Court File No. CV-17-11846-00CL

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SEARS CANADA INC., 9370-2751 QUÉBEC INC., 191020 CANADA INC., THE CUT INC., SEARS CONTACT SERVICES INC., INITIUM LOGISTICS SERVICES INC., INITIUM COMMERCE LABS INC., INITIUM TRADING AND SOURCING CORP., SEARS FLOOR COVERING CENTRES INC., 173470 CANADA INC., 2497089 ONTARIO INC., 6988741 CANADA INC., 10011711 CANADA INC., 1592580 ONTARIO LIMITED, 955041 ALBERTA LTD., 4201531 CANADA INC., 168886 CANADA INC., and 3339611 CANADA INC.

Applicants

RESPONDING FACTUM OF CERTAIN FORMER DIRECTORS OF SEARS CANADA INC.
(Returnable on December 3, 2018)

November 27, 2018

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Lawyers for Certain Former Directors of Sears Canada Inc.

TO: **SERVICE LIST**

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PART I - OVERVIEW

1. On behalf of certain former directors (the "**Former Directors**")[1] of Sears Canada Inc. ("**Sears Canada**"), this factum responds to the motions (the "**Motions**") by FTI Consulting Canada Inc., in its capacity as the Monitor of Sears Canada and its affiliates (the "**Monitor**") and by Lax O'Sullivan Lisus Gottlieb LLP, in its capacity as the Litigation Investigator (the "**Litigation Investigator**"), seeking, among other things, an order lifting the stay of proceedings imposed under the *Companies' Creditors Arrangement Act*, RSC, 1985, c C-36 ("**CCAA**") to commence claims against certain of the Former Directors, among others.

2. After an eight-month investigatory mandate, which included no attempt to gather evidence from, or otherwise consult with, any of the Former Directors, the court-appointed Litigation Investigator now recommends the commencement of five separate claims, by five separate plaintiffs, against certain of the Former Directors, including claims to be advanced by the Monitor and a proposed Litigation Trustee, with the former Litigation Investigator appointed as his counsel, and a $12 million reserve drawn from the estate for their legal fees.

3. While the Former Directors do not seek any substantive determination on the merits of these claims at this stage, there are serious flaws in the breadth of the investigation and the theory of the claims which weigh against granting the relief sought on the Motions. The five proposed claims all relate, in some way, to a dividend Sears Canada paid to its shareholders in 2013, four years prior to its CCAA filing, at a time when Sears Canada's financial condition was strong and its future insolvency was not foreseen. After paying the impugned dividend in 2013, Sears Canada ended the year with $514 million in cash, no significant debt and no borrowings.[2]

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[1] The Former Directors currently represented by Cassels Brock & Blackwell LLP are Klaudio Leshnjani ("**Leshnjani**"), William R. Harker ("**Harker**"), William C. Crowley ("**Crowley**"), Donald C. Ross ("**Ross**"), James McBurney ("**Burney**"), Ephraim J. Bird ("**Bird**"), Calvin R. McDonald ("**McDonald**"), Ronald Boire ("**Boire**"), Deidra C. Merriwether ("**Merriweather**"), and Douglas Campbell ("**Campbell**").

[2] Affidavit of Jonathan Wypych, sworn March 1, 2018 ("**Wypych Affidavit**"), Responding Record of the ESL Parties, dated November 27, 2018 ("**ESL Record**"), Tab 1, at para. 5 and Exhibit "C" (see pg. 8).

Other parties continued to see the value in Sears Canada as well. Pursuant to a rights offering completed in October 2014, Edward S. Lampert, ESL Investments Inc. and certain of its affiliates purchased additional shares of Sears Canada for approximately USD$168.5 million, far more than they received pursuant to the 2013 dividend[3] and inconsistent with a "path to inevitable insolvency."[4] In 2017, the initial affidavit in these proceedings listed six causes of Sears Canada's financial struggles, none of them related to the 2013 divided.[5] Put simply, significant intervening factors contributed to Sears Canada's demise. It is an illogical stretch to conclude that the 2013 dividend caused or contributed in any way to Sears Canada's insolvency, which occurred years later, under different management, as a result of the decisions and advice of other parties, well after the Former Directors left the board.

4. In the Former Directors' view, these Motions are, at best, a misguided attempt to lay blame for Sears Canada's demise at the feet of the wrong parties. For unexplained reasons, claims against other parties, whose conduct in the lead up to Sears Canada's CCAA filing did contribute to its insolvency, are not being pursued. From the reports filed by the Monitor and the Litigation Investigator, it is apparent there has not been a fulsome examination of other factors that more plausibly lead to Sears Canada's insolvency including, but not limited to: (i) the process for replacing Ronald Boire after his resignation as CEO; (ii) the qualifications of the new management team hired to lead a retail company through a "transformation"; (iii) the relationships between the new management and the consultants they retained, including whether any conflicts of interest prejudiced the rights of Sears Canada's creditors; (iv) the reasons high level executives (including certain of the Former Directors) left Sears Canada in

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[3] Wypych Affidavit, ESL Record, Tab 1, para. 9.

[4] Twenty Seventh Report of FTI Consulting Canada Inc., as Monitor, dated November 5, 2018 ("**Monitor's 27th Report**"), Motion Record of the Monitor, dated November 5, 2018 ("**Monitor's Record**"), Tab 2, at para. 64.

[5] Affidavit of Billy Wong, sworn June 22, 2017 ("**Wong Affidavit**"), Responding Motion Record and Compendium of Certain Former Directors of Sears Canada Inc. ("**Former Directors' Record**"), Tab 1, at para. 194.

the two years prior to the CCAA filing; (v) the corporate culture at Sears Canada prior to the filing and its effect on the demise of the Sears Canada Entities; and (vi) the governance and oversight exercised by the subsequent board of directors, including with respect to the expenditure of the $500 million in cash remaining at the Company after the 2013 dividend[6] and the $300 million in cash at the beginning of 2016.[7] The Former Directors expect that a fulsome investigation of these issues and others would have returned more realistic potential causes of action for the benefit of the creditors.

5. The basis for the moving parties' recommendations are two brief, advocacy-based reports by the Litigation Investigator and the Monitor. There is very little detail provided regarding the nature of and basis for the proposed claims. Only two of the claims have been particularized through the delivery of pleadings or draft pleadings. The others, including the claim to be advanced by the proposed Litigation Trustee, lack important details, including the identity of the defendants to each claim and any specificity with respect to the allegations to be advanced. As court officers, the Litigation Investigator and the Monitor each have a duty to act, and report, in a neutral and even-handed manner toward all stakeholders – including the Former Directors. The reports do not discuss other potential claims, what potential defences would be raised, how tenuous these claims are, or how difficult they will be to prove. A court officer would typically provide a cost-benefit analysis of a proposed action.

