Court File No. CV-18-00611219-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

B E T W E E N:

FTI CONSULTING CANADA INC.,
in its capacity as Court-appointed monitor in proceedings
pursuant to the Companies' Creditors Arrangement Act, RSC 1985, c. c-36

Plaintiff

and

ESL INVESTMENTS INC., ESL PARTNERS, LP, SPE I PARTNERS, LP, SPE MASTER I, LP, ESL
INSTITUTIONAL PARTNERS, LP, EDWARD S. LAMPERT, SEARS HOLDINGS CORPORATION, WILLIAM R. HARKER and WILLIAM C. CROWLEY

Defendants

Court File No. CV-18-00611214-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

B E T W E E N:

SEARS CANADA INC., by its Court-appointed Litigation Trustee, J. Douglas Cunningham, Q.C.

Plaintiff

and

ESL INVESTMENTS INC., ESL PARTNERS LP, SPE I PARTNERS LP, SPE MASTER I LP, ESL INSTITUTIONAL PARTNERS LP, EDWARD LAMPERT, EPHRAIM J. BIRD, DOUGLAS CAMPBELL, WILLIAM CROWLEY, WILLIAM HARKER, R. RAJA KHANNA, JAMES MCBURNEY, DEBORAH ROSATI, DONALD ROSS and SEARS HOLDINGS CORPORATION

Defendants

RESPONDING FACTUM OF THE LITIGATION TRUSTEE, THE MONITOR, AND THE PENSION ADMINISTRATOR
(VARIATION OF TIMETABLE)
(RETURNABLE SEPTEMBER 19, 2019)

September 17, 2019

Court File No. CV-18-00611217-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

B E T W E E N:

MORNEAU SHEPELL LTD., in its capacity as administrator of the Sears Canada Inc. Registered Retirement Plan

Plaintiff

and

ESL INVESTMENTS INC., ESL PARTNERS LP, SPE I PARTNERS, LP, SPE MASTER I, LP, ESL INSTITUTIONAL PARTNERS, LP, EDWARD S. LAMPERT, WILLIAM HARKER, WILLIAM CROWLEY, DONALD CAMPBELL ROSS, EPHRAIM J. BIRD, DEBORAH ROSATI, R. RAJA KHANNA, JAMES MCBURNEY, DOUGLAS CAMPBELL and SEARS HOLDINGS CORPORATION

Defendants

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TO: LITIGATION SERVICE LIST

TABLE OF CONTENTS

Page No.

PART I - INTRODUCTION

1. The Defendants Ephraim J. Bird, Douglas Campbell, William Crowley, William Harker, James McBurney, Donald Ross, R. Raja Khanna and Deborah Rosati (collectively, the "**Former Directors**") bring this motion for what they euphemistically call a "pause in the litigation".[1] In reality, they seek to stay the litigation for an indefinite but lengthy period, pending the ultimate determination of a series of complex cross-border proceedings and appeals.

2. In the alternative, the Former Directors seek an order that the estate of Sears Canada Inc. ("**Sears Canada**") advance them a non-recourse loan of an unspecified amount, for an unspecified time, to pay their unspecified (and undisclosed) defence costs.

3. The Former Directors assert in their Notice of Motion that they will suffer "extreme prejudice" in the absence of a stay or an advance of funds, but the evidence does not support this statement. Indeed, even in their factum, the most they can suggest is mere speculation that the litigation "could cause significant financial hardship".[2]

4. In fact, the evidence is that the Former Directors have significant assets and income and that they personally funded their own legal expenses for eight months in 2018, receiving reimbursement after they established insurance coverage. That is exactly how they should address their current lapse in coverage.

5. On this motion the Former Directors seek extraordinary and unprecedented relief without an evidentiary basis. Even more critically, they cannot meet the legal test for the relief they seek.

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[1] Factum of the Former Defendants (Motion to Vary Timetable or Obtain Interim Funding) ("**FD Factum**"), para. 1.

[2] FD Factum, para. 41.

6. The Former Directors consented to the order setting the timetable that they now seek to vary. They knew months before agreeing to it that their primary insurance coverage would soon be exhausted. In May 2019, their counsel stated that coverage would be "exhausted within the next few months or earlier".[3] There is no material change in circumstances that would justify a variation of the court-ordered timetable.

7. The Former Directors argue that refusal to fully pay their defence costs from the funds held by Sears Canada's estate would result in "manifest unfairness".[4] There is nothing unfair about defendants being required to pay their lawyers. Indeed, the Former Directors have entered into retainer agreements which require them to do just that. Unfairness would result if Sears Canada's creditors, who are in line to receive only a fraction of the amounts they are owed by the estate, were forced to fund the pre-filing unsecured claim for legal fees of the Former Directors.

8. There are thousands of former Sears Canada employees and pensioners with unpaid claims against the estate. Unlike the Former Directors, these employees and pensioners face real prejudice from a delay. Almost 1,000 pensioners have died since Sears Canada filed for insolvency protection. Further delay will irreparably harm other pensioners who will never get to see their claims adjudicated.

9. There is no legal basis for this motion or precedent to support it. Even if there were, the Court must balance the real prejudice to tens of thousands of former employees, retirees, and

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[3] Exhibit "G" to the Affidavit of Steven Bissell, sworn February 21, 2019 ("**Bissell Affidavit**"), Responding Motion Record of the Litigation Trustee, the Monitor, and the Pension Administrator (Timetable Motion) ("**RMR**"), Tab 1G, p. 159.

[4] FD Factum, para. 59.

other general unsecured creditors against the hypothetical harm that the Former Directors "could" suffer. The motion should be dismissed with costs.

