Court File No. CV-09-8122-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE

BETWEEN:

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 INDALEX LIMITED, INDALEX HOLDINGS (B.C.) LTD., 6326765 CANADA INC. and NOVAR INC.

the Applicants

RESPONDING FACTUM BOOK OF AUTHORITIES OF THE UNITED STEELWORKERS (Motion Returnable August 28, 2009)

August 27, 2009

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6. *Textron Financial Canada Ltd. v. Beta Brands Ltd.,* 12 P.P.S.A.C. (3d) 46, 37 C.B.R. (5th) 107
7. *Re Ted LeRoy Trucking Inc.,* 2009 BCCA 205

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Froese v. Montreal Trust Co. of Canada

Irvin J. Froese (Plaintiff / Appellant) and Montreal Trust Company of Canada (Defendant / Respondent) and 99319 B.C. Ltd., et al. (Third Parties) and George E. Allan, et al. (Fourth Parties)

British Columbia Court of Appeal

McEachern C.J.B.C., Gibbs and Williams JJ.A.

Heard: January 11, 12, 1996
Judgment: May 22, 1996
Docket: Vancouver CA020009

Counsel: I.G. Nathanson, Q.C., and G.B. Gomery, for appellant.

J.H. Shevchuk and M.E. Currie, for respondent.

Subject: Corporate and Commercial; Estates and Trusts; Contracts

Pensions.

Trusts and Trustees --- Powers and duties of trustees -- Standard of care.

Trusts and trustees -- Powers and duties of trustees -- Duties -- Trust company administering employee pension fund under contract with employer -- Employer stopping funding but trust company not making inquiries for four years -- Trust company realizing pension underfunded and implementing employer's advice to reduce benefits -- Trial judge dismissing employee's action against trust company as no duties owed to employee -- Majority of Court of Appeal finding trust company failing in duty to employee by not responding to lack of funding, not informing beneficiaries and not obtaining legal advice before reducing benefits.

Contracts -- Parties to contract -- Privity -- Third party beneficiary -- Cestui que trust -- Trust company administering employee pension fund under contract with employer -- Employer stopping funding but trust company not making inquiries for four years -- Trust company realizing pension underfunded and implementing employer's advice to reduce benefits -- Trial judge dismissing employee's action against trust company as no duties owed to employee -- Majority of Court of Appeal finding trust

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company unable to rely on contract to escape liability to beneficiaries and allowing employee's appeal.

The plaintiff's employer had maintained a pension plan for the benefit of its employees. The plan was administered by the defendant trust company and managed by an investment company. The function of the trust company was essentially to receive contributions from the employer and issue cheques to retired employees. It did not make investment decisions with respect to the pension fund. The plaintiff received an enriched pension based on an early retirement agreement. The plan was put into a deficit position by a stock market crash. Soon afterward, the employer ceased making regular contributions to the plan. Although the trust company was aware that the employer was no longer making contributions, it took no action with respect to the integrity of the pension fund until four years had passed. At that time, it consulted the employer's actuary due to concerns about the underfunding of the plan. The actuary prepared a report stating that all pension payments would have to be reduced to a 70 per cent level. The actuary also determined that the plaintiff had been improperly receiving an enhanced pension. That conclusion was based on a misunderstanding of plan documentation. The trust company, as a party to the plan documentation, ought to have recognized the error. Instead, it acted on the actuary's report without any further review or legal advice. It reduced all pensions, including the plaintiff's. It also instituted a clawback of the alleged overpayments. The effect was to reduce the plaintiff's monthly pension from $2,600 to $600. The trust company then transferred the pension fund to a life insurance annuity that would make the reduced payments. The plaintiff sued for damages for negligence and breach of fiduciary duty. The trust company relied on certain provisions of the agreement between itself and the employer that allegedly exonerated it from liability. The trial judge found that had the plan been wound up within one year of the employer starting to miss contributions, the assets of the pension fund would have been sufficient to cover future obligations. The judge also found, however, that the trust company had not failed in any alleged duty to the plaintiff. The plaintiff appealed.

Held:

Appeal allowed.

Per McEachern C.J.B.C. (Williams J.A. concurring): The trust company owed a common law duty to beneficiaries of the pension plan such as the plaintiff to recognize warning signals that the pension fund was in danger. The employer's failure to make contributions was such a warning signal. The trust company should have made further enquiries and warned the beneficiaries of the problem. For reasons of privity of contract, the exoneration provisions of the agreement between the employer and the trust company could not assist the trust company against the plaintiff. Further, the trust company did not act with sufficient care when it accepted the actuary's report, reduced the plaintiff's pension on questionable grounds and placed the assets of the pension fund out of the plaintiff's reach. At the least, the trust company should have obtained legal advice on the plaintiff's true entitlement. The question of damages should be remitted to the trial judge to consider questions of mitigation or contributory negligence, in that it appeared that the plaintiff had become aware at some point of the plan underfunding through his own sources.

Per Gibbs J.A. (dissenting): The trial decision had proceeded on the wrong basis. The analysis should have commenced with the agreement between the plaintiff and the employer, which gave rise to no duties to employees on the part of the trust company. The employer retained control of the pension plan. The trust company was merely a custodian. Custodial trustees do not have common law duties such as those alleged by the plaintiff.

Cases considered:

Considered by McEachern C.J.B.C.:

Bartlett v. Barclays Bank Trust Co., [1980] 1 All E.R. 139 (Ch. Div.) -- considered

Fales v. Canada Permanent Trust Co. (1976), [1977] 2 S.C.R. 302, [1976] 6 W.W.R. 10, 11 N.R. 487, (sub nom.

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Wohlleben v. Canada Permanent Trust Co.) 70 D.L.R. (3d) 257 -- applied

Ford v. Laidlaw Carriers Inc. (1993), 50 C.C.E.L. 165, 1 C.C.P.B. 97, 1 E.T.R. (2d) 117, reversed in part (November 24, 1994), Doc. CA C17485, C18697, C18738 (Ont. C.A.) [leave to appeal to S.C.C. refused (1995), 191 N.R. 400, 88 O.A.C. 160] -- considered

Galmerrow Securities Ltd. v. National Westminster Bank (December 20, 1993), Harmon J. (Ch. Div.) -- considered

London Drugs Ltd. v. Kuehne & Nagel International Ltd. (1992), [1993] 1 W.W.R. 1, 43 C.C.E.L. 1, 13 C.C.L.T. (2d) 1, 73 B.C.L.R. (2d) 1, 97 D.L.R. (4th) 261, [1992] 3 S.C.R. 299, (sub nom. London Drugs Ltd. v. Brassart) 143 N.R. 1, 18 B.C.A.C. 1, 31 W.A.C. 1 -- applied

Merrill Petroleums Ltd. v. Seaboard Oil Co. (1957), 22 W.W.R. 529 (Alta. T.D.) [affirmed (1958), 25 W.W.R. 236 (Alta. C.A.)] -- referred to

Metropolitan Toronto Pension Plan v. Aetna Life Assurance Co. of Canada (1992), 98 D.L.R. (4th) 582 (Ont. Gen. Div.) -- considered

Schmidt v. Air Products of Canada Ltd., 3 C.C.P.B. 1, 4 C.C.E.L. (2d) 1, 3 E.T.R. (2d) 1, 20 Alta. L.R. (3d) 225, C.E.B. & P.G.R. 8173, [1994] 8 W.W.R. 305, [1994] 2 S.C.R. 611, 115 D.L.R. (4th) 631, (sub nom. Stearns Catalytic Pension Plans, Re) 168 N.R. 81, 155 A.R. 81, 73 W.A.C. 81 -- applied

Considered by Gibbs J.A.:

