560, the Supreme Court of Canada commented on the expectations of stakeholders including but not limited to shareholders, in considering a Plan of Arrangement in the context of an oppression claim. Part of the test for"oppression" referred to in that decision is an expectation on the part of the claimant to be "treated in a certain way and that failure to meet the expectation involved unfair conduct."

[58] I fail to understand how the expectation of one or more shareholder groups can be any different with respect to the impugned transaction than those of creditors or indeed the company itself vis-à-vis the directors, particularly since neither the officers nor the company itself is pursued.

[59] The Sanction Order in this case by its terms provided release of the claims now sought to be pursued. By the terms of the Sanction Order, the only reasonable expectation of stakeholders would be that unless specifically authorized by the Order, any claim against directors would be barred. Potential claims against directors were not assigned to class plaintiffs nor was direction sought by any party about the effect of s. 5.1 prior to the issuance of the Order. Given the issue now before the Court and the disagreement of the parties, perhaps the better practice would have been to advise the Court of the issue and "carve" it out of the Plan.

[60] The Court is put in a difficult position when asked in a very constrained timeframe to approve the restructuring with releases. It should certainly not be the expectation that in every instance, releases of the type here should be granted as a matter of course. Those with unpaid obligations of the company may assert that directors are liable if they fail to fulfill the company's obligation when they are legally bound to do so.

[61] I am of the view that third-party releases in particular should be the exception rather than the rule. There may very well be instances in which the releases are not integral or necessary to the restructuring and should not be approved. That was not suggested in the approval process here. There was no evidence presented at the time of the granting of the Sanction Order to suggest that directors were not important to the restructuring. Indeed, the only evidence before the Court was to the contrary: that the directors were integral to the Plan's success.

[62] In this case, the putative Plaintiffs did not oppose the granting of the Sanction Order and in effect took their chances that the Order might after the fact permit the limited claim referred to in the Monitor's Report.

[63] All of the other stakeholders, including the secured creditors, directors, officers and the Applicant Company, approved the form of Order.

[64] It is certainly speculative at this time to consider, had the form of Order proposed been objected to, to what extent the Court would have any jurisdiction to grant the language now sought by the Plaintiffs, without rejecting the Plan entirely.

[65] The duty of directors is first and foremost to the company itself. The oppression remedy does not in my view permit one group (shareholders) to claim oppression when other stakeholders, for example employees or creditors or indeed the company itself, have allegedly suffered a loss that results in insolvency and are unable to seek redress and still preserve restructuring.

[66] To vary or amend the Sanction Order now to permit the claims to continue might at the very least require the presence and concurrence of all of those who supported the form of Order in the first place.

[67] Counsel for the proposed Plaintiffs refer to several decisions, which they urged support the proposition that shareholder actions for oppression against directors are permitted under s. 5.1 (2) of the CCCA.

[68] Each of those decisions, while fact-specific, in my view is consistent with a narrow range of actions warranted for a shareholder against the director under the exception to s. 5.1 (2).

[69] In *Re-Liberty Oil & Gas Ltd.*, 2002 ABQB 949 (CanLII), 2002 ABQB 949, where the action did proceed, the allegation involved a personal representation, indeed a fraudulent one, by the defendant director to two individuals who happened to be shareholders. The complained acts were not those of the company (as here), but rather personal and direct as between the director and shareholder. In other words, there was the proximity that one would expect in a tort situation.

[70] In *Worldwide Pork Corp.*, 2009 SK QB 414, the action was not permitted to proceed. At paragraphs 14 and15 Justice Dawson said:

> It must be remembered that the oppression remedy is not designed to settle every dispute of a corporation but only those that involve and abuse of the corporate system and for which a common-law remedy does not exist.
>
> As well, the plaintiffs have pled that their claim is for damages, for loss of profits and loss of pay out dividends. There must be a causal connection between the alleged oppresive conduct and the loss claimed to be suffered by the plaintiffs. That is, there must be a causal nexus between the alleged conduct and the loss suffered by the plaintiffs. There is no pleading which sets out how the alleged loss of profit or dividends resulted from the conduct alleged to be oppressive. But in any event the losses claimed are losses as a result of Worldwide Pork not being profitable, that is, being unable to provide a return to shareholders for their investment. Such a loss cannot support an action for oppression since it comes with in the exception contained in section 5.1 (2) (b.) of the CCAA.

[71] In *Re-Blue Star Battery Systems International Corp.* eflex, (2000), 10 B.L.R. (3d) 221, Farley J. of this Court dealt with a claim very much like that considered by the Supreme Court of Canada in *Century Services, supra,* as it involved G.S.T. At paragraph 12, he said

> Thus it appears to me that RevCan, not having put itself into position where it could (and did) perfect its derivative claims as set out in section 323 (2) (a) of the *Excise Tax Act* never had a claim against the directors which could survive the sanction of the Plan vis-à-vis the Applicants. Nothing that this Court could do at the present time (that is, at the time when considering the CCAA sanctioned motion) could crystallize a RevCan claim against the directors. RevCan would have to take additional multiple steps over some period of time to establish a claim against the directors."

[72] Farley J. went on to discuss the hypothetical of a claim in oppression against the directors as provided for in s. 5.1(2) in the context where the creditor had put the directors on notice of the promise of the company to pay the tax.

[73] The argument of the Proposed Plaintiffs here is that "oppressive conduct" is not to be carved out, but that wrongful conduct that involves directors, even though the action as against the company cannot continue, it can continue against the directors.

[74] What in my view is consistent with the decisions in the three cases mentioned and in the Québec case *Papiers Gaspésia* 2006 QCCS 1460 (CanLII), 2006 QCCS 1460 (CanLII) and with the interpretation of s. 5.1(2) is that the actions of the directors toward persons who may be regarded as creditors, and may in this context include a shareholder, are based on a direct relationship when a director takes on an obligation to make a payment that would otherwise be the obligation of the company and promises to do so or is obliged to do so by legislation. In most cases this will be a post-filing obligation. In other words, a promise by a director directly to a creditor stakeholder that is made following a CCAA Initial Order may attract liability to the director and should not be released.

[75] It would be inconsistent with the scheme of the CCAA to allow all claims in which shareholders claim oppression to proceed against directors for acts or omissions that they did in the name of the company prior to the Initial Order. There would be little if any incentive to directors to pursue restructuring if they were going to be so exposed. On the other hand, personal undertakings or obligations of directors made during the CCAA process should not easily be released.