6. The Former Directors will vigorously defend these meritless claims (which are inconsistent with publicly available facts), but insist that they be litigated in a manner that respects the procedural fairness to which all parties are entitled. The moving parties propose to equip the Litigation Trustee with extraordinary powers, including appointing the Litigation Trustee as a court officer. No explanation – or analysis – has been given as to why the existing

[6] Wypych Affidavit, ESL Record, Tab 1, Tab 1, para. 5.

[7] Wong Affidavit, Former Directors' Record, Tab 1, at Exhibit "D" (see: pg. 48).

Monitor, or the creditors, cannot bring these claims themselves. The proposed division of labour promotes a costly, one-sided process, designed to be advantageous to the putative plaintiffs. This will be of no benefit to stakeholders, other than professionals, and least of all Sears Canada's pensioners, former employees or other creditors.

7. As further set out herein, the Former Directors have serious concerns with the following aspects of the moving parties' proposed procedure:

(a) It is premature to impose a litigation protocol that would tie the hands of the defendants, and any Case Management Judge appointed to manage the proceedings, to a detailed process for discovery and trial procedure before statements of claim are even delivered. A Case Management Judge ought to be allowed to make appropriate decisions as the litigation develops and the issues are better distilled through pleadings and discovery;

(b) The funding mechanism proposed by the moving parties provides a $12 million reserve from the estate to fund the costs of the Litigation Trustee and the Monitor, but provides nothing for the substantial or full indemnity costs which the Former Directors will be entitled to when these claims, which impugn the reputation and good character of the Former Directors, are unsuccessful. Sears Canada should not be permitted to divest itself of assets that will be needed to cover these costs;

(c) The proposed Litigation Trustee is inexplicably equipped with broad discretion to waive privilege on behalf of Sears Canada (something even a trustee in bankruptcy is not empowered to do), thereby prejudicing the Former Directors who may also be entitled to the benefit of privilege over Sears Canada documents; and

(d) The proposal to set off recoveries from the Former Directors against distributions they will be owed in a future plan is an improper attempt to bind the Former Directors to aspects of a plan before they have any opportunity to vote on it.

8. Any order granting any portion of these Motions at this stage would be premature. The CCAA proceeding is presumably moving towards a plan. As creditors and potential litigation defendants, the Former Directors are entitled to fairness from the court and neutrality from the court officers. If the proposed claims are to proceed, it will not prejudice any stakeholders to wait and develop a procedurally fair litigation plan with appropriate funding mechanisms at the appropriate time.

PART II - THE FACTS

(a) Background to Sears Canada CCAA Proceeding

9. Pursuant to an order dated December 8, 2017 (the "**Claims Procedure Order**"), this Court established a claims procedure for claims against the Sears Canada Entities[8] and their current and former directors and officers. The Claims Procedure Order provided that "any claim against any of the Sears Canada Entities for indemnification by any Director or Officer in respect of a D&O Claim" was to be filed by the applicable claims bar date (the "**Indemnity Claims**").[9]

10. Pursuant to an order dated March 2, 2018 (the "**Litigation Investigator Order**"), this Court appointed the Litigation Investigator to review and recommend claims to be pursued, an appropriate procedure and the various funding mechanisms available for such actions.[10] Various creditors, including the Former Directors, opposed the broad mandate of the Litigation Investigator and its appointment as a court officer in light of the nature of its mandate.

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[8] "Sears Canada Entities" as used herein is as defined in the Initial Order and refers to the Applicants and Sears Connect LP.

[9] Claims Procedure Order, Former Directors' Record, Tab 3, at para. 3(g).

[10] Amended Litigation Investigator Order, issued April 26, 2018 ("**LI Order**"), ESL Record, Tab 2, at para. 3.

11. Although the Claims Procedure Order required the Monitor to respond to all proofs of claim by July 31, 2018, the Monitor sought three extensions because "determination of these contingent claims is closely tied to the determination of significant litigation, the approach to which will likely be informed by the Litigation Investigator's recommendations."[11] The Monitor now has until December 18, 2018 to respond to the D&O Claims and the D&O Indemnity Claims. There has been no indication what, if any, determination will be made on December 18, 2018 regarding these claims; indeed, there has been no consultation with the Former Directors as to the remaining claims and the defences thereto.

12. Eight months after its appointment, the Litigation Investigator has now made its recommendations in the form of an 11 page report and four page supplementary report (collectively, the "**LI's Report**"). Although the LI's Report makes reference to prior interim and final reports it has made to the Creditors' Committee, the Former Directors have not been privy to that information.[12]

(b) The Putative Claims

13. As described in the Twenty Seventh Report of the Monitor ("**Monitor's 27th Report**") and the LI's Report, filed in support of the Motions, the moving parties seek to advance five separate claims (the "**Putative Claims**") against various defendants, including some of the Former Directors, relating to the dividend paid by Sears Canada to its shareholders on December 6, 2013 (the "**2013 Dividend**").[13] The Putative Claims are as follows:

(a) a claim by the Monitor as against two Former Directors (namely, Harker and Crowley) and others attacking the 2013 Dividend as a "transfer at undervalue"

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[11] Twenty Fourth Report of the Monitor, dated September 13, 2018 ("**Monitor's 24th Report**"), Former Directors' Record, Tab 4, at para. 66.

[12] First Report of Lax O'Sullivan Lisus Gottlieb LLP, in its capacity as Litigation Investigator, dated November 6, 2018 ("**LI's First Report**"), at para. 12.

[13] LI's First Report, at paras. 16-30; Monitor's 27th Report, Monitor's Record, Tab 2, at paras. 76-82.

pursuant to section 96 of the *Bankruptcy and Insolvency Act*, RSC, 1985, c B-3 ("**BIA**"), (the "**Monitor Claim**");

(b) a claim by the proposed Litigation Trustee, to be appointed, on behalf of Sears Canada against certain, unspecified Former Directors and others for oppression, breach of fiduciary duty, breach of the standard of care, conspiracy, unjust enrichment, knowing assistance and knowing receipt in relation to the 2013 Dividend (the "**Litigation Trustee Claims**");

(c) a claim by Morneau Sheppell Ltd., the administrator of the Sears Canada pension plan (the "**Pension Administrator**"), against certain, unspecified Former Directors for breach of fiduciary duty, knowing assistance, knowing receipt and conspiracy (the "**Pension Administrator Claim**");

(d) a claim by the Superintendent of the Financial Services Commission of Ontario ("**FSCO**") against certain, unspecified Former Directors for oppression, breach of fiduciary duty, breach of standard of care, knowing assistance, knowing receipt and conspiracy (the "**FSCO Claim**"); and

(e) the resumption of a proposed class proceeding commenced prior to the CCAA filing in 2015 by 1291079 Ontario Limited on behalf of a proposed class of former "Sears Hometown" franchisees against six Former Directors (namely, Crowley, Harker, Ross, Bird, McBurney and Campbell) and others for oppression based upon the payment of the 2013 Dividend (the "**Proposed Class Proceeding**") while a certified class proceeding by the same group of franchisees for breach of contract and breaches of the *Arthur Wishart Act, (Franchise Disclosure), 2000*, SO 2000, c3, was pending (the "**2013 Class Proceeding**"). The moving parties propose to lift the stay only in respect of the Proposed Class Proceeding, which

has not been certified and has not advanced beyond the issuance of a Statement of Claim, but not the underlying 2013 Class Proceeding.[14]

14. At this juncture, most of the Putative Claims are lacking in any particularity. While the Monitor's 27th Report attaches a draft Statement of Claim for the Monitor Claim and the Proposed Class Proceeding claim was issued prior to Sears Canada's CCAA filing, no pleadings – even in draft form – have been provided in respect of any other Putative Claims.