Fales v. Canada Permanent Trust Co. (1976), [1977] 2 S.C.R. 302, [1976] 6 W.W.R. 10, 11 N.R. 487, (sub nom. Wohlleben v. Canada Permanent Trust Co.) 70 D.L.R. (3d) 257 -- considered

Merrill Petroleums Ltd. v. Seaboard Oil Co. (1957), 22 W.W.R. 529 (Alta. T.D.) [affirmed (1958), 25 W.W.R. 236 (Alta. C.A.)] -- considered

Schmidt v. Air Products of Canada Ltd., 3 C.C.P.B. 1, 4 C.C.E.L. (2d) 1, 3 E.T.R. (2d) 1, 20 Alta. L.R. (3d) 225, C.E.B. & P.G.R. 8173, [1994] 8 W.W.R. 305, [1994] 2 S.C.R. 611, 115 D.L.R. (4th) 631, (sub nom. Stearns Catalytic Pension Plans, Re) 168 N.R. 81, 155 A.R. 81, 73 W.A.C. 81 -- considered

Statutes considered:

Pension Benefits Act, R.S.O. 1990, c. P.8 -- considered

Pension Benefits Standards Act, S.B.C. 1991, c. 15 -- considered

Trustee Act, R.S.B.C. 1979, c. 414 -- considered

Appeal from judgment of Fraser J., 8 B.C.L.R. (3d) 262, 19 B.L.R. (2d) 88, 8 C.C.P.B. 316, dismissing action by pension plan beneficiary against plan trustee.

***McEachern C.J.B.C.* (*Williams J.A.* concurring):**

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Introduction

1 The plaintiff began his employment with Johnson Terminals Limited, "the Company", in 1949. In 1959, the Company established a pension plan ("the plan") for some of its employees, and thereafter, the Company and those employees began making contributions to the plan.

2 Montreal Trust, "the defendant", accepted the responsibilities of "Trustee" of the plan under a Trust Agreement and Declaration of Trust ("the agreement"). The plan was made a part of the agreement. The Company and the defendant were parties to the agreement, although the participating employees, the *cestui trustent* or beneficiaries, were not. The agreement originally appointed the defendant as investment manager of the plan but it was replaced in this function in 1985.

3 In 1983, by an amendment ("P-7") to the plan, the Company adopted an early retirement program which provided for "improved" or "enriched" pensions for designated employees, one of whom was the plaintiff.

4 The plaintiff retired on June 30, 1986, and was allocated an improved pension of $2,584 per month.

5 Company contributions for regular, current pensions became irregular after August, 1986, although a substantial payment of $30,000 was made in November, 1987. At the end of 1986, the Company substantially ceased making its required additional contributions for enriched, early retirement pensions.

6 The following tables disclose the irregular nature of Company contributions to these two kinds of pensions.

REGULAR EMPLOYER'S CURRENT SERVICE CONTRIBUTIONS

	Jan	Feb	March	April	May	June
1986		14,108	7,054	7,054		7,054
1987						
1988						
1989						
1990		1,229	1,229	1,229		

	July	Aug	Sep	Oct	Nov	Dec
1986	14,058	7,054			7,054	
1987				2,374.50<*>		
1988				No st.	30,000	No St.

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1989	1,229	1025.20	1,229	2,458	1,229	1,229
1990						

<*> Does not appear on Document #79

EMPLOYER'S CURRENT SERVICE CONTRIBUTIONS FOR EARLY RETIREMENT

	Jan	Feb	March	April	May	June
1986	7,054	4,225	8,450	4,225	4,225	4,225<*>
1987		1,920.25			2,011.89	1,005.92
1988						
1989					2,458	
1990						

	July	Aug	Sep	Oct	Nov	Dec
1986	4,225	4,225	4,225		4,225	10,370.25
1987	1,005.92					
1988				No st.		No St.
1989						
1990						

<*> Not shown in Doc. #79

7 The defendant did not react in any way to the Company's failure to make regular contributions; indeed, it continued to make monthly pension payments and to permit other withdrawals from the fund. Ultimately, in 1992, the pension plan had to be wound up; by that time, however, there was a serious shortfall. Existing regular pensions were actuarially pegged at 70%. The actuary recommended, however, that the reduction for enriched pensions be calculated not from the awarded amount, but rather from the amount the pension would have been without enrichment, and that extra payments already made be "clawed back". As a result, the plaintiff's pension was reduced from $2,584.84 to $555.63. Although he dismissed the action, the trial judge held that there were no grounds for these additional deductions, and that the plaintiff should have received 70% of his enriched pension.

8 As the Company is insolvent, the plaintiff brought this action, for breach of duty and in tort, against the defendant only. The

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plaintiff asserts that he is entitled to recover the full amount of his pension from the defendant, alleging that the defendant is liable because it failed to warn the beneficiaries of the trust that the company was not making regular contributions and that the plan was at risk. The plaintiff's case, supported by a finding of the trial judge, is that up to the end of 1988, there were sufficient funds to provide full pensions under the plan. This finding was:

> I accept as accurate that, had the pension plan been wound up in 1987 or 1988, all the beneficiaries would have continued to receive their full pensions.

9 Instead, because the defendant took no action until 1992, the fund continued to be bled by payments and withdrawals until beneficiaries only received 70% of their pensions after enrichments were "clawed back".

10 In the alternative, the plaintiff claims damages for the defendant's failure to ensure that he would receive at least 70% of his pension.

11 The trial judge dismissed the action, largely on the ground that the defendant's role was a limited one, and that the terms of the agreement and the context in which the defendant acted, made it unnecessary for it to act prudently.

12 There can be little doubt that the terms of the agreement governed the relationship between the Company and the defendant. The plaintiff argues that his pension entitlement and the defendant's obligations to him are governed by the general law, which imposes a duty of care. The legal issue is: did the defendant owe duties to the beneficiaries additional to those imposed upon it by the agreement?

13 The basic document establishing the pension trust is the agreement which was called "Agreement and Declaration of Trust". The only parties are the Company and the defendant who is described as "the Trustee." However, the whole purpose for which the "Agreement and Declaration of Trust" were entered into, was for the benefit of the employees in their retirement years. The pension plan is attached to, and forms part of, the agreement. The second and fourth preambles of the agreement provide:

> AND WHEREAS under the Plan certain funds will be contributed to the Trustee, which funds as and when received by the Trustee will *constitute a trust fund to be held for the benefit of the members in the Plan or their beneficiaries*; (emphasis added)
>
> . . . . .
>
> AND WHEREAS the Company desires the Trustee to hold and administer such funds and the Trustee is willing to hold and administer such funds pursuant to the terms of this agreement;

14 Clause 11 of the Plan provides:

> **Company Contributions**
>
> 11. The Company shall from time to time but not less frequently than annually, contribute such amounts as are not less than those certified to by an Actuary as necessary to provide for payment of the pension benefits accruing to members during the current year pursuant to the Plan and shall make provision for the proper amortization of any initial unfunded liability or experience deficiency with respect to benefits previously accrued to the credit of members after taking into account the assets of the Fund, the contributions of the members during the year and such other factors as may be deemed relevant.

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15 The agreement also included numerous defendant's "exonerations":

> **Article First**
>
> The Trustee shall not be responsible for the collection of any funds required by the Plan to be paid to the Trustee.
>
> **Article Second**
>
> The Trustee shall be under no liability for any payment made by it pursuant to the direction of the Company certified to be in accordance with the terms of the Plan and shall not be under the duty of making inquiries with respect to whether any payment directed by the Company is made in pursuance of the provisions of the Plan.
>
> **Article Eighth**
>
> No person other than the Company may ... bring any action against the Trustee with respect to the said trust and/or its actions as Trustee.
>
> **Article Ninth**
>
> [T]he Trustee ... shall [not] be responsible for the adequacy of the Trust Fund to meet and discharge any and all payments and liabilities under the Plan.
>
> **Article Twelfth**
>
> This trust and Agreement may be terminated at any time by the Company and upon the termination of the trust and Agreement or upon the dissolution or liquidation of the Company the Trust Fund shall be paid out by the Trustee as directed by the Company ....