[76] To permit the kind of claims as the Proposed Plaintiffs would see them would create a priority to that class of unsecured creditors that properly should belong to the creditors as a group. No leave to continue the Class action was sought before the Sanction Order was granted and even on this motion no submission was put forward for the exercise of discretion under section 5 .1 (3).

[77] None of the cases referred to in argument dealing with s. 5.1(2) squarely deals with the issue raised here – that the section was intended to related to post-filing claims or personal undertakings of directors to creditors in connection with the proposed plan prior to filing.

[78] The final argument on behalf of Class Plaintiffs is that to deny the claim of shareholders as against directors would only benefit their insurers, since the Class Plaintiffs have agreed to limit any recovery to the amount of the insurance. I fail to see how this advances the position of the Proposed Plaintiffs. No information was put before the Court about the particulars of the insurance. The Court has no information to know whether or not the insurers even know of this issue.

[79] If the claim does not lie as against the directors in the first place under s. 5.1 (2), the limitation of the claim as against the potentially available insurance does not advance the case of the class of Plaintiffs.

[80] There would be little meaning left to s. 5.1 if all claims of negligence and wrongful conduct against directors for pre-filing activity could not be released and no need for the discretion provided for in s. 5.1 (3) for Court to override this compromise as not being fair or reasonable. As noted above in the passages from

the *Century Services* case, the purpose of the CCAA and the discretion granted to the Court are to permit restructuring to work, not create new causes of action.

[81] The concern of the Court, which necessitated the further inquiry, was that the language of the Sanction Order might imply on the part of the Applicant and directors who had knowledge of the particulars of the claim that the facts could give rise to a s. 5.1(2) claim. I am satisfied based on the further information provided that no such admission is to be implied.

[82] The relief sought by the directors is therefore granted.

Underwriters

[83] Underwriters acted on share and warrant offerings of Allen-Vanguard in September 2007 and certified a related prospectus. The Love Class Action was commenced in February 2010 and the proposed Representative Plaintiff claims damages against Underwriters under s. 130 of the *Securities Act (Ontario)* and also makes claims on the basis of negligence, unjust enrichment and waiver of tort.

[84] Underwriters rely on the provisions of the releases granted by the Sanction Order and in particular the claims against the Applicant Company Allen- Vanguard. As well, Underwriters rely on the definition of "Equity Claims" in the Sanction Order and submit that because the provisions of the Order in paragraph 26 (ii) bar certain claims against third parties who might claim contribution and indemnity against the restructured company, they should be entitled to the benefit of that provision.

[85] The response of the proposed Class Plaintiffs in the Love litigation is that the claim against Underwriters is based on the negligence, fraud or wilful misconduct of Underwriters. It is submitted that Underwriters are not entitled to indemnity as against Allen-Vanguard for the several negligence of Underwriters, either at law or under s. 130 of the *Securities Act*.

[86] The proposed Class Plaintiff submits that given the nature of the claim as against Underwriters, Underwriters would never have had a right to an indemnity for the claims asserted in the Love Action and therefore there were no such claims to be released.

[87] It is submitted that Underwriters bargained any possible indemnity away by the terms of their contract with Allen-Vanguard in September 2007, and that even if they had the benefit of an indemnity, all that was required for the Plan's success was that Alan-Vanguard be protected from Underwriters, not that Mr. Love's claims against Underwriters be eliminated.

[88] Counsel for the Plaintiff in the Love Action also urges that Underwriters did not have the right of indemnity as at the time of the Initial Order, and the Sanction Order bars any indemnity that they might otherwise have had and there is nothing in the language of either Order to preclude the claim of the Class Plaintiff against Underwriters limited to Underwriters' negligence.

[89] Finally, it is submitted that since Underwriters did not "bring anything to the table" in respect of the restructuring, there is no basis on which the Court should vary the Sanction Order to now provide the indemnity that the Order fails to provide.

[90] In the alternative, the Class Plaintiffs suggest that the Sanction Order be clarified, if necessary, to clearly provide the right of the Class Plaintiff to proceed against Underwriters.

[91] In my view, there is a distinction to be made between the claim as against the directors and that against Underwriters, since in the case as against the directors, the parties appear to have bargained that if the claim could be brought under s. 5.1 (2), it could proceed. That consideration was known to the parties who negotiated and agreed on the form of the Sanction Order and that was the only claim not otherwise covered by the Release terms.

[92] In the case of Underwriters, there was nothing to suggest that any discussion or negotiation took place with respect to specific protection for Underwriters or the allowance of a claim against Underwriters at the time that the Sanction Order was approved.

[93] This is another reason why in my view s. 5.1(2) of the CCAA should be read narrowly with respect to pre-filing claims or claims that relate to pre-filing activity.

[94] The *Ontario Business Corporations Act*,R.S.O. 1990 c. B. 16 ("OBCA") contains a statutory process for that kind of action and remedy sought by the Class Plaintiffs in both actions. Section 246(1) reads as follows:

> **246.** (1) Subject to subsection (2), a complainant may apply to the court for leave to bring an action in the name and on behalf of a corporation or any of its subsidiaries, or intervene in an action to which any such body corporate is a party, for the purpose of prosecuting, defending or discontinuing the action on behalf of the body corporate.

[95] The Supreme Court of Canada dealt with the issue of collective shareholder claims versus claims that are those of the corporation itself in *Hercules Management Ltd. et al. v. Ernst & Young*,1997 CanLII 345 (SCC), 1997 CanLII 345, [1997] 2 S.C.R.165. The case involved a claim by shareholders of the corporation against its auditors for an alleged negligence in preparation of financial statements of the corporation. Paragraph 48 of the reasons refers to and adopts a statement of Farley J. in *Roman Corp. v Peat Marwick Thorne* 1992 CanLII 7404 (ON SC), (1992), 11 O.R. (3rd) 248 (Gen. Div.) at p 260.

> As a matter of law the only purpose for which shareholders receive an auditor's report is to provide the shareholders with information for the purpose of overseeing the management and affairs of the corporation and not for the purpose of guiding personal investment decisions or personal speculation with a view to profit.

[96] The plaintiffs in *Hercules* asserted reliance on financial statements in monitoring the value of their equity and then due to auditors' negligence, they failed to extract it before the financial demise of the company.