15. For example, it is entirely unclear from the LI's Report which of the Former Directors are intended to be defendants to the Litigation Trustee Claim, the Pension Administrator Claim or the FSCO Claim, whether there is any overlap between the defendants to those Putative Claims, or what allegations will be made against the Former Directors named in those claims beyond the bald assertion of various causes of action and the suggestion that these Putative Claims may relate, in some way, to the 2013 Dividend.

(c) The Proposed Litigation Trustee

16. Under the moving parties' proposal, the Litigation Investigator's role would terminate and this Court would appoint the Hon. J. Douglas Cunningham, QC as a litigation trustee with court officer status and broad powers to prosecute the Litigation Trustee Claims (the "**Litigation Trustee**"). The Creditors' Committee would continue, although the materials do not address what role it will play.[15] While the Former Directors take no issue with Mr. Cunningham's qualifications, there are serious concerns with the necessity of a Litigation Trustee in these circumstances and the terms of the appointment sought by the moving parties, which are further set out herein.

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[14] LI's First Report, at paras. 20, 26, 27 and 29.

[15] Supplement to the First Report of Lax O'Sullivan Lisus Gottlieb LLP in its capacity as Litigation Investigator, dated November 16, 2018 ("**LI's Supplemental Report**"), at para. 16.

17. Lax O'Sullivan Lisus Gottlieb LLP, upon being discharged as Litigation Investigator, propose to be retained as counsel to the Litigation Trustee with access to a $12 million reserve from the Sears Canada estate to fund the prosecution of the Litigation Trustee Claims and the Monitor Claim. Under the Litigation Investigator's proposed protocol, the Litigation Trustee would also have the authority to waive privilege on behalf of Sears Canada.[16]

(d) The Proposed Litigation Protocol

18. The moving parties also seek to impose a litigation protocol which would govern pre-trial discovery and trial procedure for all of the Putative Claims.[17] Despite the fact that most of the Putative Claims have not yet been particularized through the delivery of pleadings, the proposed protocol seeks to determine procedure for production of documents, the conduct of examinations for discovery, discovery-related motions, expert reports and a common issues trial. With respect, this is nonsensical and procedurally unfair.

19. Despite having had possession of relevant documents for eight months (or more in the case of the Monitor), the moving parties have refused the Former Directors' requests for relevant documents which they would have had access to during their respective tenures on the Sears Canada board.[18] Notwithstanding the purported urgency in the process, the moving parties have denied access to documents which would expedite any trial on the merits.

(e) The Proposed Set-off and Opt-Out Mechanisms

20. Both Motions contemplate that any recoveries from the Former Directors in the Monitor Claim and the Litigation Trustee Claims will be net of any distributions payable to the Former

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[16] Proposed Litigation Trustee Appointment Order, at paras. 3-4.

[17] Proposed Litigation Trustee Appointment Order, at Schedule "A".

[18] Affidavit of Joseph Hamaliuk, sworn November 27, 2018, Former Directors' Record, Tab 2.

Directors on account of their Indemnity Claims.[19] Neither Motion justifies the need for such a provision at this time, other than "not requiring the estate to reserve funds to satisfy such potential indemnity claims".[20] The additional Putative Claims are not included in this proposal, suggesting that the Sears Canada Entities would still be required to reserve funds pursuant to any distribution mechanism to satisfy such Indemnity Claims.

21. While attempting to establish a procedure that anticipates the success of the Putative Claims, neither proposed order anticipates their failure by providing a reserve for costs that would be awarded to the Former Directors if the claims are not proven. Instead, the Monitor suggests that it will reserve the appropriate amount to pay the Former Directors' unsecured claims for legal fees under their indemnity agreements, which would pay cents on the dollar.[21] By contrast, in order to fund the Monitor Claim and the Litigation Trustee Claims, the moving parties propose to set aside $12 million (from assets that would otherwise be distributable to creditors).[22] In addition, the Monitor proposes to distribute an "opt-out notice" to allow creditors with claims over $5,000 to opt out of funding the Monitor Claim and the Litigation Trustee Claims, but correspondingly, opt out of any recovery that flows from the proposed litigation.

PART III - STATEMENT OF ISSUES, LAW & AUTHORITIES

22. The Former Directors take the following positions on the issues in these Motions:

(a) The stay of proceedings should not be lifted as against the Former Directors to allow the Putative Claims to proceed;

(b) The Monitor Claim should not be authorized;

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[19] Proposed Litigation Trustee Appointment Order at para. 7; Monitor's Draft Order, Monitor's Record, Tab 3, at para. 13.

[20] Monitor's 27th Report, Monitor's Record, Tab 2, at para. 85.

[21] Monitor's 27th Report, Monitor's Record, Tab 2, at para. 86.

[22] Monitor's 27th Report, Monitor's Record, Tab 2, at para. 87.

(c) The appointment of a Litigation Trustee is inappropriate and unnecessary; and

(d) The proposed litigation procedure orders are premature, overbroad and unfair and should not be imposed at this stage.

(a) The Stay of Proceedings Should Not be Lifted as Against the Former Directors

23. Although the Monitor and the Litigation Investigator suggest that the stay of proceedings in the Initial Order does not apply, this reading of the order is tortured at best. Both the Monitor and the Litigation Investigator argue in their factums that the stay does not apply because the directors are not liable "in their capacities as directors or officers for the payment or performance of such obligations."[23] With respect, that is exactly what the claims allege — actions against the Former Directors as directors.

24. Claims, such as the Putative Claims, against the Former Directors, arising from alleged conduct in their capacities as directors (e.g., decisions made at board meetings), are clearly stayed pursuant to paragraph 25 of the Initial Order. The moving parties must therefore meet the heavy onus required to lift the stay of proceedings to commence the Putative Claims against the Former Directors. They have not done so.