16 Originally, the defendant was the investment manager as well as the custodian of the fund. On May 31, 1985, the former function was transferred to another investment manager. After that time and until the winding-up in 1992, the defendant's role as administrator of the plan was to receive payments, follow investment directions, honour directions made by the Company for the payment of pension benefits, keep track of contributions, and generally keep the fund safe.

17 On May 27, 1985, the defendant received a copy of an internal Company memorandum which stated the Special Early Retirement Plan had created a liability which required an additional monthly Company pension contribution of $4,654 over the next 15 years. This obligation arose from generously enriched early pensions. Other similar memoranda were also received by the defendant.

18 The trial judge found that in 1986, and in later years, "the contributions of the Company to the pension fund were sharply reduced." As shown by the tables reproduced above, this "reduction" related not just to the extra contributions already mentioned, but also to the regular required contributions. There were practically no company contributions in 1987 and thereafter. There is evidence that this failure was not discovered by the defendant, but rather that it was brought to the defendant's attention by the actuary in August, 1991. The actuary reported in 1992 that:

> The last actuarial valuation made on an on-going basis was made as at January 1, 1986 and showed an unfunded actuarial liability of about $520,000. Our estimate of the increased actuarial liabilities as a consequence of the early re-

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> tirement program was about $914,000 as at January 1, 1986 and other sources of gain and loss (notably higher than expected investment earnings) partially offset the costs of the early retirement program.
>
> . . . . .
>
> We understand from discussions with the Company that, although some Company contributions were made following the delivery of our actuarial valuation report to the Company in December, 1986, the Bank of B.C. called its loans to the Company in July of 1987, in the amount of some $16 million and placed a monitor in the Company (until July 1988), and that the Company was during this period permitted to only pay the expenses to operate the Company in order to commence the liquidation of various corporate assets. *During this period no Company contributions were made and to the best of our knowledge and understanding, no Company contributions have been made since July, 1987.* (emphasis added)

19 The evidence discloses that these statements were substantially correct, although one payment of $2,458 was made in May, 1989.

20 The trial judge made this finding:

> Since Montreal Trust kept track of both company and employee contributions, it must be taken to have been aware of the fluctuations of the company contributions.

21 With respect, one could just as easily read "cessation" for "fluctuations" of Company contributions.

22 I regard the above finding as crucial because it fixes the defendant with knowledge that contributions were not being made. The defendant had knowledge of the money going out of the fund, because it was writing the cheques. In addition, as custodian, the defendant could not have been unaware of a substantial loss suffered by the fund in the late 1987 stock market crash which was internationally notorious.

23 The trial judge made a number of findings favourable to the defendant. These include:

> From 1985, Montreal Trust says, it was on the outside, with no meaningful obligations to the beneficiaries and with no knowledge and no means of knowing whether the plan was healthy. It is true that the functions of Montreal Trust from 1985 were clerical and might as easily have been carried out by a bookkeeper with a cheque writing machine as by a big trust company.
>
> . . . . .
>
> Since Montreal Trust kept track of both company and employee contributions, it must be taken to have been aware of the fluctuations of the company contributions. However, I am unable to find that Montreal Trust was in a position to recognize the implications of them. First, the company was entitled to take contribution holidays under the terms of the plan. That it did so was not necessarily sinister. Secondly, the level of company contributions was not on its face significant. The object of the managers of a pension plan of this kind is to keep it in a position where its assets are sufficient to cover present and future liabilities. This is where the actuary comes in: it sets the level of employer contributions.
>
> Analyzing the viability of a pension fund is an inexact exercise, involving much prediction. Short-term fluctuations in the value of the fund may be tolerable. Additionally, depending on the attrition rate among potential beneficiaries and

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> changes in the employment structure of the company, fairly large employer contribution fluctuations may not be in themselves meaningful. Montreal Trust did not have a context in which what it knew or ought to have known was recognizably a warning signal: in particular, it was not privy to the periodic reports of the actuary.
>
> . . . . .
>
> ... Montreal Trust was not managing the trust fund. In the discharge of the very limited duties it carried out after 1985, there was no scope for -- and, hence no obligation to undertake -- the exercise of prudent judgment.

24 The judge suggested that the Company was entitled to take "contribution holidays" under the terms of the plan and that therefore there was no reason for suspicion when the Company failed to make regular payments. The real facts are disclosed in the actuaries' draft report, Ex. 36, which states:

> The liabilities created by these early retirements were, in fact, met from excess investment earnings during 1986 and the first half of 1987. During 1986, excess investment earnings amounted to $336,000. In the first half of 1987, the gain from excess investment earnings was $787,000. Thus, at June 30, 1987 there was an estimated surplus of $15,000. Part IV of the Plan text was then drafted to provide additional benefits to several executives. The October 1987 stock market crash placed the Plan in a significant deficit and the Plan has never recovered since then.

25 The trial judge found that the defendant did not have the benefit of these valuations, but this lack of information, in my view, works against the defendant because it emphasizes the importance of known missed contributions. As will be seen, however, the defendant did in fact have sufficient information to permit it as a prudent administrator to recognize the serious risk facing the beneficiaries.

26 The trial judge further found that the level of Company contributions may not have been significant because the defendant might assume that the contribution shortfall would be covered by investment income. Even in "buoyant" economic times, however, the Company's failure to make required contributions should have been a danger signal to a prudent trustee. It is difficult to imagine a more significant indication of trouble than the virtual termination of contributions from the principal contributor to the plan. There is no evidence the defendant noticed this failure or that it made any inquiries. Even though "Article First" provides that the Trustee is not responsible for the collection of any funds required to be paid to the Trustee, that should not exonerate the Trustee from making inquiries as to why contributions from the principal contributor to the Plan had not been made.

27 The judge concluded that the defendant did not have a "recognizable warning signal." It is difficult to accept this finding. It is based upon the view that the defendant did not have notice of or access to the entire pension picture. With respect, that is only a part of the analysis. The train engineer who misses a signal is not excused because he did not know there was another train on the track. The defendant in this case missed warning signals for regular contributions from August, 1986, to the end of 1988, and for enriched contributions during most of 1987 and 1988. Even if the defendant did not know the entire pension equation, did its knowledge of the Company's failure to make required contributions give rise to any duty on the part of the defendant to take steps to protect the interests of the beneficiaries? In my view, that question can only be answered in the negative if the judge was right in concluding that the defendant had no obligation to exercise prudence.

28 It must be remembered that throughout this period, the defendant was paying pensions and permitting withdrawals from the fund when contributions required to support them were not being paid. Section 11 of the plan required the defendant, even in its limited role as administrator, to be aware of such matters even if it were oblivious to the losses suffered in the market crash and to the other circumstances of the company. Also, as must be noted, any inquiry into the reason for the missing payments would inevitably have led the defendant to an understanding of the larger circumstances and the dangers facing the beneficiaries. Everything that was later discovered could have been predicted with reasonable accuracy in 1987 or 1988.

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29 This inaction on the part of the defendant fully justifies the judge's finding:

> It seems fair to say that, in the critical years from 1986, no one was taking responsibility for the interests of the employees: not the company, not the actuary and, by its own admission, not Montreal Trust.

Legal Relationships

30 It will be useful to discuss the legal relationships between the parties. This is a question on which there is very little authority but some helpful commentary.

31 In his seminal work, *The Law of Trusts in Canada*, 2nd ed. (Toronto: Carswell, 1984), Professor Donovon Waters foresaw some of the problems that arise in this case. First, in a pension context, starting at p. 104, he distinguished between custodial and managing trustees and suggested, in a footnote, that custodial trustees will usually have duties and liabilities expressly restricted to the building and safekeeping of investment instruments. I assume he includes "building" in this passage because he also suggests that even a custodial trustee may not be able to avoid responsibility for bad investments directed by the investment managers.