[97] The Supreme Court, in assessing the claim, referred at paragraph 59 to the rule in *Foss v Harbottle*:

> 59. The rule in *Foss v. Harbottle*provides that individual shareholders have no cause of action in law for any wrongs done to the corporation and that if an action is to be brought in respect of such losses, it must be brought either by the corporation itself (through management) or by way of a derivative action. The legal rationale behind the rule was eloquently set out by the English Court of Appeal in *Prudential Assurance Co. v. Newman Industries Ltd. (No. 2)*, [1982] 1 All E.R. 354, at p. 367, as follows:

> The rule [in *Foss v. Harbottle*] is the consequence of the fact that a corporation is a separate legal entity. Other consequences are limited liability and limited rights. The company is liable for its contracts and torts; the shareholder has no such liability. The company acquires causes of action for breaches of contract and for torts which damage the company. No cause of action vests in the shareholder. When the shareholder acquires a share he accepts the fact that the value of his investment follows the fortunes of the company and that he can only exercise his influence over the fortunes of the company by the exercise of his voting rights in general meeting. The law confers on him the right to ensure that the company observes the limitations of its memorandum of association and the right to ensure that other shareholders observe the rule, imposed on them by the articles of association. If it is right that the law has conferred or should in certain restricted circumstances confer further rights on a shareholder the scope and consequences of such further rights require careful consideration.

To these lucid comments, I would respectfully add that the rule is also sound from a policy perspective, inasmuch as it avoids the procedural hassle of a multiplicity of actions.

60. The manner in which the rule in *Foss v. Harbottle*, *supra*, operates with respect to the appellants' claims can thus be demonstrated. As I have already explained, the appellants allege that they were prevented from properly overseeing the management of the audited corporations because the respondents' audit reports painted a misleading picture of their financial state. They allege further that had they known the true situation, they would have intervened to avoid the eventuality of the corporations' going into receivership and the consequent loss of their equity. The difficulty with this submission, I have suggested, is that it fails to recognize that in supervising management, the shareholders must be seen to be acting <u>as a body</u> in respect of the corporation's interests rather than as individuals in respect of their own ends. In a manner of speaking, the shareholders assume what may be seen to be a "managerial role" when, as a collectivity, they oversee the activities of the directors and officers through resolutions adopted at shareholder meetings. In this capacity, they cannot properly be understood to be acting simply as individual holders of equity. Rather, their collective decisions are made in respect of the corporation itself. Any duty owed by auditors in respect of this aspect of the shareholders' functions, then, would be owed not to shareholders *qua*individuals, but rather to all shareholders as a group, acting in the interests of the corporation. And if the decisions taken by the collectivity of shareholders are in respect of the corporation's affairs, then the shareholders'reliance on negligently prepared audit reports in taking such decisions will result in a wrong to the corporation for which the shareholders cannot, as individuals, recover.

61. This line of reasoning finds support in Lord Bridge's comments in *Caparo*, *supra*, at p. 580:

> The shareholders of a company have a collective interest in the company's proper management and in so far as a negligent failure of the auditor to report accurately on the state of the company's finances deprives the shareholders of the opportunity to exercise their powers in general meeting to call the directors to book and to ensure that errors in management are corrected, the shareholders ought to be entitled to a remedy. <u>But in practice no problem arises in this regard since the interest of the shareholders in the proper management of the company's affairs is indistinguishable from the interest of the company itself and any loss suffered by the shareholders . . . will be recouped by a claim against the auditor in the name of the company, not by individual shareholders</u>. [Emphasis in Supreme Court decision.]

It is also reflected in the decision of Farley J. in *Roman I*, *supra*, the facts of which were similar to those of the case at bar. In that case, the plaintiff shareholders brought an action against the defendant auditors alleging, *inter alia*, that the defendant's audit reports were negligently prepared. That negligence, the shareholders contended, prevented them from properly overseeing management which, in turn, led to the winding up of the corporation and a loss to the shareholders of their equity therein. Farley J. discussed the rule in *Foss v. Harbottle* and concluded that it operated so as to preclude the shareholders from bringing personal actions based on an alleged inability to supervise the conduct of management.

> 62. One final point should be made here. Referring to the case of *Goldex Mines Ltd. v. Revill* 1974 CanLII 433 (ON CA), (1974), 7 O.R. (2d) 216 (C.A.), the appellants submit that where a shareholder has been directly and individually harmed, that shareholder may have a personal cause of action even though the corporation may also have a separate and distinct cause of action. Nothing in the foregoing paragraphs should be understood to detract from this principle. In finding that claims in respect of losses stemming from an alleged inability to oversee or supervise management are really derivative and not personal in nature, I have found only that shareholders cannot raise individual claims in respect of a wrong done to the corporation. Indeed, this is the limit of the rule in *Foss v. Harbottle*. Where, however, a separate and distinct claim (say, in tort) can be raised with respect to a wrong done to a shareholder *qua* individual, a personal action may well lie, assuming that all the requisite elements of a cause of action can be made out.

[98] The policy of limiting indeterminate liability as in *Hercules* is consistent with the basis for the limitation of claims under s. 5.1(2) as set out above. In my view the words of s. 5.1(2) do not create a cause of action that would otherwise not exist except by leave of the Court. It simply provides an exception to what otherwise could be included in a release.

[99] The release terms contained in the Sanction Order would deprive Underwriters from any claims for contribution or indemnity to which they would otherwise be entitled at law from the Company and its directors and officers should the actions of the Class Plaintiffs proceed.

[100] This is just one further reason to support not just what is required for a derivative action but also what is required to be taken into consideration before the Court issues a Sanction Order in this case in effect on consent.

[101] As noted above, what has come to be known as a "liquidating" CCAA application can provide problems not just for the parties but the Court itself. The presumption behind the timing of the Application in this case was that if not granted quickly, bankruptcy would have ensued with the inevitable loss of jobs, assets and creditor claims.

[102] The Class Plaintiffs are taken to have known of the CCAA proposal as early as September 2009 and could have sought leave to commence a derivative action prior to or during the CCAA process. No such step was taken.

[103] I am satisfied that it is appropriate in the circumstances to stay the claims as against Underwriters in negligence and misrepresentation.

[104] The Claim against Underwriters also alleges fraud. If the only claim were in fraud and full particulars of alleged fraud were contained in the pleading, the claim might survive since the wording of the Release does not extend to fraud.

[105] Apart from fraud, claims in negligence against Underwriters are caught by the terms of the Release. Arguably, the claims are those of the Company that are specifically released.

Variation of the Sanction Order

[106] As noted above in reference to the decision in *Canadian Red Cross*, a Sanction Order in addition to being an Order of the Court and subject to the normal rules for variation thereof, represents an agreed contract between the creditors of an insolvent corporation.

[107] The Class Plaintiffs in the Laneville action did not seek to lift the stay at the time of the Initial Order. The Class Plaintiff accepted the Release provisions which extend to Underwriters when the Sanctioned Order was granted.