PART II - SUMMARY OF FACTS

A. THE FORMER DIRECTORS' INSURANCE

10. Sears Canada made an application under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("**CCAA**"), on June 22, 2017.

11. In or around March 2018, six of Sears Canada's former directors, Ephraim J. Bird, Douglas Campbell, William Crowley, William Harker, James McBurney, and Donald Ross (the "**Cassels Directors**"), retained Cassels Brock & Blackwell LLP ("**CBB**") to represent them in connection with Sears Canada's insolvency and claims arising from it.[5] Each agreed to be personally liable, on a joint and several basis, for the entirety of CBB's legal fees, regardless of the availability of insurance coverage.[6]

12. Until October 2018, the Cassels Directors paid CBB's fees personally. Each client paid an equal share, but each is jointly responsible for the entire amount owed to CBB.[7]

13. One of CBB's first orders of business after being retained was to attempt to secure insurance coverage for their clients under a directors' and officers' ("**D&O**") insurance policy of Sears Canada or Sears Holdings Corporation ("**SHC**"). On March 8, 2018, CBB sent an email to

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[5] Transcript from the Cross-Examination of Donald Ross, held September 10, 2019 ("**Ross Transcript**"), pp. 17-18, qq. 42-43, Joint Transcript Brief of the Litigation Trustee, the Monitor, and the Pension Administrator ("**Joint TB**"), Tab 3.

[6] Transcript from the Examination of William Crowley, held September 10, 2019 "(**Crowley Transcript**"), p. 58, q. 164, Joint TB, Tab 1.

[7] Ross Transcript, p. 19, q. 50; p. 58, q. 193, Joint TB, Tab 3.

Sears Canada's primary D&O insurance providers, notifying them of "actual and potential claims" against the Cassels Directors.[8]

14. CBB sent a similar notice to Sears Canada's excess insurers on March 19, 2018.[9]

15. The insurers considered these claims notices over the spring and summer of 2018. As it became clear that confirmation of coverage would not arrive in short order, the Cassels Directors also retained Covington & Burling LLP ("**Covington**") to serve as coverage counsel in the United States.[10]

16. The Cassels Directors retained Covington jointly. Each client pays an equal share of Covington's fees personally and is jointly responsible for the entire amount owed to Covington.[11]

17. On October 22, 2018, Sears Canada's primary D&O insurer, XL Specialty Insurance Company ("**XL**"), advised that it would pay the defence costs of the Cassels Directors and the other two Former Directors, Deborah Rosati and R. Raja Khanna, under a 2015-16 D&O insurance policy originally issued to SHC (the "**2015 XL Policy**").

18. After XL agreed to pay defence costs, the Cassels Directors were reimbursed for the fees they had paid CBB personally over the eight months between March and October 2018.[12]

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[8] Exhibit "C" to the Affidavit of Donald Campbell Ross, sworn September 6, 2019 ("**Second Ross Affidavit**"), Reply Motion Record of the Former Directors ("**Reply MR**"), Tab 1C, p. 20.

[9] Exhibit "D" to Second Ross Affidavit, Reply MR, Tab 1D, pp. 22-24.

[10] Affidavit of Donald Campbell Ross, sworn August 23, 2019 ("**First Ross Affidavit**"), at paras. 18-19, Amended Motion Record of the Former Directors ("**MR**"), Tab 2, p. 14.

[11] Ross Transcript, pp. 22-23, qq. 62-65, Joint TB, Tab 3.

[12] Ross Transcript, p. 19, q. 50, Joint TB, Tab 3.

19. The original limit of the 2015 XL Policy was $15 million (USD). However, previous claims against the Policy had depleted that limit. As of November 7, 2018, the remaining limit under the 2015 XL Policy was $3 million (USD).[13]

20. The three proceedings in which this motion is brought (the "**Actions**") were commenced on December 19, 2018. Two of the Actions name all of the Former Directors, among others, as defendants. The third names, among others, Mr. Crowley and Mr. Harker.

21. The Former Directors understood by at least the spring of 2019 that the 2015 XL Policy would be exhausted prior to completion of the trial of these Actions.[14]

22. At that time, the first excess insurer under the 2015-16 D&O insurance tower, QBE Insurance Corp. ("**QBE**"), had not committed to providing coverage following the exhaustion of the primary policy. Between November 2018 and May 2019, Covington made "repeated" requests to QBE on the Former Directors' behalf, asking it to commit to providing excess coverage of their defence costs. QBE did not respond to these requests.[15]

23. On May 7, 2019, Covington sent QBE's counsel an email explaining that the 2015 XL Policy would be "exhausted within the next few months or earlier", and reiterating its request that QBE provide coverage following its exhaustion.[16] The Former Directors knew at that point that "the XL policy would at some point in the not too distant future be used up".[17]

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[13] Exhibit "S" to Second Ross Affidavit, Reply MR, Tab 1S, p. 99.

[14] First Ross Affidavit at para. 27, MR, Tab 2, p. 16.

[15] Exhibit "F" to Second Ross Affidavit, Reply MR, Tab 1F, p. 34.

[16] Exhibit "G" to Bissell Affidavit, Reply MR, Tab 1G, p. 159.

[17] Ross Transcript, p. 42, q. 125, Joint TB, Tab 3.

24. On May 16, 2019, QBE responded to inform the Former Directors that it would not agree to provide excess coverage. QBE took the position that the Actions involve claims first made in 2013, so defence costs should be paid under Sears Canada's 2013-14 D&O policy, in which QBE has no involvement. QBE also advised Covington of its intention to bring a proceeding in the United States to seek a declaration that it is not responsible for funding the Former Directors' defence costs.[18]

25. In the meantime, the Actions continued to progress. Statements of Defence in two of the Actions were served in May 2019, and schedules were fixed for production of documents.