32 At p. 438, Dr. Waters predicted great expansion in the use of trust concepts in the pension industry and he commented that "some difficult questions are going to face Canadian legislatures." He concluded that "the indenture is of key importance because it determines the role and duties of the trustee." As will be seen, however, contractual responsibilities to the settlor do not tell the whole story.

33 In considering the future of trusts in Canada, at p. 1145, Dr. Waters observed that "broadly stated principles of equity" will apply to many and varied areas of business and commercial life. As if he knew this case would arise, he suggested, "[t]here is likely to be a call for new formulations of the duty of the trustee to account" but he went on to ask whether, with sometimes thousands of beneficiaries:

> [w]hat sort of accounts ought they therefore to receive, and with what frequency? If accounting takes place to the employer only, there is another nice question as to whether there has been any proper accounting at all. Can it be relevant that it is the *employer* who created the trust, even if it is also the case that the trust is non-contributing on the employer's part? Associated with this issue is the question of information. What information concerning the trust and its investment policies is the trust beneficiary entitled to demand ...

34 Several provinces have recently enacted Pensions benefits legislation. In British Columbia, the *Pension Benefits Standards Act* S.B.C. 1991, c. 15, requires a pension administrator to "act honestly, in good faith and in the best interests of the members and former members and any other persons to whom a fiduciary duty is owed," and to "exercise the care, diligence and skill of a reasonably prudent person under comparable circumstances." The statute specifically states that these requirements exist "in addition to, and not in derogation of, any enactment or rule of law or equity relating to the duties or liabilities of a trustee."

35 There have been some useful commentaries about the Ontario legislation with particular reference to some of the issues that must be decided in this case. I refer particularly to *The Role and Responsibilities of Trustees in Pension Plan Trusts: Some Problems of Trust Law*, by Robert P. Austin in T.G. Youdan, ed., *Equity, Fiduciaries and Trusts* (Toronto: Carswell, 1989), pp. 111- 129; *Legal Issues Arising Out Of The Use of Business Trusts in Canada*, by Maurice C. Cullity Q.C., also in Youdan, pp. 181-204; and *Doing One's Duty: Pension Plan Administrators, Agents and Trustees*, by Patricia J. Myhal, (Sept. 1991) 11 Estates and Trusts Journal, pp. 10-43; and *Record-Keepers or Whistle-Blowers? A Look at the Role of Pension Fund Custodians*, by Dona L. Campbell, (Sept. 1995) 15 Estates and Trusts Journal, pp. 26-47. While I have found these articles most

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helpful, they must be considered in the light of developing jurisprudence, particularly the recent decision of the Supreme Court of Canada in *Schmidt v. Air Products of Canada Ltd.*, [1994] 2 S.C.R. 611, which was decided while the present case was at bar. As stated by Cory J., writing for the majority, at p. 639:

> ... If there has been some express or implied declaration of trust, and an alienation of trust property to a trustee for the benefit of the employees, then the pension fund will be a trust fund.
>
> If no trust is created, then the administration and distribution of the pension fund and any surplus will be governed solely by the terms of the plan ...

36 Further, at p. 643, Cory J. said:

> When a pension fund is impressed with a trust, that trust is subject to all applicable trust law principles.

37 I pause to note that the partially dissenting passage in the judgment of McLachlin J. in *Schmidt*, and the earlier passage from *Merrill Petroleums Ltd. v. Seaboard Oil Co.* (1957), 22 W.W.R. 529 (Alta. T.D.), both quoted by the trial judge, related to ascertaining the terms of the trust, and do not touch upon the question I am considering which is whether there are trust obligations additional to the specific terms of the trust indenture or agreement.

38 I agree, as found by the trial judge, that the Supreme Court of Canada has laid to rest any question about the status of the defendant herein as a "true trustee".

39 I therefore conclude that there is what academics call an "overarching" obligation upon a custodial or administrative trustee to pay attention to the interests of the beneficiaries additional to its contractual duties provided in the trust indenture. This obligation is not unlimited: it arises only within the function assigned to or assumed by the trustee.

40 In her article at p. 32, Ms. Campbell confirms that even a custodial trustee owes a duty of care at common law. I am, however, dubious about the authority of some of her examples, including *Metropolitan Toronto Pension Plan v. Aetna Life Assurance Co. of Canada* (1992), 98 D.L.R. (4th) 582 (Ont. Gen. Div.), which was really a case between contracting parties, and *Ford v. Laidlaw Carriers Inc.* (1993), 50 C.C.E.L. 165 (Ont. Gen. Div), reversed in part by an Endorsement, [1994] O.J. 2663 (C.A.), where the court was critical of a custodian's lack of knowledge about the terms of the plan it was administering, and cited with approval dicta from *Bartlett v. Barclays Bank Trust Co.*, [1980] 1 All E.R. 139 at 152 (Ch. Div.), which stresses the higher duty expected of a professional trustee. In *Ford*, the Court of Appeal did not impose liability upon the administrator, because it corrected its errors before any harm was done, and because the real cause of the loss was a deliberate misrepresentation to the employee-beneficiaries on the part of the Company. However, the trial judgment in that case includes many passages of interest in this case. At p. 238, the trial judge said:

> Since a trustee's fundamental duty and obligation is owed to the beneficiaries, a competent trustee would have advised the employees (beneficiaries) that what Laidlaw was proposing to do was not permitted under the plan.

41 Of special interest in Ms. Campbell's article is her section on the responsibility of custodians to monitor contributions. This is specifically required by the Ontario Act. However, at p. 40, Ms. Campbell comments: "it would be difficult to argue that a pension fund trustee bears no responsibility ...[as part of its duty of care] to monitor the adequacy of contributions and to ensure that required contributions are made to the fund in a timely fashion."

42 Ms. Campbell also raises the question of whether a custodian has any responsibility to "react" to events. She notes that this seems to be indicated in the *Aetna* case, but in a recent English Case, *Galmerrow Securities Ltd. v. National Westminster Bank*,

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suggests its terms should be imposed upon the beneficiaries as if they were parties.

49 Accordingly, I conclude that the beneficiaries should not be treated as parties to the agreement. Counsel did not suggest otherwise.

50 Lastly, returning to what I stated a moment ago, the foregoing does not decide this case against the defendant because its responsibility can only be assessed in a factual context, and legal truth can usually be found only in the details. I turn, therefore, to consider the conduct of the defendant in the circumstances disclosed by the evidence.

The Duty to Warn

51 As already mentioned, the trial judge found that the defendant, because it was not managing the trust fund, had "no scope" for -- and, hence no obligation to undertake -- the exercise of prudent judgment.

52 This case, of course, can be approached from at least two perspectives. First, one can take the approach taken by the trial judge, which was that the agreement alone defined the duties and obligations of the defendant and that, accordingly, the defendant was under no duty to be prudent; if it failed in that connection, it was protected against liability by the many exoneration clauses within the Agreement. The defendant alleges in its factum, and the judge found, that even if it appreciated the significance of the uneven (or absent contributions), it had no express duty, and therefore no obligation, to volunteer information to beneficiaries.

53 If this is the correct approach then I would agree that the plaintiff must fail on this branch of his appeal.

54 The trial judge did not consider the broader approach, that although the plaintiff is not a party to the agreement, duties in trust and tort may arise because of the close financial relationship between the beneficiaries and the defendant. What stands out in this case is that the defendant did not seem to consider or appreciate until 1991 that it had duties which it then described as "fiduciary duties" to the beneficiaries.