[108] Underwriters were released by the terms of the Sanction Order, and the Order, which was not appealed, represents a final determination of the rights of shareholders as against Underwriters.

[109] As was mentioned above, in respect of the suggestion of variation of the Sanction Order to permit the claim as against the directors, I conclude that it is not appropriate to vary a Sanction Order after the fact. The reliance that parties place on the finality of a Sanction Order is such that it would only be in extraordinary circumstances of a clear mistake, operative misrepresentation or fraud that would permit variation without re-opening the whole process.

[110] In *Extreme Retail (Canada) Inc. v. Bank of Montréal*, [2007] O.J. 3304 (Ont. S. J.) [Commercial List], Stinson J. held at paragraph 21 that an Approval and Vesting Order was a final determination of the rights of parties represented in that proceeding. Morawetz J. adopted those comments in *Royal Bank Body Blue Inc.* 2008 CanLII 19227 (ON SC), 2008 CanLII 19227 [ON S.C.] to the same effect at paragraphs 19 and 20. In my view the same principle applies to a Sanction Order.

[111] I see nothing in the requests of either Underwriters or the Class Plaintiffs that would be appropriate to permit variation of the Sanction Order as each of them have proposed.

[112] Should the Class Plaintiff in the Laneville action seek to pursue a claim against Underwriters limited alone in fraud, the action should be permitted to proceed subject to the Plaintiff persuading a judge that such a limited claim should be certified.

Conclusion

[113] For the above reasons the motion by the directors will succeed to enjoin the claims as against them in both the Love and Laneville actions. The motion of Underwriters to strike is granted, and motions for variation of the Sanction Order of both Underwriters and the Class Plaintiffs are dismissed. Counsel may make written submissions on the issue of costs.

C. CAMPBELL J.

Released:

Citation: Re Allen-Vanguard Corporation, 2011 ONSC 5017
Court File No. CV-09-00008502-00CL
Date: 20110825

SUPERIOR COURT OF JUSTICE
ONTARIO
(Commercial List)

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF ARRANGEMENT AND REORGANIZATION OF **ALLEN-VANGUARD CORPORATION** UNDER THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED AND SECTION 186 OF THE *ONTARIO BUSINESS CORPORATIONS ACT*., R.S.O. 1990, c.B.16, AS AMENDED

REASONS FOR DECISION

C. CAMPBELL J.

RELEASED: August 25, 2011

by LEXUM for the Federation of Law Societies of Canada

Tab 6

Indexed as:
Armstrong v. Shaw

Between
Robert Armstrong and Ann Armstrong, plaintiffs, and
Kennedy L. Shaw, Ken Shaw Motors Ltd. and Shaw Automotive Group Ltd., defendants

[1996] O.J. No. 4443

18 O.T.C. 25

67 A.C.W.S. (3d) 971

Court File No: 95-CQ-62090CM

Ontario Court of Justice (General Division)
Motions Court

Greer J.

Heard: November 15, 1996.
Oral judgment: December 18, 1996.

(10 pp.)

Guarantee and indemnity -- Rights of surety against principal debtor -- Discharge and other defences of surety -- Discharge by discharge of principal obligation -- Merger -- Acts of debtor -- Misrepresentation to surety -- Changes, principal debtor -- Change of corporate status.

Motion for summary judgment brought by the plaintiffs. The plaintiff Robert had gone to work as a manager of a car dealership controlled by the defendant Ken Shaw Motors. Originally, Robert was to operate a franchise Hyundai dealership. He and his wife had arranged funding, given guarantees to a bank, and mortgaged their cottage for that purpose. When the Hyundai dealership fell through, they were still indebted to the bank. The assets of Ken Shaw Motors were then transferred to a new company, Shaw Automotive, which also took over the debt and the guarantees. The evidence showed that Ken Shaw Motors, the principal debtor, had deposited monies into Shaw Automotive's account in order to repay the debt to the bank.

HELD: Motion granted. The guarantees were discharged because the principal debtor was discharged. A debtor and creditor must be two separate entities and a debt was extinguished with merger of the interest and creditor. The plaintiffs were granted a declaration that they were entitled to full indemnity from the defendant in connection with guarantees given in writing by them to the bank, a declaration that the indebtedness of the defendants to the bank or to the defendant Shaw Automotive had been paid in full, and that all guarantees of the plaintiffs had been discharged. The plaintiffs were granted judgment discharging the mortgage given by the plaintiffs on their cottage to the bank, judgment for the plaintiff

Robert for $4,100 for wages and vacation pay for wrongful dismissal and judgment for the plaintiff wife for $7,000 as a repayment of a loan made by her to the defendant company. There was no triable issue other than assessment of damages and no material issues of credibility which were genuine issues for trial.

Statutes, Regulations and Rules Cited:

Bulk Sales Act.
Courts of Justice Act.
Ontario Rules of Civil Procedure, Rule 20.02.

Counsel:

P. David McCutcheon and Janice L. Page for the plaintiffs.
Jeffrey C. Goldberg for the defendants.

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1 GREER J. (orally):-- The plaintiffs Robert Armstrong and Ann Armstrong, have moved for Summary Judgment against the defendants Kennedy L. Shaw, Ken Shaw Motors Ltd., and Shaw Automotive Group Ltd. in connection with a somewhat complex commercial history, but based on claims as set out in their Amended Statement of Claim dated March 16, 1995.

2 For purposes of this oral judgment, I do not propose to outline the facts as, in my view, they are clearly set out in the plaintiff's factum on p. 1, 2 and 17. Indeed the relief being requested is set out in the Notice of Motion which is dated August 27, 1996, and on the Motion I grant the plaintiffs Summary Judgment as follows:

(1) A declaration that the plaintiffs are entitled to full indemnity from the defendant Ken Shaw Motors Ltd. for all principal, interest, costs and other expenses incurred by them in connection with guarantees given in writing by them to the Canadian Imperial Bank of Commerce dated on or about May 13, 1991 and May 22, 1991 guaranteeing the debt and liabilities of Ken Shaw Motors as principal debtor.

(2) A declaration that the indebtedness of Ken Shaw Motors to the Canadian Imperial Bank of Commerce or to the defendant Shaw Automotive Group Ltd. has been paid and satisfied in full and that all guarantees and other security given by the plaintiffs in respect of any such indebtedness has been discharged and terminated.

(3) Judgment discharging the mortgage registered as instrument number 132720 on June 13, 1991 in the Land Registry Office in the District of Parry Sound, given by the plaintiffs to the Canadian Imperial Bank of Commerce in respect of the plaintiffs' cottage property which is described in the materials.