25. Lifting the stay in a CCAA proceeding is a discretionary decision which requires the party seeking to lift the stay to meet a high burden. The interests of all affected parties must be considered.[24] In *Sino-Forest*, Justice Morawetz summarized the three groups of factors to be considered on a lift-stay motion:

(a) the relative prejudice to parties from lifting the stay;

(b) the balance of convenience; and

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[23] Monitor's Factum, dated November 20, 2018 ("**Monitor's Factum**"), at para. 66.

[24] *Canwest Global Communications Corp.*, 2010 ONSC 3530, BOA, Tab 2, at paras. 40-41.

(c) where relevant, the merits of the claim (i.e. if the matter has little chance of success, there may not be sound reasons for lifting the stay).[25]

The court should also consider "whether the debtor company has acted and is acting in good faith."[26] All of these factors weigh against lifting the stay in this case.

(i) Lifting the Stay Would Prejudice the Former Directors and the Balance of Convenience Weighs Against Lifting the Stay

26. Since the Litigation Investigator's appointment, it has been a *fait accompli* that litigation would be recommended to this Court, but the manner in which the Monitor and the Litigation Investigator propose to proceed with the Putative Claims is highly prejudicial to the Former Directors and does not warrant lifting the stay.

27. The moving parties seek to lift the stay *only* with respect to certain Former Directors and not other relevant parties which are subject to the stay. They do not propose to lift the stay to allow the Former Directors to assert counterclaims, crossclaims or third party claims that likely ought to be filed in response to the Putative Claims, including claims against the parties who took control of the Sears Canada Entities after the Former Directors departed and the professionals who advised them. Indeed, because three of the five claims have not yet been drafted, any lifting of the stay would be incomplete, and could result in a situation where the Former Directors have claims commenced against them, but are unable to proceed, either by way of counterclaim or third party claims, due to a stay not being lifted, or not being lifted in a timely fashion.

28. If the stay is to be lifted as against the Former Directors, the Former Directors submit that it must also be lifted as against all relevant parties who may be the subject of crossclaims,

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[25] *Sino-Forest Corporation (Re)*, 2012 ONSC 6275, BOA, Tab 1, at para. 16 ["***Sino-Forest***"]; *Timminco Limited (Re)*, 2012 ONSC 2515, BOA, Tab 3, at para. 17.

[26] *Canwest Global Communications Corp. (Re)*, 2009 CanLII 70508 (ON SC), BOA, Tab 4, at para. 25.

counterclaims and third party claims by the Former Directors and other defendants to the Putative Claims. This may include, without limitation, the Sears Canada Entities and other former directors and officers of the Sears Canada Entities, whose conduct well after the Former Directors' tenure contributed to the company's demise. The fact that these potential parties cannot be identified yet (because the pleadings have not yet been delivered) illustrates that these Motions are premature at best.

29. Similarly, under the moving parties' proposal, the Proposed Class Proceeding would only be reinstated against the Former Directors and not the other Sears Canada Entities named as defendants. The stay would remain in place as to Sears Canada, prohibiting the adjudication of the underlying claims in the 2013 Class Proceeding. By lifting the stay of proceedings in such a limited fashion, the Monitor and the Litigation Investigator ask the Court to tie the Former Directors' hands, prohibiting them from properly seeking an adjudication on the merits of the 2013 Class Proceeding which may be necessary to fully defend themselves on the merits of the Proposed Class Proceeding.

30. Finally, the Monitor's apparent unwillingness to pursue any claim against Sears Holdings Corporation ("**Sears Holdings**") due to its recent Chapter 11 filing will cause further prejudice, as Sears Holdings would be a necessary party, both for evidentiary purposes for all of the Putative Claims and with respect to the relief sought in the Monitor Claim under section 96 of the BIA. Such uneven prosecution of claims is prejudicial to the Former Directors and other defendants to the Putative Claims.

(ii) The Monitor and Litigation Investigator Have Failed to Demonstrate Sufficient Merit to the Putative Claims to Justify Lifting the Stay

31. In a situation rife with prejudice, the Court's gate-keeper function in assessing the merits of the proposed claims takes on a more important role. The party seeking to lift the stay bears the onus of establishing that the claim it seeks to commence or continue is reasonable, tenable

and not oppressive, vexatious or an abuse of process.[27] On the limited materials filed, the Monitor and the Litigation Investigator fail to meet even this low hurdle.

32. The LI's Report fails to identify the parties or the nature of the allegations in the Litigation Trustee Claims, the Pension Administrator Claim or the FSCO Claim. It does not attach draft Statements of Claim or identify any of the evidence on which it has relied in recommending that these claims be pursued. The LI's Report does not contain any evidence in support of the proposed claims at all, but instead relies on suppositions in the Monitor's draft Statement of Claim as if they were facts.[28] The Litigation Investigator does not clarify how it can candidly advise the Court on the "facts" in the Monitor's report because it admits that it has not reviewed any potentially privileged documents that the Former Directors may have reviewed in their deliberation.[29] In the absence of any such detail, the Litigation Investigator has no basis for its assertion that these claims have "*prima facie* merit."

33. The Proposed Class Proceeding also suffers from two glaring issues on the merits, neither of which have been addressed in the LI's Report. First, the claim relies upon and is derivative of the 2013 Class Proceeding brought on behalf of the same group of franchisees. The 2013 Class Proceeding remains stayed and is subject to the Claims Process approved in the CCAA proceeding. The Monitor, a party seeking to sue the Former Directors, is now the arbiter of that 2013 Class Proceeding, while at the same time seeking to pursue the Former Directors (and others) on the same set of facts. Second, the oppression claim advanced against the Former Directors in the Proposed Class Proceeding is *prima facie* without merit. In a recent similar franchisee class action, this court struck claims by Tim Hortons franchisees against the

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[27] *Ivaco Inc. (Re)*, 2006 CarswellOnt 8025 (SCJ), BOA, Tab 5, at paras. 20, 29-30.

[28] LI's Supplemental Report, at para. 11: The Litigation Investigator attempts to deal with the lack of particularization for the Putative Claims by stating that it "anticipates that the LT Claims (as defined in the LI's First Report) will be based largely on the same facts as those alleged in the Monitor's draft statement of claim (attached to the Monitor's 27th Report) concerning the Monitor's Claim."

[29] LI's Supplemental Report, at para. 14.

directors of the franchisor and its affiliates for being untenable on the basis that the franchisees lacked standing to bring such claims and because there was no basis to assert an oppression claim against the directors, as opposed to the franchisor itself.[30]

34. Equally importantly, neither the Monitor nor the Litigation Investigator have made any effort to address the significant limitations concerns raised by many of the Putative Claims. The Litigation Trustee Claims, Pension Administrator Claim and FSCO Claim are all presumed to be statute-barred as of December 2015, at the latest, based on the application of sections 4 and 5(2) of the *Limitations Act, 2002*, SO 2002, c 24, Sch B ("***Limitations Act***").[31] Nothing in the *Limitations Act* suggests that claims for breach of a fiduciary duty, oppression, or any of the other causes of action asserted in Litigation Trustee Claims, Pension Administrator Claim or FSCO Claim, escape that statute's two year limitation period.[32] Accordingly, the moving parties (along with FSCO and the Pension Administrator) will bear the onus of rebutting the statutory presumption that the applicable limitation periods have expired. No explanation has been provided as to how these parties intend to do so.