55 The question is whether, in these circumstances, the defendant in 1987 and more particularly in 1988, given its state of knowledge, could as a matter of law, fail to advise the beneficiaries that required contributions were not being made. The defendant must have known that if it did not so advise the beneficiaries, it is unlikely anyone else would.

56 For the reasons already mentioned, the defendant's "exonerations" provide no defence to the plaintiff's claim. Was the defendant's duty of care so limited that it was not required to react?

57 The trial judge framed the question as whether there was any obligation to volunteer information to the beneficiary. With respect, I think that is far too narrow. In my view, "true" trustees have obligations of prudence to protect not just the corpus of the trust, but also the interest of the beneficiaries from the ongoing operation of the plan.

58 I postulate a simple example. Assume that the Company appoints an investment manager, and that that manager instructs the trustee to invest the corpus, or so much thereof as the plan permits, in the subordinated securities of the company. (This is an extreme example because most plans provide investment rules that must be followed.) Absent such rules, can it seriously be argued that a trustee owes no larger, general duty of prudence respecting the trust which transcends the four corners of the agreement? In this respect, I agree with the comments of Dickson J. (as he then was) in *Fales v. Canada Permanent Trust Co.* (1976), [1977] 2 S.C.R. 302, at p. 316, although stated in a different context. He said, no matter how wide their discretionary powers:

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> ... a trustee's primary duty is preservation of the trust assets, and the enlargement of recognized powers does not relieve him of the duty of using ordinary skill and prudence, nor from the application of common sense.

59 In my view, there is more involved in this case than volunteering information. In the ordinary course of its contractual responsibility as administrator or custodial trustee, the defendant became aware, as found by the trial judge, that required contributions were not being made. In view of the fact that payments were flowing out of the fund, a prudent administrator, in my view, was required to make inquiries of the Company and possibly of the actuary which would have permitted the defendant to make a prudent decision about what should be done to protect the beneficiaries. The duty of care it owed to the beneficiaries did not permit it to do nothing when the plan was at risk. Simple inquiries would have filled in any gaps that existed in the defendants understanding of the context.

60 Thus, within the scope of its duties as administrator, it is my view that the defendant breached its duty of care to the beneficiaries when it failed to respond to the discontinuance of Company contributions.

61 Once it is concluded that the defendant had a duty to respond to this discontinuance of Company contributions, it follows that the defendant was obliged to inform the beneficiaries that the plan was at risk.

62 A further matter that must be considered is the $30,000 payment made by the Company for regular pensions in November, 1988. It might be argued that this payment supports the views of the trial judge that the Company indeed appeared to be taking a "holiday" and that the defendant, not being required to make collections, was entitled to assume that payments would be made as required.

63 I am unable to accept that view. That payment, except for the $2,374.50 paid in October, 1987, was the first payment for regular pensions since November, 1986, a period of 23 months. At the date of that payment, there had been only four undersized payments for enriched pensions in early 1987, and none in the first eleven months of 1988.

64 In my view, the defendant as a prudent trustee had an obligation to respond appropriately before the $30,000 payment was made.

65 Because he was dismissing the plaintiff's action, the trial judge did not undertake any damages assessment. The plaintiff called an actuary to estimate the plaintiff's loss at $291,216, which includes a past loss, after giving credit for pension payments actually received of $49,904, plus the present value of the future loss, as of the date of trial in March, 1994, of $241,312.

66 On the other hand, the defendant urges that, if necessary, the question of damages ought to be sent back to the trial court because of the need for decisions on the life expectancy of the plaintiff, and on the difficult questions of mitigation or contributory negligence arising because of evidence that the plaintiff knew, or suspected from his own sources, that the plan was underfunded.

67 I agree that this question should be remitted to the trial court. In this judgment, I have pronounced only on the obligation of the defendant to warn the plaintiff of the risks created by the failure of the Company to make required payments. The defendant is not foreclosed from arguing such other defences as it may be advised.

The Winding-Up

68 In the alternative, the plaintiff claims that the defendant failed to protect him during the winding-up of the plan. Specifically, the plaintiff argues that the defendant could not properly appropriate the corpus of the trust to purchase 70% pensions for other members with funds to which he was equally entitled. If the plaintiff succeeds on this ground of appeal, he would be

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returned to the equivalent of a 70% pension.

69 It appears from the evidence that in 1985, the Company was expecting substantial numbers of early retirements consequent upon the downsizing of the company's operations. Accordingly, the advice of the actuary was requested. He drafted an amendment to the plan, called P-9, which specified several kinds of improved benefits and necessary funding requirements. Clause 7 imposed restrictions on the amount of pensions that could be paid, and clause 8 provided that in the event of termination or winding-up, clause 23(c) of the plan (which provides for the distribution of the assets upon "termination" of the entire plan) would apply only:

> ... to that portion of the additional pension benefits which can be financed by the extent of the special payments made in respect of such benefits.

70 If adopted as an amendment to the plan, clause 7 of P-9 might have limited the amount of the plaintiff's pension, and clause 8 would have permitted distribution for enriched pensions, upon a winding-up, only to the extent such enrichments had been funded by special Company contributions. P-9 was not adopted until 1991, however, and clauses 7 and 8 were not included in that amendment. It may have been for this reason that the trial judge found that the plaintiff's original pension was a proper one under the plan.

71 The basis for the plaintiff's reduced pension (below 70%) resulted from a recommendation of Mr. Taylor, the plan's actuary, that the plaintiff's original pension represented an overpayment, and that a drastic "claw-back" was necessary to correct the account. P-9, as originally drafted, was the basis for this recommendation because the actuary concluded, wrongly in the case of the plaintiff, that some of these enriched pensions did not comply with its terms.

72 The trial judge dealt with the merits of this claw-back this way:

> When he [Taylor] decided that Mr. Froese had been overpaid, Mr. Taylor was out of his own field of expertise. The basis for his decision was the absence of formal documentation in the files of Johnston Terminals.
>
> Non-lawyers attach much more significance to "technicalities" than lawyers do, despite popular belief to the contrary. No competent lawyer would have been buffaloed by the state of Mr. Froese's personnel file. The pension of Mr. Froese had gone to the Board of Johnston Terminals, it had been approved, and there was express documentation of that, although certain documents of a standard type were either missing or had never come into existence. The rationale for concluding that Mr. Froese had been overpaid "permitted form to triumph over substance", in the words of the Ontario Court of Appeal in *Truckers Garage Inc. v. Krell.*
>
> I agree with the contention of Mr. Froese that his pension could have passed muster under the applicable laws and regulations.
>
> I conclude that the amount of the original pension was lawful and proper.

73 I accept the judge's conclusions in this respect. As the plaintiff cannot recover his loss from the Company, he must succeed, if at all, against the defendant, who decided to reduce the plaintiff's pension and then to give up the fund, even though it knew that funds deducted from the plaintiff's pension would be used to purchase annuities for other beneficiaries.

74 I next propose to review some of the history leading up to the reduction of the plaintiff's pension and the winding-up on the plan.

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75 A memo dated October 28, 1991, based largely upon information obtained from the actuary, discloses several significant facts which I shall paraphrase as follows:

> 1. The plan was in a deficit position probably since the market crash in [October] 1987;
>
> 2. Prior to 1987, the Company authorized additional payments to select pensioners, including some senior executives, as an inducement for them to retire early. The liability for funding these additional pensions was that of the Company.
>
> 3. The Company did not have resources to contribute the amounts necessary to overcome the deficit, and was suggesting that both the actuary and the defendant had some responsibility in this connection;
>
> 4. The defendant was not anxious to advance any claim against the actuary because his firm was a considerable source of new business for the defendant;
>
> 5. The Company expected that it would have to renege on its commitment to the unfunded pensioners.

76 On November 20, 1991, in another memo, the defendant recognized its own potential liability. It states the purpose of the memo to Head Office "is to formally report to you a potential liability we may have regarding the above mentioned pension plan."