26. On June 24, 2019, counsel for XL advised CBB that the remaining policy limit on the 2015 XL Policy was only $700,000 (USD).[19]

27. On June 27, 2019, the parties attended a case conference at which the Court set a tentative trial start date of May 19, 2020. This date was based on a draft timetable agreed to by the parties, subject to being finalized in July.[20]

28. At a case conference on July 12, 2019, the parties agreed to and the Court ordered a consent timetable for the remaining steps in the Actions (the "**Timetable**").[21] By that date, the Former Directors knew that:

(a) The first tier of insurance was about to be exhausted; and

[18] Exhibit "C" to Bissell Affidavit, RMR, Tab 1C, pp. 116-19.

[19] Exhibit "U" to Second Ross Affidavit, Reply MR, Tab 1U, pp. 106-107.

[20] Bissell Affidavit at para. 5(k), RMR, Tab 1, p. 6.

[21] Exhibit "H" to Bissell Affidavit, RMR, Tab 1H, p. 163.

(b) The second tier insurer, QBE, had denied excess coverage.

29. Knowing that QBE intended to commence proceedings in the United States regarding its insurance coverage obligations, the Former Directors commenced an application in Ontario for a declaration that QBE is required to pay their defence costs (the "**Coverage Application**"). In a supporting affidavit sworn on July 15, 2019, three days after the Former Directors consented to the Timetable, Donald Ross stated that the "2015 Policy limits have been or will be exhausted imminently".[22] Later that day, counsel for XL advised CBB that the 2015 XL Policy had been exhausted.[23]

30. The Former Directors brought the Coverage Application on July 18, 2019. The Application was originally scheduled to be heard on August 27, 2019.[24] On July 25, 2019, counsel for QBE advised the Former Directors that QBE would likely challenge the jurisdiction of the Ontario courts, and that it would not have materials prepared in time for an August 27 hearing.[25]

31. On August 8, 2019, more than three weeks after they were informed that the 2015 XL Policy had been exhausted – as anticipated in the May 7 email from Covington to QBE – and several months after coming to the conclusion that available insurance funds under that policy would not be sufficient to defend the Actions through trial, CBB wrote to counsel for the Plaintiffs and to the Court to advise that the 2015 XL Policy had been exhausted, and to request

[22] Exhibit "I" to Bissell Affidavit, at para. 30, RMR, Tab 1I, p. 179.

[23] Exhibit "R" to Second Ross Affidavit, Reply MR, Tab 1R, p. 91.

[24] Exhibit "H" to Bissell Affidavit, RMR, Tab 1H, p. 163.

[25] First Ross Affidavit at para. 49, MR, Tab 2, pp. 21-22.

the scheduling of a case conference on August 27, 2019.[26] In their letter to Plaintiffs' counsel, CBB also advised that they would "not be in a position to" meet the deadlines set out in the Timetable.[27]

32. The parties attended a telephone case conference before Justice McEwen on August 15, 2019. Justice McEwen directed that the issue of the Former Directors' insurance coverage be addressed at a case conference on August 27, 2019.

B. THE TIMETABLE MOTION

33. On Friday, August 23, 2019, after 6:00 pm, the Cassels Directors served this motion to suspend the Timetable pending the determination of the Coverage Application or coverage proceedings taking place in the United States.

34. At the August 27 case conference, the Court declined to hear this motion without a complete record. The Court pointed out that it did not have any evidence of the amount of the costs to which the Former Directors would be subject if required to interim fund their own defence, or of the financial harm that they would incur as a result.

35. At that case conference, the Court also set a schedule for the Coverage Application. A preliminary jurisdiction motion will be heard on September 25, 2019, with the merits to be heard on October 18, 2019. The Former Directors do not know when the Coverage Application will be resolved.[28]

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[26] Exhibit "H" to First Ross Affidavit, MR, Tab 2H, p. 98.

[27] Exhibit "G" to First Ross Affidavit, MR, Tab 2G, p. 96.

[28] Ross Transcript, pp. 54-55, qq. 175-82, Joint TB, Tab 3.

36. On August 30, 2019, the moving parties served an Amended Motion Record. The other two Former Directors, R. Raja Khanna and Deborah Rosati, joined the motion at that time. The Amended Notice of Motion seeks, as alternative relief, an order that the Former Directors' defence costs be paid for by Sears Canada's estate through a non-recourse loan to the Former Directors to be "repaid out of reimbursement of defence costs made from one or more insurers".[29]

C. THE ASSETS OF THE FORMER DIRECTORS

37. Counsel for the Litigation Trustee wrote to counsel for the Former Directors on August 30, 2019, to request production of net worth and income statements for each of the Former Directors.[30]

38. The Former Directors have refused to produce such statements for Mr. Harker or Mr. Crowley. CBB advised that Mr. Harker and Mr. Crowley would stipulate that they "have sufficient assets to interim fund their respective *pro rata* share of the currently anticipated legal fees that will be incurred until the [Coverage Application] is resolved".[31] Counsel also refused every question asked about Mr. Harker's and Mr. Crowley's finances at their examinations.[32]

39. The evidence in the record (distilled by the plaintiffs from publicly available information) strongly supports a conclusion that Mr. Harker and Mr. Crowley are extremely wealthy, and that

[29] Amended Notice of Motion at para (c), MR, Tab 1, p. 3.