(b) The Monitor Claim Should Not Be Authorized

35. The Monitor has not demonstrated why it should be authorized to pursue the Monitor Claim at this time. While there is no specific test to determine when a Monitor should be authorized to pursue claims under section 36.1 of the CCAA, as this court recently noted in *Urbancorp Cumberland 2 GP Inc., (Re*), a Monitor seeking authorization to take on a litigation role must demonstrate with proper evidence how its pursuit of a claim will further the restructuring process. The court's observations in that case are equally applicable here:

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[30] *1523428 Ontario Inc. / JB&M Walker Ltd. v TDL Group*, 2018 ONSC 5886, BOA, Tab 6, at paras. 21-30, 67-71.

[31] *Limitations Act, 2002*, SO 2002, c 24, Sch B, ss. 4, 5(1)(b),(2).

[32] See for example: *Fracassi v Cascioli,* 2011 ONSC 178, BOA, Tab 7, at para. 272.

> [...] **I do not see how, in this liquidating *CCAA* process, the Monitor bringing proceedings in place of the creditors who stand to gain from it can be said to facilitate the restructuring**. In *Essar* there was a particular roadblock to a fair and proper restructuring affecting all interested parties. Here, by contrast, the Monitor pits the current creditors against a group of creditors who were paid over one year before the proceedings commenced. **Why is this a fight for the Monitor rather than the creditors who stand to benefit from the claim?**
>
> If there is no actual creditor with a sufficient stake to sue or to support the Monitor with evidence in a suit, then I again question the utility of empowering the Monitor to bring a claim that pits creditors against each other. **It is not the Monitor's role to "try one on" to see if it can increase recovery for the current creditor body. Creditors are free to spend their money and face the consequences.** The Monitor, by contrast, acts with the *imprimatur* the Court. It is far more constrained in its activities and ought typically to consider seeking court approval before undertaking litigation on behalf of particular interests. [emphasis added][33]

Aside from bald assertions in its 27th Report that authorizing the Monitor Claim would be "appropriate", the Monitor has not addressed these important questions.

36. As noted above, the Monitor Claim is also fatally flawed on the merits because it seeks to attack a shareholder dividend under section 96 of the BIA, which does not apply to dividends. Section 96 is designed to review non-arm's length "transfers" in the five year period prior to the CCAA filing. The 2013 Dividend is not a transfer. As the Monitor notes, no consideration is paid by shareholders in exchange for receiving a dividend. Dividends are dealt with separately under the more specific scheme of section 101 of the BIA, which only permits the review of dividends for a one-year period prior to the CCAA filing and is intended to be an exhaustive code for the review of dividends under the BIA.

37. Including dividends within the scope of section 96 would render the specific power to review dividends under section 101 meaningless and redundant. This cannot have been Parliament's intention. Such an interpretation runs contrary to the accepted approach to statutory interpretation: "namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the

[33] *Urbancorp Cumberland 2 GP Inc., (Re)*, 2017 ONSC 7649, BOA, Tab 8, at paras. 21, 26.

Act, and the intention of Parliament."[34] Alternatively, to the extent any internal conflict exists between sections 96 and 101, the interpretive principle that specific statutory provisions must prevail over more general provisions favours interpreting the specific provision of section 101 as an exception, carving out dividends from the general application of section 96.[35]

38. As the Monitor admits in its factum, there is no precedent for reviewing a dividend under section 96. The Monitor relies on *Armoires de cuisine de Montréal ltée (Re)*, a case decided 35 years ago, on very different facts and under a different iteration of the BIA. This case provides no authority for the Monitor's proposed application of the current section 96 to the 2013 Dividend.

39. Even if section 96 of the CCAA is applicable to the 2013 Dividend, the Monitor admits there is little evidence to suggest that it can meet the preliminary threshold of establishing that Sears Canada was "insolvent" at the time of the 2013 Dividend or rendered insolvent by it. For example, the Monitor states as follows:

(a) "The Monitor is not able to conclude that as of the date of the 2013 Dividend, Sears Canada was an insolvent person, as defined in the BIA";[36]

(b) "From a cash flow perspective, Sears Canada continued to operate for several years after the 2013 Dividend. Accordingly, one could not reasonably conclude that Sears Canada had ceased paying or ceased to be able to pay its obligations as they were coming due at the time of, or as a result of, the 2013 Dividend";[37] and

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[34] *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 SCR 27, BOA, Tab 9, at para. 21.

[35] *Schnarr v Blue Mountain*, 2018 ONCA 313, BOA, Tab 10, at paras. 4, 61-64.

[36] Monitor's 27th Report, Monitor's Record, Tab 2, at para. 42.

[37] Monitor's 27th Report, Monitor's Record, Tab 2, at para. 44.

(c) "[...] the Monitor cannot conclude that Sears Canada was insolvent at the time of the 2013 Dividend [...]".[38]

In light of these admissions, the Monitor will be required to prove that the Former Directors intended to "defraud, defeat or delay a creditor" by approving the 2013 Dividend, which is untenable based on facts available in the public record.

40. Authorizing the Monitor to proceed with such a speculative claim at this stage would be prejudicial to all creditors. Given that multiple sets of defence counsel will be required to defend the Monitor Claim, the legal fees required to prosecute the claim (which the Monitor estimates to be $12 million for only two of the Putative Claims), and the potential costs exposure if the claim is unsuccessful (which could very well be higher than $12 million, given the nature of the Putative Claims), the unsuccessful prosecution and dismissal of the Monitor Claim may result in a 15% *reduction* in estate funds available for distribution. As such, the Monitor should not be authorized to proceed with the Monitor Claim.

(c) A Litigation Trustee Should Not Be Appointed

41. The LI's Report provides no justification for the extraordinary remedy of appointing a Litigation Trustee in these circumstances. This is particularly troubling given that the Monitor already exists as a court officer with a continuing mandate. While the Litigation Investigator rightly points out that litigation trustees have been appointed in prior insolvencies, it fails to note that in all of the cases it relies upon, the litigation trustees were appointed as a result of a restructuring plan, settlement, or other circumstances where it could be shown that the Monitor or creditors themselves were not well placed to litigate the claims at issue. The circumstances in this case are different and do not justify the creation of an entirely new court officer role to prosecute claims alongside the Monitor and other creditors.

[38] Monitor's 27th Report, Monitor's Record, Tab 2, at para. 45.