77 In December, 1991, the defendant was expecting calculations from the actuary for the wind-up of the plan. That this question was very much in the mind of the defendant's officers is demonstrated by a letter dated January 15, 1992, from the defendant to the actuary seeking information and asking hard questions. It ends with this statement:

> I would appreciate hearing from you at your earliest convenience regarding these concerns we have expressed. In order for all parties to ensure that any payouts from the Plan are effected in accordance with the provisions of the Plan, we may be required to engage external legal counsel. *As well, we would want to ensure that the funded status of the Plan is clarified to our satisfaction in order to enable us to properly discharge our fiduciary obligations to the Plan Members.* (emphasis added)

78 On January 15, 1992, in a memo to Head Office, the defendant wrote:

> As this issue gets more contentious each day, I think it is time to engage external legal counsel to ensure that the interests of beneficiaries are handled appropriately.

79 On February 4, 1992, the defendant's officers met with the actuary, Mr. Taylor, who advised that certain pensions were enriched between 1985 and 1988, and that while "some of them were proper, others were doubtful and others were probably invalid." Recipients of questioned payments are not identified in this memorandum.

80 The next day, the defendant received a copy of a legal opinion obtained by the Company dated August 23, 1991. This opinion assumed contributions by employees and the Company were suspended as of December, 1988 (which was not true: employees' contributions, as the defendant knew, continued into 1990). Notwithstanding this, the opinion concluded, correctly I think, that the plan had not been terminated. This opinion estimates a $2.5 million shortfall, of which $1 million was attributed to the market crash, and $1.5 million to "unauthorized payments." The evidence does not disclose how this latter amount is calculated. I suspect it relates largely to the payment of enriched pensions and not primarily to alleged miscalculations of original pensions.

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81 On March 20, 1992, the actuary, Mr. Taylor, submitted a comprehensive report which was obviously the basis for the recalculation, reduction and claw-back of the plaintiff's pension. The following comments about the report are necessary.

82 The report states:

> We have estimated that the assets of the plan will be sufficient to only finance 70% of basic pension benefits. The amount of individual reduction will vary, with an estimated reduction of 30% or more, but the final calculations of these reductions will depend on the procedure used to wind-up the plan and, in turn, the wind-up procedure will have to take into account certain aspects of trust law and the plan text. In particular, the wind-up procedure will have to take into account the financial consequences of the corporate downsizing which was effected through the early retirement program. This program commenced in 1983 and, we understand, ended in 1987.

83 The report stated that 36 out of 96 current pensioners were provided with early retirement improvements under either P-7 or P-9, although he discovered that some amendments, prepared in 1985, were not ratified until "a later date". This obviously refers to P-9, which we now know was not adopted until 1991.

84 Under the heading "Company Contributions", it was stated:

> We understand from discussions with the Company that, although some Company contributions were made following the delivery of our actuarial valuation report to the Company in December, 1986, the Bank of B.C. called its loans to the Company in July of 1987, in the amount of some $16 million and placed a monitor in the Company (until July 1988), and that the Company was during this period permitted to only pay the expenses to operate the Company in order to commence the liquidation of various assets. During this period no Company contributions were made and to the best of our knowledge and understanding, no Company contributions have been made since July, 1987.
>
> Despite the suspension of Company contributions from July, 1987 [for early retirement pensions], the pension plan continued to credit benefits for service, and employee contributions continued to be deducted and remitted to the plan trust until December 31, 1988.
>
> Solvency Valuation at June 30, 1987
>
> As a result of the Company only being permitted to pay operating expenses, the Company was concerned as to the solvency status of the plan and instructed us to make an estimated solvency valuation as at June 30, 1987. Based on data supplied to us, which we considered to be reliable, we estimated that the plan had a small surplus on a solvency basis, of about $15,000, and that this surplus had developed primarily because of gains from investment returns up to that date.

85 With apparent regard to Granholm and J. Miller, the report states:

> In the course of a previous review of the plan records and financial statements we identified certain payments that appear to have been made from the plan trust in error, to 2 retired members. These payments involve amounts that were due from the Company to the ex-employee, and this matter is now the subject of discussions between the Company and Montreal Trust. Our solvency valuation has accounted for these payments as amounts due to the plan and trust, and we understand that steps are being taken to recover these over-payments, either through the corporate trustee, Montreal Trust, or by way of a charge against future pension benefit entitlements.
>
> If these over-payments are not recovered, together with investment earnings thereon, this will have an adverse effect

> on retired members over and above our current calculations. Our recommendation on the procedure to be adopted to recover these over-payments is given later. The accumulated value of these over-payments to date is about $200,000.

86 With possible reference to the plaintiff, it is stated:

> In the course of setting out the procedure for wind-up, we requested and were provided in December, 1991 with the personnel files of all of the employees, and have made our best efforts to review those files to determine which pensioners were early retirements, and how the pension benefit improvement was calculated. At this time, some of the individual files show no records of how the calculations were done. A few of the early retirement improvements are not consistent with Amendment P-9 and we are forwarding material on these cases to the Retirement Committee.

87 It is obvious the actuary concluded the plaintiff had been substantially overpaid and this error on his part was carried right through into the wind-up of the plan.

88 On page 8 of the report, the actuary clearly indicates that he believed that P-9 included the missing clause 8, and that all enriched pensions for retirees after January 1, 1983, would be subject to that clause. The defendant must have been aware that this was factually incorrect because, as administrator of the plan, it must have known that clause 8 had never been adopted.

89 Under the heading "Terms of Wind-Up" the actuary stated:

> 3. *Under paragraph 8 of Amendment P-9*, none, or virtually none, of the improvements in pension benefits provided to early retirements has been financed by additional special payments by the Company. *Under clause 8 of this amendment, upon termination or wind-up of the plan, these additional pension benefits will have to be discontinued.*
>
> 4. If the plan is wound-up effective as of December 31, 1988, which is when the plan discontinued future service credits, then, *applying paragraph 8 of Amendment P-9*, all improvements in pension benefits that were paid after that date should now be recovered. This recovery would be by way of implementing a charge on an individual basis against future pension benefits such that the charge has a current actuarial equivalent value of all such payments made since December 31, 1988, accumulated to date at a market rate of interest. (emphasis added)

90 On page 10 of the report, the actuary referred to several outstanding matters that were yet to be resolved, and said a legal opinion would be required "on the final wind-up of the plan". "Correspondingly," he advised, "it is not possible to finally wind-up this plan until these matters have been resolved or clarified." As will be seen, no such opinion was ever obtained.

91 The report then recommended, as an interim measure, the immediate reduction of pensions to 70% of what would have been paid without enrichment, and a claw-back of payments already made. It also included a recommendation that:

> ... when the plan is finally wound-up, and assuming that the interim measure described above shall be adopted as the final calculation of the future pension benefit entitlements of each member, then the beneficial interests of each member shall be calculated...for winding-up the Plan.

92 Thus, without clause 8 in the amended P-9, it was not necessarily correct, as assumed in the report, that pension improvements would only be payable upon a winding-up to the extent that special funding had been provided.

93 I pause to mention that, in cross-examination, the actuary admitted that the report contained several errors and that it was misleading.

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94 Clause 8 was the basis for reducing *enriched* pensions. In proper cases, a claw-back for *miscalculated* pension payments could be recovered by way of set off. The plaintiff suffered deductions back to a lower level and for a claw-back of benefits paid although there was no reason for him to suffer deductions on either ground.

95 On March 20, 1992, a trust officer of the defendant wrote a memo questioning the accuracy of the actuary's report and its fairness to Granholm and J. Miller. He noted:

> Recovery of pymts [sic] due to errors in original calculations have not been specified.

But nevertheless, he advised:

> I told [the actuary] in principal [sic] the report and method of calculation looked fine. We do have a fiduciary resp. [sic] to the beneficiaries and could not commit without review by our legal counsel.