[30] Exhibit "A" to Second Ross Affidavit, Reply MR, Tab 1A, p. 12.

[31] Exhibit "B" to Second Ross Affidavit, Reply MR, Tab 1B, p. 15.

[32] Crowley Transcript, pp. 32-36, qq. 73-91, Joint TB, Tab 1; Transcript from the Examination of William Harker, held September 10, 2019, p. 8, Joint TB, Tab 2.

they could easily pay the entire cost of the Former Directors' defence (or finance it for the other Former Directors) with little difficulty.

40. Mr. Crowley and Mr. Harker are the co-founders of Ashe Capital Management, LP ("**Ashe**"), a hedge fund with approximately $1.3 billion (USD) in assets under management.[33] Mr. Crowley is the CEO and Mr. Harker is the President of the fund.[34] In securities filings, Ashe has disclosed that it has four related persons (Mr. Harker, Mr. Crowley, a third individual, and a limited liability company in which Mr. Harker and Mr. Crowley are executive officers), and that its related persons and/or persons connected to them are the beneficial owners of 7% of the $1 billion in assets held by one of Ashe's funds, a total of approximately $70 million (USD).[35]

41. Mr. Crowley is a graduate of Yale Law School, and was formerly a managing director at Goldman Sachs (where he worked for 13 years), the chief administrative officer and CFO of SHC, the President and COO of ESL Investments, Inc. ("**ESL**"), and a director of AutoZone, Inc.[36] He appears to own an apartment on Central Park Avenue West in New York City which he purchased for $12,500,000 (USD) in September 2006.[37] At his examination, Mr. Crowley refused to answer questions about a house in the Hamptons that he appears to have bought in 2006 for $6,700,000 (USD).[38]

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[33] Exhibit "B" to the Affidavit of Eun Ji Yoon, sworn September 3, 2019 ("**Yoon Affidavit**"), RMR, Tab 2B, p. 257.

[34] Exhibit "B" to Yoon Affidavit, RMR, Tab 2B, p. 211; Exhibit "C" to Yoon Affidavit, RMR, Tab 2C, p. 361.

[35] Exhibit "B" to Yoon Affidavit, RMR, Tab 2B, pp. 247-249; Crowley Transcript, pp. 30-31, qq. 65-70, Joint TB, Tab 1.

[36] Exhibit "B" to Yoon Affidavit, RMR, Tab 2B, pp. 211, 267.

[37] Exhibit "B" to Yoon Affidavit, RMR, Tab 2B, p. 356.

[38] Crowley Transcript, p. 34, qq. 81-84, Joint TB, Tab 1. Joint TB, Tab 1D.

42. Mr. Harker is a graduate of the University of Pennsylvania Law School, and served as the general counsel of SHC and ESL, as well as a director of Sears Hometown & Outlet Stores, Inc. and Allison Transmission Holdings, Inc. In 2010, he received a salary of $1,330,000 (USD, including bonuses) in his position as general counsel of SHC.[39]

43. Although Mr. Harker and Mr. Crowley are the wealthiest of the Former Directors, the six other Former Directors have access to sufficient resources to fund their own defence costs. Financial records they have produced show [redacted].[40]

D. PROJECTED DEFENCE COSTS

44. The Former Directors have refused to provide information regarding their past defence costs, except to state that CBB incurred legal fees of approximately $260,000 over a seven-week period from July 15 to September 6, 2019.[41]

45. The Former Directors have also failed to produce any evidence of their projected or anticipated future defence costs.

46. The Former Directors have asserted that defence costs will ultimately be covered under either the 2015-16 or 2013-14 SHC D&O policies, and that the lapse in insurance coverage will

[39] Exhibit "C" to Yoon Affidavit, RMR, Tab 2C, pp. 360-363.

[40] Supplementary Joint Motion Record of the Monitor, the Litigation Trustee, and the Pension Administrator (Timetable Motion), Tabs 1A-1F.

[41] Exhibit "B" to Second Ross Affidavit, Reply MR, Tab 1B, p. 15.

be "temporary" and on an "interim" basis.[42] However, they have also admitted that they do not know whether their defence costs will ultimately be covered by D&O insurance.[43]

47. The only evidence that the Former Directors have provided about the impact of being required to fund their own defence costs is a bald statement by Donald Ross that the cost of defence counsel would deplete his assets and "may become unaffordable" at an unspecified time in the future.[44] Mr. Ross' unsubstantiated assertions ignore the fact that the Former Directors expect to eventually get reimbursed by whichever insurance tower is found to apply. Additionally, none of the other Former Directors have disclosed what they may be required to pay and what impact that would have on them, or how they would be prejudiced.

48. Mr. Crowley admitted at his examination that he will continue to fund his own defence if the Former Directors are unsuccessful on this motion, regardless of the duration or ultimate outcome of the Coverage Application.[45]

E. THE SEARS CANADA ESTATE

49. Since June 2017, the estate of Sears Canada, under the supervision of its court-appointed Monitor (the "**Monitor**"), has engaged in a process to identify claims against the estate. As of August 30, 2019, the currently estimated value of the outstanding claims is approximately $1.662 billion.[46]

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[42] FD Factum, para. 75.

[43] Exhibit "I" to Bissell Affidavit, RMR, Tab 1I, p. 189.

[44] First Ross Affidavit at para. 61, MR, Tab 2, pp. 24-25.

[45] Crowley Transcript, p. 58, q. 164, Joint TB, Tab 1.

[46] Bissell Affidavit at para. 6, RMR, Tab 1, pp. 9-10.