(4) Judgment for the plaintiff Robert Armstrong as against Kennedy L. Shaw and Ken Shaw Motors Ltd. in the amount of $4,100 for wages and vacation pay owing to him.

(5) Judgment for the plaintiff Ann Armstrong as against Ken Shaw Motors Ltd. and Kennedy L. Shaw in the amount of $7,000 as a repayment of a loan made by her to the company.

The Summary Judgment has been granted by me under these particulars headings for the following reasons as I hereinafter set out. In my view, there is no triable issue other than assessment of certain damages which I will set out at the end of reasons. In addition, there are no material issues of credibility which are genuine issues for trial in these proceedings.

3 The plaintiffs have set out in three volumes, with 73 tabs of materials, a very detailed and careful outline of the complex transactions which took place over a period of years from the time the plaintiff Robert Armstrong left his employment with Wietze's Motors and became involved with Kennedy L. Shaw ("Ken Shaw"). The Shaw and Armstrong families are related and their relationship goes back many years.

4 The Armstrongs became involved with Ken Shaw's businesses on or about mid-1989 and the facts with respect to the Hyundai dealership which Robert Armstrong believed was to be his business are clearly set out in his materials. In the end, Robert Armstrong got nothing from his move and ended up without a business, and both he and wife ended up guaranteeing debts and being liable under a line of credit with the Canadian Imperial Bank of Commerce in connection with a number of corporate moves made by Ken Shaw and his company. The guarantees are set out at tabs 16 and 68 of the Motion Record. The tracing of the corporate moves on the part of Ken Shaw and his companies are also set out in the materials.

5 The evidence, as presented by Robert Armstrong in his lengthy affidavit, in no way has been contradicted by the defendants' materials, in actual fact, the defendants filed no materials and filed no affidavit by Ken Shaw or his children who were eventually involved in the business of Shaw Automotive Group Ltd. at the end of the relationship between Robert Armstrong and Ken Shaw and his companies, nor were there any affidavits presented by any other possible witnesses who may have been able to support the contentions which Mr. Shaw made in his examination for discovery.

6 I am mindful of Rule 20.02 in that I am entitled to draw an adverse inference on a motion for Summary Judgment where there is a failure of a party to provide the evidence of persons having personal knowledge of contested acts. No such affidavits were presented and the only materials on which I was expected to rely in support of Mr. Shaw's allegations, which are set out in his eight-page factum, are those portions of his transcript which appear in the applicant's materials.

7 The guarantees which were given by Robert and Ann Armstrong were in connection with a business, being a franchise operation called Armstrong Hyundai, but which was also involved a numbered company. I am satisfied that it was Ken Shaw who induced Robert Armstrong to leave his employment with Wietze's and who talked him into giving up a Hyundai car dealership. There is no evidence which contradicts this in the materials before me except the bald allegation of Ken Shaw that it is not so. None of Ken Shaw's allegations, as set out in those portions of the transcript which are referred to in his factum, had a ring of truth to them when balanced with the evidence of the plaintiffs in the uncontradicted documentation which supports the plaintiffs' position.

8 I am satisfied that the initial representations made by Ken Shaw in the agreement entered into by him and Robert Armstrong, in particular, are as set out on pages 3, 4 and 5 of the applicants' factum. There is supporting documentation to show that Robert Armstrong and Ann Armstrong dealt with the bank in order to obtain funding and a line of credit from the Canadian Imperial Bank of Commerce and that they mortgaged their cottage property as security for the funding. The guarantees are guarantees in support of this. When the dealership (the Hyundai dealership) did not come to fruition because Ken Shaw said he was unable to sell his building to the doctors, from whom Robert Armstrong intended to lease the premises, the second series of representations and the second agreement between the parties came about. These facts are clearly set out on pages 5, 6 and 7 of the applicant's factum. It is in that area where Robert Armstrong ended up the position of General Manager of the dealership which was in the control of Ken Shaw Motors Ltd.

9 There were representations in a third agreement which are set out on pages 7 and 8 of the factum which show that the mortgage on the cottage property was never discharged and where the guarantees

remained outstanding during a corporate manoeuvre whereby the assets of Ken Shaw Motors Ltd. were transferred and sold to a new entity operated by Ken Shaw and his sons called "Shaw Automotive Group Limited." The documentation in the applicants' materials supports the transfer, yet no Bulk Sales Act affidavit was ever completed. Paragraph 19 of the factum sets out what took place in October of 1994 whereby Ken Shaw told Robert Armstrong that he would take the cottage property to pay the $200,000 line of credit that he claimed Ann and Robert Armstrong owed on the guarantees, or alternatively they could sell the cottage property and keep everything after the repayment of the loan. The business was never transferred to Robert Armstrong as Ken Shaw had promised several years prior to this. The bank on the other hand had never called the loan. It is clear from the documentation that when the assets of Ken Shaw Motors Ltd. were transferred to the new company, the value of the business was approximately $436,000 based on Ken Shaw's own financial statements and this did not include good will. Therefore it is clear that the debt could have been paid off and ought to have been paid off, thereby releasing the Armstrongs from the guarantee and line of credit. It therefore appeared that the corporate manoeuvres would have a very adverse impact on the Armstrongs and there is no evidence that they were ever properly explained to them.

10 The debt and the guarantees were taken over by the new company of which Ken Shaw was the secretary and his signature appears on many of the documents. At the time of the sale to Shaw Automotive, the Armstrong Hyundai liabilities of Ken Shaw Motors were extinguished at the bank and Ken Shaw Motors was entitled to receive a release of its debt on payment. After that point the bank could then look to Shaw Automotive for the repayment of the debt and not Ken Shaw Motors. The balance of the overdraft as of January 20, 1995 was $240,188.95 and a cheque payable to the bank in the amount of $241,430.26 dated January 23, 1995 was drawn on the Shaw Automotive account and deposited into the account of Ken Shaw Motors Ltd. operating as Armstrong Hyundai. The Shaw Automotive account shows that a debit and a credit on January 23 and 24, 1995 representing a deposit in the sum of $241,430.26 to the Shaw Automotive account in payment to the Canadian Imperial Bank of Commerce. The $241,000 deposited to the Shaw Automotive account came from Ken Shaw Motors. Shaw Automotive paid the amount in full which was due and owing to the Canadian Imperial Bank of Commerce. All of this evidence is set out in the applicants' motion materials. I am therefore satisfied on the evidence that the guarantees were discharged because the principal debtor was discharged. The law is clear that a debtor and creditor must be two separate entities and that a debt is extinguished with merger of the interest and creditor. On the evidence in the applicants' materials I am satisfied that this took place. Reference can be made to Re Central Capital Corp. (1996), 132 D.L.R. (4th) 223 at p. 236. Where there is a material variation in the relationship between creditor and principal a guarantor may be released from his or her obligations where the alteration has been undertaken without the consent of the guarantor and where the alteration material change the risk is assumed by the guarantor. K.P. McGuinnes, The Law of Guarantee, (2nd ed.) (Carswell Scarborough, 1996) at p. 533. The Armstrongs were never informed as to what was taking place as their guarantees moved from Armstrong Hyundai to the company being assumed by Ken Shaw Motors Ltd. and then the guarantees and debt were moved to Shaw Automotive Group Ltd. Further it has been held that guarantees will be discharged where the creditor acts in bad faith. See: Bank of Montreal v. Wilder (1986), 32 D.L.R. (4th) 9 (S.C.C.) at 22.