96 Obviously with prior knowledge of this report, the Company wrote and sent a letter to the plaintiff dated March 19, 1992. This letter (the Douglas letter) enclosed a copy of the report, and advised in part:

> Effective April 1, 1992:
>
> > Basic pension benefits are reduced to 70% of the current amount;
> >
> > For those members who retired before January 1, 1983 and who also received an enhanced pension benefit in addition to their basic pension, the enhanced pension benefit is reduced to 70% of the current amount;
> >
> > For those members who retired after January 1, 1983 and who also received an enhanced pension benefit in addition to their basic pension, the enhanced pension benefit is discontinued. Also for these members, payments of these enhanced pension benefits made since December 31, 1988 are to be recovered by way of a reduction in future pension entitlements. The amount to be recovered is calculated as prior payments of enhanced pension benefits plus interest at 12% p.a. up to October 31, 1991. This amount is then set equal to the estimated market value of an annuity, so as to calculate the amount of reduction needed;
> >
> > Similarly, in cases where any excess payments or miscalculated payments have been identified in the audit, prior payments of this type, plus interest, are to be recovered by way of an additional reduction.

97 Attached to the plaintiff's copy of this letter was a statement showing that his pension should originally have been calculated without improvements; that is, at $1,746 rather than what he had been receiving, namely $2,584. This new pension amount was then reduced by 30% to $1,222.59. In order to recover past improvements, a claw-back of $658.50 was applied, leaving a final pension of $564.09. This letter does not mention winding-up the plan, but that possibility is mentioned in the report.

98 Thus, the report of the actuary, which does not identify the plaintiff except possibly as one whose file had been examined, was adopted by the Company and by the defendant as a valid basis for a recalculation of the plaintiff's pension, a reduction of 30%, and a claw-back, for the reasons already stated. These reasons included both alleged error in the original calculation, and an acceptance that enrichments could not be paid in the forthcoming wind-up because of clause 8 of P-9, which had never been adopted. The recommendations were subject to a detailed legal opinion which was never obtained.

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99 Three days later, on March 23, 1992, the Company delivered a Resolution to the defendant in the following terms:

> **Johnston Terminals & Storage Ltd.**
>
> The Board of Directors reviewed the report dated March 20, 1992, prepared by Mr. Les Taylor of The Wyatt Company regarding wind-up the Pension Plan, a copy of which is attached hereto and forms part of these minutes.
>
> UPON MOTION DULY PROPOSED AND SECONDED IT WAS UNANIMOUSLY RESOLVED THAT the Board accept the recommendations contained in The Wyatt Company report.
>
> UPON MOTION DULY PROPOSED AND SECONDED IT WAS UNANIMOUSLY RESOLVED THAT the Board instruct the Pension Committee to advise Montreal Trust to amend benefit payments to all plan members effective April 1, 1992, in accordance with The Wyatt Company Report and the calculations contained therein.

100 There must have been some accompanying schedule showing the amount of reductions to be paid to individual members because the plaintiff's monthly pension was reduced as of April 1.

101 At this point, the defendant obtained a legal opinion on April 6, 1992. The opinion was based only on the agreement, the plan and amendments, the actuarial report, and the Resolution just quoted. It advised only that, on the basis of the foregoing documents, it would be proper for the defendant to amend benefit payments to all plan members on April 1, 1992, in accordance with the actuarial report and its calculations. The author obviously assumed the correctness of the report, and clearly took a narrow view of the defendant's obligation to the beneficiaries, particularly individual beneficiaries who were being singled out for special treatment. Although the report identified only two retired members (Granholm and J. Miller) who were said to be in receipt of erroneous benefits, the plaintiff's pension entitlement, and possibly that of other pensioners, was also re-calculated. The opinion does not mention the agreement's certification requirement, nor does it purport to advise on the proposed wind-ing-up of the plan.

102 After this, there was period of inactivity. The defendant's attitude is probably summarized by its solicitor, who noted, in a memo to file dated March 31, that the Director's Resolution had "modified" the plan and that, "[U]nder the circumstances, it seems that the only course of action, given the shortfall in the assets of the fund is to do as recommended by the [actuaries'] Report." With respect, I do not agree that the Resolution modified the plan. If it did, it would be invalid because s. 23(a) of the plan protects earned benefits.

103 It is unfortunate that the defendant did not respond in any way to the different and unequal treatment recommended for individual pensioners, or to the larger responsibilities it admitted it owed to the beneficiaries.

104 The plan was finally wound up in July, 1992, by transferring the corpus of the fund to a life insurance company for the purchase of reduced individual annuities. The Company's instruction for the disbursement of the fund is contained in a letter to the defendant dated July 31, 1992:

> Herewith your authorization to disburse funds and follows:
>
> • To Montreal Trust usual management fees to 2 p.m., July 31/92. We do not expect to be charged for your outside legal counsel. You should take into account that there will be no assets in the trust at month-end closing. Please notify Wyatt by fax of your final number.
>
> • To Wyatt, fees to 2 p.m. July 31, 1992, to be notified to you by fax.

> • Refund payments to deferred pensioners, Wyatt will fax to you the amounts. These are to be held in a suspense account, under the same registration number, pending completion of "roll-over" documentation.
>
> • Philips Hager North will not charge for July since there are no month-end closing assets.
>
> Balance of trust at 3 p.m. to be transferred to Standard Life, attention Don Liesch.

105 The procedure for winding-up the plan is specified in s. 23(c) which provides in part:

> **(c) Termination**
>
> The Company may at any time, by resolution of its Board of Directors, terminate the Plan by filing with the Trustee a certified copy of the resolution of the Board of Directors authorizing the termination of the Plan and trust.
>
> . . . . .
>
> When the assets have been allocated as heretofore provided, the Trust Fund shall be terminated. The interests of those members, retired members, former members, their beneficiaries and joint annuitants described in paragraph (ii) shall be paid to a life insurance company to purchase immediate or deferred life annuities, with payments commencing at age sixty-five (65) ...

It is clear, however, that such termination may only be done in accordance with the terms of the Agreement.

106 It is apparent that the plaintiff was wrongly deprived of a substantial part of his pension because no one questioned or checked the conclusions or assumptions of the actuary. The defendant argues that it was not a part of its responsibility to check the calculations made with respect to every beneficiary. In a case such as this, there could be thousands of employees and it would be unreasonable to expect the trustee to descend into that kind of detail.

107 But it is necessary to consider whether the casual approach taken with regard to these drastic measures conformed with the defendant's duty of care. The Company resolution merely adopted the recommendation of the actuary's report, which is expressly stated to be subject to a number of other matters and to a legal opinion that was not obtained, except to the extent already described. The report was singularly lacking in detail about the plaintiff or any beneficiaries for whom re-calculations or claw-backs were being recommended. It appears the defendant accepted without hesitation or inquiry the calculations submitted with the report.

108 After the April 1 reduction in benefits, the actuary explored the purchase of annuities as authorized by s. 23 of the plan, and eventually settled upon a specific insurance company. Except for the letter of instructions, however, neither the Company nor the defendant passed in a formal way upon the final disposition of the fund, or upon the amount of the individual annuities. The defendant acted solely upon the report, the resolution and the Company's letter of instruction. It is unnecessary to consider whether the foregoing was sufficient as between the Company and the defendant. It is another question whether it was sufficient as between the defendant and the beneficiaries. I add that, in my judgment, the April and July directions given to the defendant by the Company were parts of a single scheme to carry out the recommendations of the actuary's interim report which, as I have said, was not a final report, and was manifestly premised incorrectly.

109 The result of all these procedures was to put the fund beyond the reach of the plaintiff whose pension entitlement had been incorrectly and permanently reduced by over $2,000 a month. I say "incorrectly" because of the findings of the trial judge.