42. The proposed appointment of a Litigation Trustee in this case is effectively an end run around the existing mechanisms under the BIA and CCAA whereby the Monitor or creditors themselves can advance the Litigation Trustee Claims by way of section 38 proceedings or an application by the Monitor, without creating an entirely new court officer and the resulting duplication of estate-funded litigation costs. The Reports offer no justification for this duplicative structure.

43. The Litigation Investigator should be held to the same standard as the Monitor or any creditor seeking leave to commence an action on behalf of the estate. If the Monitor were seeking to commence the Litigation Trustee Claims, it would be required to meet the high threshold outlined by the Ontario Court of Appeal in *Ernst and Young Inc. v Essar Global Fund Limited*, including that:

(a) there is a *prima facie* case that merits an oppression action or application;

(b) the proposed action or application itself has a restructuring purpose, that is to say, it materially advances or removes an impediment to a restructuring; and

(c) whether any other stakeholder is better placed to be a complainant.[39]

None of these factors has been addressed by the moving parties in seeking to justify why the Litigation Trustee Claims ought to proceed.

44. If, as appears to be the case, the Monitor has decided against proceeding with the Litigation Trustee Claims, section 38 of the BIA, as incorporated by section 36.1 of the CCAA, already provides creditors with a mechanism to take up an action for their own benefit and at their own cost, so long as the claim is not "obviously spurious".[40] If the major creditors of Sears

[39] *Ernst & Young Inc. v Essar Global Fund Limited*, 2017 ONCA 1014, BOA, Tab 11, at para. 123.

[40] *Bankruptcy and Insolvency Act* (Canada), R.S.C. 1985, c. B-3, s. 38; *Smith v Pricewaterhousecoopers Inc.*, 2013 ABCA 288, BOA, Tab 12, at para. 16.

Canada wish to pursue the Litigation Trustee Claims, they ought to do so under that procedure and at their own risk and expense. No explanation has been provided as to why that existing statutory procedure should not be followed. Instead, the Monitor proposes to add yet another layer of complication and expense, sending out an additional notice to creditors allowing them to "opt-out" of the litigation rather than allowing creditors to "opt-in" and bear their own costs under section 38 of the BIA.

45. The proposed appointment of a Litigation Trustee as a court officer also raises a number of procedural concerns vis-à-vis the alternatives available under section 38 of the BIA. Specifically, as a court officer, the Litigation Trustee will be entitled to file evidence by way of report, which this Court has recognized as being on par or "in many ways more reliable" than an affidavit, but not subject to the same rights of cross-examination.[41] This court has held that litigants opposite court officers have no *prima facie* right to cross-examine a court officer, may only do so in "unusual" circumstances and must apply to the court for leave.[42] No justification has been provided for the moving parties' request to cloak a proposed litigant with such extraordinary protections.

46. The current Litigation Investigator's request to be appointed as counsel to the Litigation Trustee raises additional issues. Given the manner in which the Litigation Investigator has conducted its investigation, which did not include any attempt to seek input from the Former Directors, and the one-sided nature of the LI's Report, which makes no reference any exculpatory evidence that might benefit the Former Directors, there is little reason to invite the creation of a further court officer who will act as an adversarial participant in this proceeding.

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[41] *Montor Business Corp. (Trustee Of) v Goldfinger*, 2011 ONSC 2044, BOA, Tab 13, at para. 25.

[42] *Martellacci, Re*, 2014 ONSC 5188, BOA, Tab 14, at para. 21; *Bell Canada International Inc., Re*, 2003 CarswellOnt 4537 (SCJ), BOA, Tab 15, at para. 8.

(d) The Proposed Litigation Procedure Should Not Be Imposed

47. The moving parties' proposal to coordinate multiple actions, through multiple counsel, raises substantive and procedural concerns that must be remedied before any order can be made. Although the moving parties present this procedure as "streamlining" the litigation to achieve efficiency, there is no basis to determine whether such efficiencies even exist at this stage and many reasons to believe that, if adopted, the proposed procedure would create unfairness. As is further detailed below, the proposed litigation protocol, funding mechanism, privilege waiver and set-off provisions are of particular concern to the Former Directors.

(i) The Litigation Protocol is Premature and Overbroad

48. It is premature, at this stage, to bind the hands of the Former Directors to a far-reaching protocol that seeks to regulate the pre-trial and trial conduct of the action despite the lack of details about the Putative Claims. As noted above, pleadings have been provided only in respect of the Monitor Claim and the Proposed Class Proceeding. The only details provided for the other Putative Claims relate to the proposed plaintiffs, vague assertions of causes of action that will be asserted, and a suggestion that the claims will relate to the 2013 Dividend. Even the identity of the defendants to each of the Putative Claims has not been provided. In this context, there is no basis for the Litigation Investigator's assertion that "interwoven issues, overlapping damages and evidence, similar parties and the potential for costs savings" would justify the imposition of their proposed protocol.[43]

49. The Former Directors are not opposed to the notion of a litigation protocol to assist with streamlining the litigation of the Putative Claims, if they are permitted to proceed. However, such a protocol would be more appropriately discussed and determined, assuming the claims are authorized to proceed at all, once the claims are fully particularized, and if necessary with the assistance of a Case Management Judge. This ought to be a collaborative process, with

[43] Litigation Investigator's Factum, dated November 20, 2018 ("**LI's Factum**"), at para. 53.

input from all parties. In this instance, the moving parties made no attempt to discuss the proposed protocol before serving their motion materials – ignoring the guiding principles of Commercial List practice embodied by the "Three C's": "cooperation, communication and common sense".[44]

(ii) The Proposed Funding Mechanism Unduly Favours the Plaintiffs

50. The funding mechanism proposed by the moving parties fails to account for the likelihood that, if the Putative Claims are unsuccessful, the Former Directors will likely be entitled to costs on a substantial or full indemnity basis from the plaintiffs since the Putative Claims are based on allegations of improper, dishonest conduct which puts the reputations and character of the Former Directors at issue.

51. The Putative Claims all involve allegations of dishonest conduct on the part of the Former Directors and, as such, may trigger a higher scale of costs if they are not proven. In *1175777 Ontario Ltd. v Magna International Inc.*, the court awarded substantial indemnity costs to a defendant director after the plaintiff unsuccessfully advanced a similar allegation of conspiracy against him at trial. In doing so, the court stressed that substantial indemnity costs are not limited to unproven allegations of fraud, but may be awarded in cases where "dishonest conduct" is alleged against a director seeking to "financially gain" from an alleged conspiracy. Awarding a higher scale of costs in such circumstances recognizes that conspiracy claims, even absent express allegations of fraud, disclose allegations of "serious personal misconduct" which are "seriously prejudicial to the character or reputation of the individual."[45]

52. Similar awards of substantial or full indemnity costs have also been made in cases involving breach of fiduciary duty and other causes of action based on allegations of intentional

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[44] Consolidated Practice Direction Concerning the Commercial List, at Part III.5.