11 The guarantors Robert and Ann Armstrong are entitled to be indemnified by the principal debtor with respect to the guarantee obligations and I have granted the relief in that regard.

12 I have further granted them Judgment discharging the mortgage on their cottage property, as a guarantor is entitled to have any mortgage given in respect of a guarantee obligation discharged once the guarantee has been discharged. The court in Summary Judgment motions must take a hard look at what is presented to it. The respondent has to put his or her best foot forward. It has been noted in the case 1061590 Ontario Ltd. v. Ontario Jockey Club (1995), 21 O.R. (3d) 547 (C.A.) that the respondent must "...lead trump or risk losing...". I have taken a hard look at the merits and in my view there is no genuine

issue for trial other than the issues with respect to Robert Armstrong's claim for wrongful dismissal and the subsequent damages that he acts for in this regard.

13 I am satisfied on the evidence as presented in the materials that Robert Armstrong was wrongfully dismissed. I have awarded damages for the wages and vacation pay which are due and owing to him. I have concluded, however, that parties will either have to obtain a reference in connection with the damages for his claim or breach of agreement or breach of contract or an assessment in connection with his quantum meruit claim and claim for breach of fiduciary duty. His claim for punitive and exemplary damages flow out of his case for the breach of fiduciary duty. These issues perhaps can be dealt with by the parties at their pre-trial or perhaps can be dealt with in mediation. I am of the view that wrongful dismissal cases are often best dealt with at mediation rather than a trial. Counsel will both be in a better position to present the next Judge or the mediator with a supporting case law on the terms of wrongful dismissal and the adequate notice period and on the issues of quantum meruit, breach of fiduciary duty and punitive and exemplary damages.

14 In connection with the claim of Ann Armstrong, at the beginning of these reasons I granted judgment for her in the amount of $7,000. Ann Armstrong is entitled to the pre-judgment interest on that amount at the Courts of Justice Act rate on the date that the loan was made. The materials presented quite clearly show that the loan was made to the company and that she is entitled to repayment of it. Robert Armstrong is entitled to pre-judgment interest on the amount I have awarded to him from the date of his Statement of Claim at the Courts of Justice Act rate on that date.

GREER J.

qp/d/mmr/DRS/DRS/DRS

Indexed as:
Armstrong v. Shaw

Between
Robert Armstrong and Ann Armstrong, plaintiffs (respondents),
and
Kennedy L. Shaw, Ken Shaw Motors Limited, and Shaw Automotive Group Limited, defendants (appellants

[1998] O.J. No. 58

76 A.C.W.S. (3d) 986

Court of Appeal File No. C26225 and

Court File No. 95-CQ-62090 CM

Ontario Court of Appeal
Toronto, Ontario

Robins, Laskin and Rosenberg JJ.A.

January 7, 1998.

(2 pp.)

On appeal from Greer J.

Practice -- Appeals.

This was an appeal by the defendants from judgment.

HELD: Appeal allowed in part. The judgment was varied by deleting words from one paragraph.

Counsel:

Jeffrey Goldberg, for the appellant.
R. David McCutcheon and J.L. Page, for the respondent.

The judgment of the Court was delivered by

1 **ROBINS J.A.** (endorsement):-- The appeal will be dismissed save to the extent that paragraph 8(a) of the judgment below will be varied by deleting therefrom the words following "breach of agreement". The cross-appeal is dismissed.

2 Success being divided, there will be no costs.

ROBINS J.A.

qp/mjb/DRS

Tab 7

Halsbury's Laws of Canada

First Edition

BENNETT JONES
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(ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 179
(QC) *Business Corporations Act*, R.S.Q., c. S-31.1, ss. 285, 286
(SK) *Business Corporations Act*, R.S.S. 1978, c. B-10, s. 180
(NT) *Business Corporations Act*, S.N.W.T. 1996, c. 19, s. 188
(NU) *Business Corporations Act*, S.N.W.T. (Nu.) 1996, c. 19, s. 188
(YT) *Business Corporations Act*, R.S.Y. 2002, c. 20, s. 188.

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(5) Short-form Amalgamation

▼HBC-338▼ Explanation of vertical. A vertical short-form amalgamation occurs where a parent corporation, A, amalgamates with its subsidiary, B. The simplified procedure in short-form amalgamations reveals that, ultimately, the same shareholder interests remain after the amalgamation as before. The procedure for a vertical short-form amalgamation is set out in the various incorporating statutes[1]. Essentially, a holding corporation and one or more of its wholly owned subsidiary corporations may amalgamate and continue as one corporation provided two conditions are satisfied. The first condition is that the amalgamation must be approved by a resolution of the directors of each amalgamating corporation. The second condition is that these resolutions must each provide that:

(i) the shares of each amalgamating subsidiary corporation shall be cancelled without any repayment of capital in respect thereof;
(ii) the by-laws and articles of the amalgamated corporation shall be the same as the by-laws and articles of the amalgamating holding corporation; and
(iii) no securities shall be issued and no assets shall be distributed by the amalgamated corporation in connection with the amalgamation.

Following the adoption of these resolutions, the same administrative procedures must be followed as in a long-form amalgamation (*i.e.*, submission of the articles to the Director, accompanied by a completed director's or officer's statement, the giving of notices to creditors and endorsement of the certificate of amalgamation by the Director) to consummate the amalgamation of the parent corporation and its subsidiary.