50. Among the claims against the estate are pension benefit claims of approximately 16,300 beneficiaries of the Sears Canada Inc. Registered Retirement Plan ("**Pensioners**"), amounting to more than $260 million. Many of the Pensioners are elderly: more than three-quarters are over 65, almost a third are over 80, and more than 1,000 of them are over 90 years old. Almost 1,000 Pensioners have died since June 2017.[47]

51. Sears Canada's unsecured creditors also include thousands of former employees and other retirees, whose claims total more than $630 million.[48]

52. The current assets of the estate are $205 million. This amount remains subject to reduction for ongoing costs of the CCAA proceedings, litigation costs funded through the $12 million litigation reserve, and any priority claims, and is in any event far less than required to satisfy the outstanding claims against it.[49]

53. Indemnification claims by Former Directors against Sears Canada under their indemnification agreements are unsecured pre-filing claims against the estate, to the extent they are determined to be valid claims at all, and are not entitled to any priority distribution.[50]

PART III - STATEMENT OF ISSUES, LAW & AUTHORITIES

A. ISSUES PRESENTED

54. There are two issues presented on this motion:

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[47] Bissell Affidavit at paras. 7-8, RMR, Tab 1, p. 10.

[48] Bissell Affidavit at para. 6, RMR, Tab 1, pp. 9-10.

[49] Transcript from the Cross-Examination of Steven Bissell, held September 11, 2019, p. 35, q. 105 Joint Transcript Brief of the Former Directors, Tab 1. Bissell Affidavit at para. 9, RMR, Tab 1, p. 10.

[50] Bissell Affidavit at para. 12, RMR, Tab 1, p. 11.

(a) whether the Court-ordered consent Timetable should be suspended until the dispute over whether, and, if so, which, insurer(s) will pay the Former Directors' defence costs has been resolved; and

(b) whether the Court should require the estate of Sears Canada to advance a non-recourse loan to the Former Directors for an unknown period of time, for an unspecified sum of money, to fund their undisclosed defence costs pending the resolution of the Coverage Application.

B. THE COURT-ORDERED TIMETABLE SHOULD NOT BE SUSPENDED

55. The Former Directors seek to suspend the Timetable, which they consented to and which was ordered by the Court, for an indefinite period of time. There is no basis to do so.

56. A suspension would seriously delay the resolution of the Actions, possibly for years, causing prejudice to Sears Canada's creditors and contravening public policy against the unnecessary delay of litigation. There is no precedent for defendants being able to stop litigation from proceeding because they wish to have a third party cover their legal fees, or because they would prefer not to pay their own fees. Such a rule would cause litigation to come to a standstill; this case is no different.

57. The justice of the case does not favour modification of the Court-ordered Timetable, nor has there been an unexpected change in circumstances that would justify such an exceptional step.

(i) Justice of the Case Favours Maintaining the Consent Order Timetable

58. The Court of Appeal has held that courts must be "cautious about setting aside orders, particularly those made on consent", both because of the importance of finality in the litigation process and the importance of holding parties to their agreements.[51] Consent orders will not be modified except when doing so is "necessary to achieve the justice of the case".[52]

59. Variation of the consent order establishing the Timetable is not necessary to achieve justice in this case. The delay resulting from a suspension of the Timetable would cause serious prejudice to Sears Canada's creditors and continued compliance with the Timetable does not materially prejudice the Former Directors.

60. The Former Directors are unable to say when the Coverage Application or proceedings on the same subject in the United States will be resolved.[53] However, given the existence of questions of jurisdiction, the interpretation of foreign law, competing proceedings in the United States, and likely appeals, the dispute will take at least a year, and probably much longer. Moreover, there is no certainty that the Former Directors will be successful in obtaining insurance coverage for their defence costs at all.

61. Distribution of any recoveries from the Actions to Sears Canada's creditors cannot take place until this litigation is resolved. As a result, any delay will further deprive creditors of the amounts that they are owed from the estate.

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[51] *Clatney v. Quinn Thiele Mineault Grodzki LLP*, 2016 ONCA 377, at para. 57, Book of Authorities of the Former Directors ("**FD BOA**"), Tab 11.

[52] *Stoughton Trailers Canada Corp. v. James Expedite Transport Inc.*, 2008 ONCA 817, at para. 1, FD BOA, Tab 9.

[53] Ross Transcript, pp. 54-55, qq. 175-82, Joint TB, Tab 3.

62. That concern is not merely academic. Almost 1,000 Pensioners with claims against Sears Canada's estate have died since Sears Canada made its CCAA application in June 2017. Many of the remaining Pensioners are elderly: more than 5,000 are over the age of 80 and more than 1,000 are over 90.[54] A delay in the resolution of these Actions will cause real harm to vulnerable people.

63. On the other hand, the benefit to the Former Directors of a delay would be limited. Their position is that the availability of insurance funding for their defence costs is a matter of "when", not "if", and that any lapse in coverage will be temporary, with repayment to follow once the Coverage Application is resolved.[55]

64. It is important to note that: (i) if the Former Directors are successful in obtaining coverage, then any fees that they pay in the interim will be reimbursed (as happened in 2018); or (ii) if they are unsuccessful, they will have paid their own fees as any defendant without insurance coverage must do. Either way, there is no cause to delay the Actions, because the outcome will be the same.

65. There is also no evidence or reason to believe that the Former Directors are impoverished such that they will not be able to pay or finance their own way in the interim. Much the opposite: the record suggests that their finances are more than adequate to do so. Furthermore, and in any event, there is no evidence that any of the Former Directors will no longer be represented by counsel if the Timetable is maintained while the insurance coverage issues are being litigated.