[45] *1175777 Ontario Ltd. v Magna International Inc.*, 2007 CarswellOnt 4135, BOA, Tab 16, at paras. 32-34.

wrongdoing.[46] The Monitor Claim, which alleges that certain Former Directors were "privy" to the alleged transfer at undervalue for having conspired to deliver a benefit to other parties, also falls in this category, as it asserts a concerted, unlawful scheme between certain Former Directors and the proposed shareholder defendants (notwithstanding the fact that they have not and cannot show a relationship between the Former Directors and the proposed shareholder defendants at the relevant time).

53. Accordingly, the Former Directors suggest, at a minimum, that sufficient funds be set aside at the outset of any proposed litigation to satisfy an award of substantial or full indemnity costs which may be made in the event the Putative Claims are not successful. While the moving parties propose to create a $12 million reserve from the estate to fund their two sets of counsel fees, no such similar protection is provided for the Former Directors' potential costs claim. In the interest of fairness, it is important that the Sears Canada estate not be depleted such that it is without sufficient funds to satisfy such a costs award when the Putative Claims are unsuccessful. Requiring that funds be set aside is preferable to an order for security for costs, since such orders are generally reserved for situations where the plaintiff is already without sufficient assets to satisfy a costs award. Sears Canada must not be allowed to deplete its assets so as to render itself impecunious and unable to pay a costs award in favour of the Former Directors and other defendants.

(iii) The Privilege Waiver is Inappropriate

54. The moving parties have also failed to justify their proposal to equip the Litigation Trustee with the extraordinary power to waive privilege on behalf of Sears Canada. It is well established that a trustee in bankruptcy, a court officer who actually takes possession of an insolvent person's assets, does not have the ability to waive privilege on behalf of the bankrupt

[46] *MacKinnon v MacKinnon*, 2010 ONSC 2661, BOA, Tab 17, at paras. 27-29; *Hawkins v Hawkins Estate,* 2015 ONSC 1106, BOA, Tab 18, at para. 15; *New Solutions Extrusion Corporation v Gauthier*, 2010 ONSC 1897, BOA, Tab 19, at paras. 3-4.

and that the protection of creditors or the resignation of a company's directors and officers are not sufficient reasons to permit a trustee in bankruptcy to waive privilege.[47] Given that this extraordinary power is not even afforded to a trustee in bankruptcy, it is inappropriate to empower the Litigation Trustee to do so.

55. The proposed protocol fails to adequately address the likely issues of overlapping privilege belonging to both Sears Canada and the Former Directors with respect to privileged documents and information created during their tenure on the board. The Alberta Court of Appeal noted in *Bre-X Minerals Ltd., Re* as follows:

> In the case of a company, the privilege is solely the right of the company. There may also be situations where questions of privilege will arise with respect to individuals such as directors, officers and managers of the corporation who seek advice from the corporate solicitor as to their own obligations, which may become intertwined with corporate opinions.[48]

This is precisely the situation faced by the Former Directors. Again, the moving parties have made no attempt to address these concerns in a manner that is fair and reasonable.

(iv) The Set-Off Provisions Are Premature, Unfair and Improper

56. The set-off provisions proposed by the moving parties are an improper attempt to pre-determine the elements of a plan that the Former Directors have not yet seen and which, under this formulation, would not be allowed to vote on. These aspects of the proposed orders are not justified or addressed at all in the moving parties' factums. Implementing the proposed set-off provisions now would violate the long-held principle that creditors cannot be bound by the provisions of a compromise or plan before they have had the opportunity to vote on it.[49] The Former Directors are creditors with significant claims for indemnification in respect of both legal

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[47] *Clarkson Co. v Chilcott*, 1984 CarswellOnt 187 (CA), BOA, Tab 20, at paras. 8-15; *Bre-X Minerals Ltd., Re*, 2001 ABCA 255, BOA, Tab 21, at paras. 24-45, 65 ["***Bre-X***"]; *Katz, Re*, 2013 ONSC 4543, BOA, Tab 22, at para. 10.

[48] *Bre-X*, *supra*, BOA, Tab 22, at para. 34.

[49] *Re, Doman Industries Ltd. (Trustee of)*, 2003 BCSC 376, BOA, Tab 23, at para. 9.

defence costs and any amounts for which they may be found liable. As such, they are entitled to review the plan and deal with this issue at the appropriate time.

57. Moreover, the purported simplifying effect that the Monitor and the Litigation Investigator claim the set-off provisions will have is far from certain. The proposed orders do not provide that the other three proposed plaintiffs to the Putative Claims will agree to the same treatment and the Monitor would therefore be required to reserve for the full amounts of the Former Directors' indemnity claims. Once the Sears Canada Entities (or the Monitor) propose a plan, this provision can be reconsidered with full information.

PART IV - ORDER REQUESTED

58. Accordingly, the Former Directors respectfully request that the Motions be dismissed.

ALL OF WHICH IS RESPECTFULLY SUBMITTED this 27th day of November, 2018.

Cassels Brock & Blackwell

per Cassels Brock & Blackwell LLP

SCHEDULE "A"

LIST OF AUTHORITIES

1. *Sino-Forest Corporation (Re)*, 2012 ONSC 6275
2. *Canwest Global Communications Corp.*, 2010 ONSC 3530
3. *Timminco Limited (Re)*, 2012 ONSC 2515
4. *Canwest Global Communications Corp. (Re)*, 2009 CanLII 70508 (ON SC) *Ivaco Inc. (Re)*, 2006 CarswellOnt 8025 (SCJ)
5. *Ivaco Inc. (Re)*, 2006 CarswellOnt 8025 (SCJ)
6. *1523428 Ontario Inc. / JB&M Walker Ltd. v TDL Group*, 2018 ONSC 5886*Fracassi v Cascioli,* 2011 ONSC 178
7. *Fracassi v Cascioli*, 2011 ONSC 178
8. *Urbancorp Cumberland 2 GP Inc., (Re)*, 2017 ONSC 7649 (CanLII)
9. *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 SCR 27
10. *Schnarr v Blue Mountain*, 2018 ONCA 313
11. *Ernst & Young Inc. v Essar Global Fund Limited*, 2017 ONCA 1014
12. *Smith v Pricewaterhousecoopers Inc.*, 2013 ABCA 288
13. *Montor Business Corp. (Trustee Of) v Goldfinger*, 2011 ONSC 2044
14. *Martellacci, Re*, 2014 ONSC 5188
15. *Bell Canada International Inc., Re*, 2003 CarswellOnt 4537 (Ont SCJ)
16. *1175777 Ontario Ltd. v Magna International Inc.*, 2007 CarswellOnt 4135
17. *MacKinnon v MacKinnon*, 2010 ONSC 2661
18. *Hawkins v Hawkins Estate,* 2015 ONSC 1106
19. *New Solutions Extrusion Corporation v Gauthier*, 2010 ONSC 1897
20. *Clarkson Co. v Chilcott*, 1984 CarswellOnt 187 (Ont CA)
21. *Bre-X Minerals Ltd., Re*, 2001 ABCA 255
22. *Katz, Re*, 2013 ONSC 4543
23. *Re, Doman Industries Ltd. (Trustee of)*, 2003 BCSC 376