Horizontal. A horizontal short-form amalgamation occurs where two or more corporations (Priorco and Beforeco), each of which is a wholly owned subsidiary of a third corporation (Parentco), amalgamate with each other. The procedure is not available for two corporations that are wholly owned by the same individual. The horizontal short-form amalgamation

procedure is very similar to that of vertical short-form amalgamation. Two or more wholly owned subsidiary corporations of the same holding body corporate may amalgamate and continue as one corporation without complying with the amalgamation agreement and shareholder approval provisions, provided three conditions are satisfied.[2]

1. First, as in a vertical short-form amalgamation, the subsidiaries must be wholly owned. Where any subsidiary has a minority shareholder, the corporations may still amalgamate, but they must follow the long-form amalgamation procedure.
2. The second condition is that the shares of all but one of the amalgamating subsidiary corporations must be cancelled without repayment of capital in respect thereof.[3] However, the stated capital of the amalgamating subsidiary corporations whose shares are cancelled shall be added to the stated capital of the amalgamating subsidiary corporation whose shares are not cancelled.
3. The third condition is that, except as may be prescribed, the articles of amalgamation must be the same as the articles of the amalgamating subsidiary corporation whose shares are not cancelled. It is not possible in the course of the amalgamation procedure itself to combine the most desired features of the two sets of articles, or otherwise to make amendments to the articles of the corporations. Any such amendments must be approved in the manner set out in the Act for amending the articles of incorporation. Until recently, it was unclear whether Amalco would inherit the by-laws of its dominant parent, or whether it was necessary to adopt new by-laws. This question has now been resolved. The by-laws of the amalgamated corporation shall be the same as the by-laws of the amalgamating subsidiary corporation whose shares are not cancelled.

Creation of successor corporation. Upon the articles of amalgamation becoming effective, the amalgamating corporations are amalgamated and continue as a single successor corporation under the terms and conditions prescribed in the amalgamation agreement.[4] The term "successor corporation" is not a strict legal term of art. In general terms, it describes a corporation that by merger, amalgamation, or otherwise by operation of law assumes the obligations and burdens and is vested with the rights and privileges of an earlier corporation.[5] The amalgamated corporations do not form a new company; rather, they are subsumed and continue to subsist as a single successor corporation.[6] The amalgamated corporation possesses all the property, rights, privileges and franchises and is subject to

all liabilities, including civil, criminal and quasi-criminal, and all contracts, disabilities and debts of each of the amalgamating corporations.[7] However, as the law is clear that a debtor and creditor must be two separate entities, any debt existing between the two predecessor corporations is extinguished upon the merger of the interest and creditor.[8] Although one corporation is not normally liable for debts and other obligations owed by another corporation, this rule does not apply to the corporation fused as a result of the amalgamation *vis-à-vis* the debts and obligations of its predecessors.[9] Thus, any mortgage or other security agreement entered into by either of the predecessor corporations does not disappear but continues as a security agreement of Amalco,[10] as will any other contract, and Amalco retains the same obligations[11] and rights[12] under such agreements as possessed by its predecessors. So, if a bond holder of old corporation A had a right to convert his or her bonds to some other form of security, that right will continue should A amalgamate with B to form Amalco.[13]

Survival of certain rights. Following an amalgamation, every conviction against, or a ruling, order or judgment in favour of or against an amalgamating corporation may be enforced against the amalgamated corporation,[14] and the amalgamated corporation (Amalco) is deemed to be the party plaintiff or party defendant, as the case may be, in any civil action commenced by or against either of the amalgamating corporations before the amalgamation became effective.[15]

Saving of security interests. Where two corporations amalgamate (*e.g.*, A Corp. and B Ltd.) and the name of the amalgamated corporation is the same as one of those corporations (*e.g.*, A Corp.), it is not necessary to register a new financing statement under the *Personal Property Security Act*[16] to maintain the perfection of security interests that were perfected by registration against the corporate name of the old A Corp.[17] However, in regard to (1) security interests perfected by registration against the name of B Ltd., or (2) security interests perfected by registration against the name of A Corp. or B Ltd. where the two corporations amalgamate and continue under a new name (*e.g.*, C Inc.). It may be necessary to comply with personal property security legislation requiring that where a security interest is perfected by registration and the secured party learns that the name of the debtor has changed, the security interest in the collateral becomes unperfected unless the secured party registers a financing change statement or takes possession of the collateral within a prescribed period.

Notes

1. For provisions dealing with short-form amalgamations generally, see:
   (CAN) *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 184(1)
   (AB) *Business Corporations Act*, R.S.A. 2000, c. B-9, s. 184(1)
   (BC) *Business Corporations Act*, S.B.C. 2002, c. 57, s. 273
   (MB) *Corporations Act*, C.C.S.M. c. C225, s. 178(1)
   (NB) *Business Corporations Act*, S.N.B. 1981, c. B-9.1, s. 123(1)
   (NL) *Corporations Act*, R.S.N.L. 1990, c. C-36, s. 291
   (ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 177(1)
   (QC) *Business Corporations Act*, R.S.Q., c. S-31.1, ss. 281, 282
   (SK) *Business Corporations Act*, R.S.S. 1978, c. B-10, s. 178(1)
   (NT) *Business Corporations Act*, S.N.W.T. 1996, c. 19, s. 186(1)
   (NU) *Business Corporations Act*, S.N.W.T. (Nu.) 1996, c. 19, s. 186(1)
   (YT) *Business Corporations Act*, R.S.Y. 2002, c. 20, s. 186(1).

   In 1994, the short-form amalgamation provisions of the (*Canada Business Corporations Act* ("CBCA") were amended (S.C. 1994, c. 24, s. 20) so that s. 184(1) of the Act now provides that a holding corporation and one or more of its subsidiary corporations may amalgamate and continue as one corporation without complying with ss. 182 and 183 of the CBCA if,

   (a) the amalgamation is approved by a resolution of the directors of each amalgamating corporation;

   (a.1) all of the issued shares of each amalgamating subsidiary corporation are held by one or more of the other amalgamating corporations; and

   (b) the resolutions provide that,

   (i) the shares of each amalgamating subsidiary corporation shall be cancelled without any repayment of capital in respect thereof,

   (ii) except as may be prescribed, the articles of amalgamation shall be the same as the articles of incorporation of the amalgamating holding corporation, and

   (iii) no securities shall be issued by the amalgamated corporation in connection with the amalgamation and the stated capital of the amalgamated corporation shall be the same as the stated capital of the amalgamating holding corporation.