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[54] Bissell Affidavit at paras. 7-8, RMR, Tab 1, p. 10.

[55] FD Factum para. 75.

(ii) Lapse of Insurance not an Unexpected Circumstance

66. The Former Directors have failed to show the existence of an exceptional fact situation necessary to justify the variation of a timetable order. As the Court of Appeal noted in *1196158 Ontario Inc.*, fundamental principles of fairness require the enforcement of timelines absent "exceptional or unusual circumstances"[56]

67. The enforcement of timetable orders is not just a matter of fairness to the non-breaching party, but a reflection of the "strong public interest in promoting the timely resolution of disputes".[57] Unnecessary delay in the litigation process "undermines public confidence in the capacity of the justice system to process disputes fairly and efficiently".[58] The Supreme Court of Canada has recognized the importance of this policy goal, explaining that "The notion that justice delayed is justice denied reaches back to the mists of time" and "unnecessary delay strikes against [the] core values" of our legal system.[59]

68. Notwithstanding the overarching policy in favour of the enforcement of timetable orders, limited exceptions may be granted when the parties are faced with "unexpected and unusual contingencies".[60] However, no such circumstances are present in this case.

69. The Former Directors were aware no later than May 7, 2019 that the 2015 XL Policy would be depleted in the near future.[61] On May 16, 2019, they learned that QBE had refused to

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[56] *1196158 Ontario Inc. v. 6274013 Canada Ltd.*, 2012 ONCA 544, at para. 44, FD BOA, Tab 20.

[57] *Ibid.*, para. 39.

[58] *Ibid.*, paras. 19-20.

[59] *Ibid.*, para. 39 (quoting *Blencoe v. British Columbia (Human Rights Commission)*, 2000 SCC 44, para. 146).

[60] *Ibid.*, para. 19.

[61] Exhibit "G" to Bissell Affidavit, RMR, Tab 1G, p. 159.

provide excess coverage. QBE advised them on the same day of its intention to bring a proceeding in the United States for a declaration to that effect, putting the Former Directors on notice that it was likely to dispute the jurisdiction of the Ontario courts to hear the matter.[62] The Former Directors knew, or should have known, that resolution of the coverage dispute would not be imminent.

70. Despite knowing that their coverage under the primary insurance policy was on the verge of depletion and that no excess coverage was available, the Former Directors agreed to a timetable for the remaining steps in the Actions, up to and including trial. They consented to a tentative trial date on June 27, 2019, and to a final schedule on July 12, 2019, almost two months after they became aware of the looming interruption in their insurance coverage.[63]

71. Even after learning on July 15, 2019, that the 2015 XL Policy had been exhausted, the Former Directors waited more than three weeks before advising the other Parties and the Court of that fact, and another two weeks after that before bringing this motion. In short, although they knew that exhaustion was imminent when they consented to the Timetable order, and of the actual exhaustion of the 2015 XL Policy within three days of the Timetable order, they waited a further five weeks before seeking to vary it.

72. In light of what they knew and when they knew it, the Former Directors cannot now claim that the lapse in their insurance coverage is an unexpected development justifying suspension of the consent, Court-ordered litigation Timetable.

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[62] Exhibit "C" to Bissell Affidavit, RMR, Tab 1C, p. 119.

[63] Exhibit "H" to Bissell Affidavit, RMR, Tab 1H, p. 163.

(iii) No Other Reason to Delay Litigation

73. There would be no "economizing of resources and proceedings" if the Former Directors' motion is granted and the proceedings suspended.[64] A delay would not avoid any unnecessary procedural steps or save any costs.

74. Nor does the brief endorsement of Myers J. in the *Noranco* matter support the Former Directors' argument. There is no indication of the reason for the adjournment of proceedings in that case. It does not appear that any of the parties were seeking to vary a court-ordered schedule and the order did not follow a contested motion. Justice Myers also noted specifically that an adjournment would cause little or no prejudice in light of other pending procedural steps.[65] None of those factors are present here.

75. The assertion that mediation cannot proceed without a resolution of the insurance coverage issue is both speculative and incorrect. First, there is no evidence that Sears Canada's D&O insurers would refuse to participate in a mediation – it is common for insurers to attend settlement meetings even where there is doubt regarding coverage. In any event, it appears from the information provided that the Former Directors themselves have substantial personal assets that could meaningfully contribute to a settlement.

76. The Former Directors have not shown any reason to suspend the timetable sufficient to overcome the prejudice that would be suffered by Sears Canada's creditors and the strong public policy against the delay of litigation timelines.

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[64] *David v. Loblaw*, 2018 ONSC 7519, at para. 24, FD BOA, Tab 12.

[65] Handwritten Endorsement of Justice Myers, dated November 26, 2018, FD BOA, Tab 7.

C. THE ESTATE OF SEARS CANADA SHOULD NOT BE REQUIRED TO FUND THE FORMER DIRECTORS' DEFENCE

77. The alternative relief sought by the Former Directors is an order that they be given a loan from the estate of Sears Canada in an unspecified amount, for an unspecified period of time, on a non-recourse basis, to fund their individual defence costs.

78. There is no basis for such an order. It is the responsibility of the Former Directors, as it would be for any other defendant, to pay their own costs.

79. The precise amount of cash in the estate of Sears Canada is irrelevant to the Former Directors' obligation to pay their own costs in the absence of insurance coverage. This money does not belong to "Sears Canada": it is owed to creditors, and more particularly the tens of thousands of individual claimants in the estate.