SCHEDULE "B"

TEXT OF STATUTES, REGULATIONS & BY - LAWS

Companies' Creditors Arrangement Act, RSC 1985, c C-36

***Application of sections 38 and 95 to 101 of the* Bankruptcy and Insolvency Act**

36.1 (1) Sections 38 and 95 to 101 of the *Bankruptcy and Insolvency Act* apply, with any modifications that the circumstances require, in respect of a compromise or arrangement unless the compromise or arrangement provides otherwise.

Interpretation

(2) For the purposes of subsection (1), a reference in sections 38 and 95 to 101 of the *Bankruptcy and Insolvency Act*

(a) to "date of the bankruptcy" is to be read as a reference to "day on which proceedings commence under this Act";

(b) to "trustee" is to be read as a reference to "monitor"; and

(c) to "bankrupt", "insolvent person" or "debtor" is to be read as a reference to "debtor company".

Bankruptcy and Insolvency Act, RSC 1985, c B-3

Proceeding by creditor when trustee refuses to act

38 (1) Where a creditor requests the trustee to take any proceeding that in his opinion would be for the benefit of the estate of a bankrupt and the trustee refuses or neglects to take the proceeding, the creditor may obtain from the court an order authorizing him to take the proceeding in his own name and at his own expense and risk, on notice being given the other creditors of the contemplated proceeding, and on such other terms and conditions as the court may direct.

Transfer to creditor

(2) On an order under subsection (1) being made, the trustee shall assign and transfer to the creditor all his right, title and interest in the chose in action or subject-matter of the proceeding, including any document in support thereof.

Benefits belong to creditor

(3) Any benefit derived from a proceeding taken pursuant to subsection (1), to the extent of his claim and the costs, belongs exclusively to the creditor instituting the proceeding, and the surplus, if any, belongs to the estate.

Trustee may institute proceeding

(4) Where, before an order is made under subsection (1), the trustee, with the permission of the inspectors, signifies to the court his readiness to institute the proceeding for the benefit of the creditors, the order shall fix the time within which he shall do so, and in that case the benefit derived from the proceeding, if instituted within the time so fixed, belongs to the estate.

[…]

Transfer at undervalue

96 (1) On application by the trustee, a court may declare that a transfer at undervalue is void as against, or, in Quebec, may not be set up against, the trustee — or order that a party to the transfer or any other person who is privy to the transfer, or all of those persons, pay to the estate the difference between the value of the consideration received by the debtor and the value of the consideration given by the debtor — if

(a) the party was dealing at arm's length with the debtor and

(i) the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and that ends on the date of the bankruptcy,

(ii) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, and

(iii) the debtor intended to defraud, defeat or delay a creditor; or

(b) the party was not dealing at arm's length with the debtor and

(i) the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and ends on the date of the bankruptcy, or

(ii) the transfer occurred during the period that begins on the day that is five years before the date of the initial bankruptcy event and ends on the day before the day on which the period referred to in subparagraph (i) begins and

(A) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, or

(B) the debtor intended to defraud, defeat or delay a creditor.

Establishing values

(2) In making the application referred to in this section, the trustee shall state what, in the trustee's opinion, was the fair market value of the property or services and what, in the trustee's opinion, was the value of the actual consideration given or received by the debtor, and the values on which the court makes any finding under this section are, in the absence of evidence to the contrary, the values stated by the trustee.

Meaning of *person who is privy*

(3) In this section, a ***person who is privy*** means a person who is not dealing at arm's length with a party to a transfer and, by reason of the transfer, directly or indirectly, receives a benefit or causes a benefit to be received by another person.

[…]

Inquiry into dividends and redemptions of shares

101 (1) Where a corporation that is bankrupt has paid a dividend, other than a stock dividend, or redeemed or purchased for cancellation any of the shares of the capital stock of the corporation within the period beginning on the day that is one year before the date of the initial bankruptcy event and ending on the date of the bankruptcy, both dates included, the court may, on the application of the trustee, inquire

into the transaction to ascertain whether it occurred at a time when the corporation was insolvent or whether it rendered the corporation insolvent.

Limitations Act, 2002, SO 2002, c 24, Sch B

Basic limitation period

4 Unless this Act provides otherwise, a proceeding shall not be commenced in respect of a claim after the second anniversary of the day on which the claim was discovered. 2002, c. 24, Sched. B, s. 4.

Discovery

5 (1) A claim is discovered on the earlier of,

(a) the day on which the person with the claim first knew,

(i) that the injury, loss or damage had occurred,

(ii) that the injury, loss or damage was caused by or contributed to by an act or omission,

(iii) that the act or omission was that of the person against whom the claim is made, and

(iv) that, having regard to the nature of the injury, loss or damage, a proceeding would be an appropriate means to seek to remedy it; and

(b) the day on which a reasonable person with the abilities and in the circumstances of the person with the claim first ought to have known of the matters referred to in clause (a). 2002, c. 24, Sched. B, s. 5 (1).

Presumption

(2) A person with a claim shall be presumed to have known of the matters referred to in clause (1) (a) on the day the act or omission on which the claim is based took place, unless the contrary is proved.

Consolidated Practice Direction Concerning the Commercial List

Part III: Judges, Court Officials, Courtrooms and General Procedures
[…]

5. Cooperation, communication and common sense shall continue to be the principles of operation of the 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 COMPROMISE OR ARRANGEMENT OF SEARS CANADA INC., 9370-2751 QUEBEC INC., 191020 CANADA INC., THE CUT INC., SEARS CONTACT SERVICES INC., INITIUM LOGISTICS SERVICES INC., INITIUM COMMERCE LABS INC., INITIUM TRADING AND SOURCING CORP., SEARS FLOOR COVERING CENTRES INC., 173470 CANADA INC., 2497089 ONTARIO INC., 6988741 CANADA INC., 10011711 CANADA INC., 1592580 ONTARIO LIMITED, 955041 ALBERTA LTD., 4201531 CANADA INC., 168886 CANADA INC., and 3339611 CANADA INC.

Court File No. CV-17-11846-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST
PROCEEDING COMMENCED AT
TORONTO

RESPONDING FACTUM OF CERTAIN FORMER DIRECTORS OF SEARS CANADA INC.

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