2. (CAN) *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 184(2)
   (AB) *Business Corporations Act*, R.S.A. 2000, c. B-9, s. 184(2)
   (BC) *Business Corporations Act*, S.B.C. 2002, c. 57, s. 274
   (MB) *Corporations Act*, C.C.S.M. c. C225, s. 178(2)
   (NB) *Business Corporations Act*, S.N.B. 1981, c. B-9.1, s. 123(2)
   (NL) *Corporations Act*, R.S.N.L. 1990, c. C-36, s. 292
   (ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 177(2)
   (QC) *Business Corporations Act*, R.S.Q., c. S-31.1, s. 281
   (SK) *Business Corporations Act*, R.S.S. 1978, c. B-10, s. 178(2)
   (NT) *Business Corporations Act*, S.N.W.T. 1996, c. 19, s. 186(2)
   (NU) *Business Corporations Act*, S.N.W.T. (Nu.) 1996, c. 19, s. 186(2)
   (YT) *Business Corporations Act*, R.S.Y. 2002, c. 20, s. 186(2).

3. (ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 177(2)(b)(i).
4. (ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 179(a).
5. See, generally, *National Trust Co. v. Mead*, [1990] S.C.J. No. 76, [1990] 2 S.C.R. 410 (S.C.C.).
6. *Stanward Corp. v. Denison Mines Ltd.*, [1966] O.J. No. 1020, 57 D.L.R. (2d) 674 at 681 (Ont. C.A.), *per* Kelly J.A, affd [1968] S.C.J. No. 23, [1968] S.C.R. 441 (S.C.C.); *R. v. Black & Decker Manufacturing Co.*, [1974] S.C.J. No. 56, 43 D.L.R. (3d) 393 at 396-97 (S.C.C.).
7. (CAN) *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 186
   (AB) *Business Corporations Act*, R.S.A. 2000, c. B-9, s. 186
   (BC) *Business Corporations Act*, S.B.C. 2002, c. 57, s. 282
   (MB) *Corporations Act*, C.C.S.M. c. C225, s. 180
   (NB) *Business Corporations Act*, S.N.B. 1981, c. B-9.1, s. 125
   (NL) *Corporations Act*, R.S.N.L. 1990, c. C-36, s. 294(2)
   (NS) *Companies Act*, R.S.N.S. 1989, c. 81, s. 134(11), (12), (13), (21)
   (ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 179
   (QC) *Business Corporations Act*, R.S.Q., c. S-31.1, s. 286
   (SK) *Business Corporations Act*, R.S.S. 1978, c. B-10, s. 180
   (NT) *Business Corporations Act*, S.N.W.T. 1996, c. 19, s. 188
   (NU) *Business Corporations Act*, S.N.W.T. (Nu.) 1996, c. 19, s. 188
   (YT) *Business Corporations Act*, R.S.Y. 2002, c. 20, s. 188.
8. *Armstrong v. Shaw*, [1996] O.J. No. 4443, [1996] O.T.C. LEXIS 3917 (Ont. Gen. Div.), *per* Greer J, vard [1998] O.J. No. 58 (Ont. C.A.).
9. *Ramirez v. Amstead Industries Inc.*, 431 A.2d 811, 86 N.J. 332 (Sup. Ct. 1981).
10. *Re Manco Home Systems Ltd.*, [1990] B.C.J. No. 666, 78 C.B.R. (N.S.) 109 (B.C.C.A.), also reported as *Gesco Industries Ltd. v. Hongkong Bank of Canada*.
11. *Stanward Corp. v. Denison Mines Ltd.*, [1966] O.J. No. 1020, [1966] 2 O.R. 585 at 591 (Ont. C.A.), *per* Aylesworth J.A, affd [1968] S.C.J. No. 23, [1968] S.C.R. 441 (S.C.C.).
12. *Norcen International Ltd. v. Sunco Inc.*, [1988] A.R. No. 919, 91 A.R. 81 at 91 (Alta. Q.B.), *per* McBain J.
13. *Cayley v. Coburg, Peterborough & Marmora Railway & Mining Co.*, [1868] O.J. No. 225, 14 Gr. 571 (U.C. Ct. Ch.).
14. (ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 179(c).
15. (ON) *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 179(e); see also *C. & J. Enterprises (1971) Ltd. v. Curtis*, [1978] N.B.J. No. 329, 25 N.B.R. (2d) 537 (N.B.Q.B.). There is no similar provision in regard to administrative, criminal or quasi-criminal proceedings. The (CAN) *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 contains no provision equivalent to s. 179(e) of the Ontario *Business Corporations Act*.
16. (ON) R.S.O. 1990, c. P.10, as amended.
17. *Heidelberg Canada Graphic Equipment Ltd. v. Arthur Anderson Inc.*, [1992] O.J. No. 2530, 7 B.L.R. (2d) 236 (Ont. Gen. Div.).

Tab 8

Court File No. 04-CL-5306

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

THE HONOURABLE	THURSDAY, THE 16th
JUSTICE H.J.W. SIEGEL	DAY OF NOVEMBER, 2006

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO STELCO INC. AND THE OTHER APPLICANTS LISTED ON SCHEDULE "A"

APPLICATION UNDER THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

ORDER

THIS MOTION, made by Sunrise Partners Limited Partnership, Appaloosa Management L.P. and TD Securities, a Division of The Toronto Dominion Bank, Irving Wortsman, the Senior Debenture Holders, and 2074600 Ontario Inc. (collectively, the "Moving Parties") for leave to appeal to Court of Appeal, was heard this day at 393 University Avenue, Toronto, Ontario.

ON HEARING the submissions of counsel for the Moving Parties:

1. **THIS COURT ORDERS** that the Moving Parties be granted leave to appeal to the Court of Appeal from the Order of Mr. Justice H.J.W. Siegel dated October 31, 2006.

2. **THIS COURT ORDERS** that there be no costs on this motion.

ENTERED AT / INSCRIT À TORONTO
ON / BOOK NO:
LE / DANS LE REGISTRE NO.:

NOV 16 2006

PER/PAR:

O. Palumbo
Registrar

MBDOCS_3293313.3

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

Court File No. 04-CL-5306

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO STELCO INC. AND THE OTHER APPLICANTS LISTED IN SCHEDULE "A"

APPLICATION UNDER THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

Proceeding commenced at Toronto

ORDER

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IN THE MATTER OF THE *COMPANIES CREDITORS' ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED AND IN THE MATTER OF A PLAN OR COMPROMISE OR ARRANGEMENT OF GROWTHWORKS CANADIAN FUND LTD.

Court File No. CV-13-10279-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

Proceedings commenced in Toronto

BOOK OF AUTHORITIES OF THE OFFEREE SHAREHOLDERS
(Motion for a Mini-Trial, Returnable February 11, 2014)

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