80. In any event, it is undisputed that the estate has nowhere near enough assets to fund the claims of all of its creditors, including Pensioners and retirees.[66] It would not be appropriate for the estate to fund, at one hundred cents on the dollar, the defence of the wealthy Former Directors against its claims of breach of fiduciary duty, oppression and conspiracy while other creditors may eventually receive distributions of less than ten cents on the dollar for their claims.

81. Nor is the existence or amount of the court-ordered litigation reserve relevant to the Former Directors' obligation to pay their own costs. That reserve was established for very specific purposes that did not include funding of director legal fees, other than in the case of

[66] Bissell Affidavit at para. 9, RMR, Tab 1, p. 10.

adverse cost awards.[67] It would be contrary to its purpose to use the reserve to pay the Former Directors' costs.

82. The relief being sought by the Former Directors would have the effect of shifting the up-front cost and the risk of the Former Directors' defence to the estate of Sears Canada, and ultimately to its unsecured creditors. Because the Former Directors' proposed order would grant them a non-recourse interest-free loan, the estate would be required to take legal action to collect from any available insurance in the event that the insurers refuse to pay.

83. There is no valid basis to impose this burden on the estate of Sears Canada and its creditors. The Former Directors are the proper parties to bear or finance any costs associated with their own defence, and there is no evidence that they cannot do so.

(i) No Public Policy Basis for Estate to Fund Former Directors' Defence

84. There are no "principles of corporate indemnification" which require the estate to fund the Former Directors' defence. The Plaintiffs do not dispute that public policy generally favours the indemnification of corporate directors. However, indemnification is not an absolute right, and there is no rule or jurisprudence exempting corporate directors from the responsibility to bear their own costs if necessary, or requiring that civil proceedings be suspended when there is a lapse in their insurance coverage.

85. Unlike post-filing claims, for which a director's indemnity is provided for in the CCAA, indemnity for claims against an insolvent corporation's current or former directors arising from

[67] Bissell Affidavit at paras. 10-11, RMR, Tab 1, pp. 10-11.

pre-filing events are general unsecured claims against the estate.[68] The purpose of a s. 11.51 indemnity is to ensure the retention of directors during the restructuring process, not to protect former directors from legal costs relating exclusively to pre-filing conduct.[69]

86. That objective is not engaged in this case. As Morawetz J. noted in *Northstar*, allowing indemnification for pre-filing costs would "inequitably affect the priority of claims" in the CCAA process.[70] While the Former Directors have unsecured claims for indemnification against Sears Canada's estate, they have no entitlement to a pre-emptive distribution, and certainly no entitlement to a pre-emptive distribution at one hundred cents on the dollar.

87. There is also no basis for an order requiring the estate to fund the Former Directors' defence under s. 11.52 of the CCAA. That section allows the court to order the estate of an insolvent corporation to pay for the legal counsel of an "interested person" when it is "necessary for their effective participation in proceedings under [the CCAA]."[71] As Justice Pepall (as she then was) noted in *Fraser Papers*, an order under section 11.52 will be appropriate where "vulnerable" creditors "require assistance in the restructuring process" and are "not otherwise represented".[72]

88. That is not the case here. The Former Directors do not require assistance in the restructuring process, are already represented, and have provided no evidence to justify a finding

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[68] *Northstar Aerospace Inc., Re*, 2013 ONSC 1780 [Commercial List], para. 36 ["*Northstar*"], Joint Brief of Authorities of the Monitor, Litigation Trustee and Pension Administrator ("**Joint BOA**"), Tab 1.

[69] *Ibid.*, para. 29.

[70] *Ibid.*, para. 34.

[71] CCAA, s. 11.52(1)(c).

[72] *Fraser Papers Inc., Re*, [2009] O.J. No. 4287 (S.C.J. [Commercial List]), at para. 7, FD BOA, Tab 22.

that they are "vulnerable", or that payment from the estate is "necessary" for them to defend these Actions.

89. In *Fraser Papers*, this Court refused to order the estate to pay for counsel to a party that had indicated it would proceed "with or without funding", because "funding by the Applicants should only be provided for the benefit of those who otherwise would have no legal representation".[73] None of the Former Directors have said that they would stop defending the Actions without funding from the estate of Sears Canada, nor have their counsel said they would cease acting. Mr. Crowley testified that he would continue to defend the Actions with or without insurance funding.[74]

(ii) No Hardship Basis for Estate to Fund Former Directors' Defence

90. While courts occasionally authorize interim distributions in CCAA proceedings to alleviate hardship to creditors, such orders are rare and must be strongly compelled by the facts. Preliminary distributions are appropriate where necessary to prevent "dire and harsh consequences" to stakeholders who are "particularly vulnerable and at risk", and who would be "severely impacted" by a delay in payments.[75] They are limited to "bare-bone payments", which are contingent on the recipient demonstrating serious hardship.[76]

91. In the Sears Canada CCAA proceedings, the Court has approved pre-emptive distributions only to a limited number of unsecured creditors in entirely different circumstances

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[73] *Ibid.*, para. 10.

[74] Crowley Transcript, p. 58, q. 164, Joint TB, Tab 1.

[75] *EarthFirst Canada Inc., Re*, 2009 ABQB 78, at para. 6 ["*EarthFirst*"], Joint BOA, Tab 2; *Nortel Networks Corp., Re*, [2009] O.J. No. 2558 (S.C.J. [Commercial List]), at para. 87 ["*Nortel*"], Joint BOA, Tab 3.

[76] *EarthFirst*, at para. 8, Joint BOA, Tab 2; *Nortel*, at para. 88, Joint BOA, Tab 3.

from the Former Directors. The Employee Hardship Fund, established by an order of Justice Hainey on August 18, 2017, allowed former employees to receive hardship payments of up to $1,200 per week for eight weeks, plus $2,500 for medical or other emergencies. To access the fund, employees were required to show that they had no source of income, no reasonable expectation of earning any income, and that they were unable to work or access employment insurance benefits.[77] The Former Directors seek to receive more favourable treatment in their capacities as unsecured creditors than even this highly vulnerable group.

92. The Former Directors have not provided and cannot provide any basis for such an exceptional finding. There is no evidence of an inability to pay or obtain financing for their legal fees. In fact, the limited information provided for six of the Former Directors suggests that they can fund or finance their own defence costs. This is without taking into consideration the assets of Mr. Harker and Mr. Crowley, who have refused to provide financial information on the basis that they *can* indeed pay their defence fees.

93. Nor have the Former Directors provided any evidence as to what the cost of their defence is estimated to be. Those costs may well be limited. Mr. Crowley testified on cross-examination that he will continue to defend the Actions regardless of the availability of insurance coverage.[78] It is reasonable to expect that the marginal cost of representing the additional defendants would be minimal.

94. In light of the Former Directors' "tactical defence decision" to withhold relevant information about their financial status and anticipated costs, the Court should draw an inference

[77] Order of Hainey J. (Employee Hardship Fund), dated August 18, 2017, Joint BOA, Tab 4.

[78] Crowley Transcript, p. 58, q. 164, Joint TB, Tab 1.

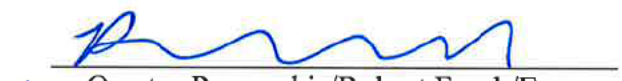
that they will collectively be able to afford their own defence without significant, if any, hardship.[79]

95. There is therefore no basis to treat the Former Directors differently from Sears Canada's other creditors by giving them an extraordinary pre-emptive distribution.

PART IV - ORDER REQUESTED

96. The Plaintiffs respectfully request that the Former Directors' motion be dismissed, with costs.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 17th day of September, 2019.



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[79] *Himel v. Molson*, 2015 ONCA 405, at para. 4, Joint BOA, Tab 5.

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SCHEDULE "A"

LIST OF AUTHORITIES

1. *Clatney v. Quinn Thiele Mineault Grodzki LLP*, 2016 ONCA 377

2. *Stoughton Trailers Canada Corp. v. James Expedite Transport Inc.*, 2008 ONCA 817

3. *1196158 Ontario Inc. v. 6274013 Canada Ltd.*, 2012 ONCA 544

4. *David v. Loblaw*, 2018 ONSC 7519

5. *Northstar Aerospace Inc., Re*, 2013 ONSC 1780 [Commercial List]

6. *Fraser Papers Inc., Re*, [2009] O.J. No. 4287 (S.C.J. [Commercial List])

7. *EarthFirst Canada Inc., Re*, 2009 ABQB 78

8. *Nortel Networks Corp., Re*, [2009] O.J. No. 2558 (S.C.J. [Commercial List])

9. Order of Hainey J. (Employee Hardship Fund), dated August 18, 2017

10. *Himel v. Molson*, 2015 ONCA 405

SCHEDULE "B"

TEXT OF STATUTES, REGULATIONS & BY - LAWS

1. *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36

Security or charge relating to director's indemnification

11.51 (1) On application by a debtor company and on notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring that all or part of the property of the company is subject to a security or charge — in an amount that the court considers appropriate — in favour of any director or officer of the company to indemnify the director or officer against obligations and liabilities that they may incur as a director or officer of the company after the commencement of proceedings under this Act.

Priority

(2) The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.

Restriction — indemnification insurance

(3) The court may not make the order if in its opinion the company could obtain adequate indemnification insurance for the director or officer at a reasonable cost.

Negligence, misconduct or fault

(4) The court shall make an order declaring that the security or charge does not apply in respect of a specific obligation or liability incurred by a director or officer if in its opinion the obligation or liability was incurred as a result of the director's or officer's gross negligence or wilful misconduct or, in Quebec, the director's or officer's gross or intentional fault.

Court may order security or charge to cover certain costs

11.52 (1) On notice to the secured creditors who are likely to be affected by the security or charge, the court may make an order declaring that all or part of the property of a debtor company is subject to a security or charge — in an amount that the court considers appropriate — in respect of the fees and expenses of

> **(a)** the monitor, including the fees and expenses of any financial, legal or other experts engaged by the monitor in the performance of the monitor's duties;
>
> **(b)** any financial, legal or other experts engaged by the company for the purpose of proceedings under this Act; and
>
> **(c)** any financial, legal or other experts engaged by any other interested person if the court is satisfied that the security or charge is necessary for their effective participation in proceedings under this Act.

Priority

(2) The court may order that the security or charge rank in priority over the claim of any secured creditor of the company.

SEARS CANADA INC., by its Court-appointed Litigation Trustee, J. Douglas Cunningham, Q.C. Plaintiff	-and-	ESL INVESTMENTS INC. et al. Defendants	Court File No. CV-18-00611214-00CL
FTI CONSULTING CANADA INC. Plaintiff	-and-	ESL INVESTMENTS INC. et al. Defendants	Court File No. CV-18-00611219-00CL
MORNEAU SHEPELL LTD. Plaintiff	-and-	ESL INVESTMENTS INC. et al. Defendants	Court File No. CV-18-00611217-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

PROCEEDING COMMENCED AT TORONTO

RESPONDING FACTUM OF THE LITIGATION TRUSTEE, THE MONITOR, AND THE PENSION ADMINISTRATOR

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