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110 The first question is whether the defendant owed any duty of care in connection with the wind-up of the plan. I have no doubt on that question. As administrator of the plan, it was clearly within the area of the defendant's responsibility to ensure that the plan was properly wound up.

111 The second question is whether the defendant breached its duty of care to the plaintiff as a beneficiary during the wind-up of the plan.

112 So far as I can ascertain, the defendant had no authority from the Company to carry out the recommendations of the actuary apart from the March 20, 1992, resolution quoted above, and the directions contained in the letter of July 31, 1992. In fact, at trial, the resolution was the basis upon which the defendant tried to justify what it had done to the plaintiff's pension. The actuary gave this evidence:

> Q Sir, is it your position that the wind-up, the division of assets on wind-up is ultimately justified by the fact that the board of directors approved your report?
>
> A It was then.
>
> Q I see. Was it your position that it really didn't matter what amendment P-9 said?
>
> A No.
>
> Q Did it matter at all that P-9 wasn't enacted if you chose to wind-up the plan?
>
> A I'm sorry, yes.
>
> Q That was your position?
>
> A That was my understanding that, yes, in the actual final adjustment to cheques for April 1st.

113 The defendant's Factum on this appeal states at p. 15:

> In any event, Montreal Trust is protected by the exculpatory language in paragraphs 2,3 and 4 of Clause Ninth. Under paragraph 2, Montreal Trust was entitled to rely upon the Company's resolution and the Wyatt report received in March 1992 and the directions it received in July 1992 to transfer funds to Standard Life. Paragraph 2 also specifically stated that Montreal Trust did not have to make any investigation or inquiry. Paragraph 3 stated that Montreal Trust was not responsible for the adequacy of the Trust Fund to meet and discharge liabilities under the Plan. Paragraph 4 provided more generally that Montreal Trust was only liable if it was negligent or wilfully misconducted itself. The evidence demonstrated that Montreal Trust was not negligent and it did not wilfully misconduct itself.

114 The Trust Agreement provides:

> SECOND: Subject to the provisions of Article THIRD hereof, the Trustee shall from time to time on the written directions of the Company *certified to be in accordance with the terms of the Plan* make payments out of the Trust Fund to such persons in such manner, in such amounts and for such purposes as may be *certified to be in accordance with the terms of the Plan* and upon any such payment being made, the amount thereof shall no longer constitute a part of the Trust Fund.

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(and act upon) these casual, uncertified instructions without question and without prudence.

117 In my view, there was no need for the defendant to make independent inquiries or investigations in order to know that the beneficiaries, or some of them, were at risk. At the very least, the defendant knew or should have known that the report upon which the entire winding-up was based was seriously flawed; it knew the Company was seriously in default and adverse in interest to the beneficiaries; it knew the proposed winding-up amounted to forgiveness of the Company's default; it knew the report recommended and the Company confirmed that the files of individual beneficiaries had been "reviewed" and were being treated differently on questionable legal grounds; it knew no legal opinion had been obtained; it knew, because of the failure of the Company to make required contributions, that the defendant itself might have some responsibility; and it must have observed that the Company had not certified that the alienation of the entire fund in the manner and for the purpose proposed was authorized by the plan.

118 In these circumstances, in my view, it was imprudent and negligent to hand over the fund regardless of the question of certification. The defendant breached its duty of care to the plaintiff when it gave up the fund in these circumstances. I recognize that, as a "real trustee", the defendant was in an impossible position, but that did not permit it arbitrarily to adopt a course of convenience. It was required to be careful and as trustee to maintain an even hand between these obviously conflicting interests. It could not do so by putting the fund out of the reach of beneficiaries it knew were being arbitrarily deprived of substantial parts of their pensions.

119 I test my conclusions by asking what the position of the defendant should be if, as a "real trustee", it had received even a certified direction to hand over the fund for a purpose it knew would put it beyond the reach of the beneficiaries. Breach of trust, or at least negligence, spring immediately to mind. I have no difficulty concluding that the defendant breached its duty of care to the plaintiff and it is not necessary to select just one of those courses of action. The plaintiff is entitled to succeed on both. Such breach, in my judgment, directly caused or contributed to the cause of the losses I have described.

120 I do not say that the defendant was required to check every calculation or to satisfy itself that every member of the plan was treated with perfect correctness, as that might be an impossible task in a large or even medium-size pension plan. A trustee must, however, respond to obvious issues of danger to beneficiaries which were, in this case, easily identified by the defendant upon reading the actuary's report. At the very least, prudence required the defendant to act on the basis of independent, informed advice when it knew from reading the report and the consequent calculations that one or more of the beneficiaries were being deprived of substantial portions of their pensions on highly doubtful grounds. The defendant also had the option of seeking the opinion of the court but there is no suggestion in the evidence that that was ever considered.

121 I have also been concerned by the failure of the plaintiff to take any steps to prevent the dispersal of the fund. His solicitor was in touch with the defendant shortly after March 20, 1992, but nothing further was heard from him. In this respect, however, the report contemplated a legal opinion, and the plaintiff was entitled to assume that such an opinion would be obtained before the plan was wound up as suggested in the report. In any event, the plaintiff was not obliged to bring proceedings prior to the winding-up of the plan.

122 Thus I conclude that the plaintiff is also entitled to succeed on his alternative argument. I suppose it is possible that, but for the reduction and claw-back of the plaintiff's and some other pensions, all other pensions might have been less than 70%. I leave that to counsel to consider. The plaintiff is entitled to have his pension supplemented by an award of damages, either by way of periodic payments, or by a present value lump sum to bring his pension up to 70% (or as may be adjusted) of his original pension.

123 I would not like to leave the impression that custodial trustees will always be subject to liability beyond the terms of the trust agreement. The Trustee does, however, have (and has in law always had) a general duty of care to beneficiaries which, on the facts of this case, was not discharged.

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124 The defendant claims relief under the *Trustee Act*, R.S.B.C. 1979, c. 414. With respect, I would not accede to that application. The defendant contributed in a substantial way to a serious loss suffered by the plaintiff and I would not deprive him of his remedy on a discretionary basis.

125 I would allow the appeal to the extent I have mentioned. I would remit to the trial court the question of whether the plaintiff is entitled to damages for the failure of the defendant to warn him in 1987 or 1988 that his pension was at risk. The plaintiff is entitled to damages at least in an amount sufficient to restore him to a 70% or lesser adjusted pension as directed above.

***Gibbs J.A.* (dissenting):**

126 The appellant seeks reversal of an order in the court below dismissing his claim against the defendant. The third and fourth party proceedings have been severed and are being held in abeyance pending the decision on this appeal.

127 The claim sounds in tort. It is founded upon allegations of breach of duty on the part of Montreal Trust in the administration of a pension fund forming part of a pension plan. The plan was set up by Johnston Terminals Ltd. in July of 1959 and terminated in March of 1992 at a time when there were insufficient funds to meet all of the plan membership entitlements.

128 The plaintiff was receiving a pension when the plan was terminated. On termination his pension was sharply reduced hence this proceeding. He claims compensation from Montreal Trust of approximately $240,000 to restore that to which he says he was entitled and would have enjoyed but for the aforesaid breaches of duty.

129 There is no claim against Johnston Terminals even though it seems clear that failure by Johnston Terminals to maintain an adequate level of employer funding during the latter years of the plan was the direct cause of the plaintiff's loss.

130 Montreal Trust was not a party to the pension plan under which the pension fund was created. But the settlor, Johnston Terminals, made provision in the plan for Montreal Trust to perform functions under contract limited to custody and management of the pension fund including the investment of it in a permitted class of securities:

> **Trust Fund**
>
> 2. All contributions of the members and of Johnston Terminals & Storage Ltd. and of its subsidiary companies as set forth in Exhibit A hereto (hereinafter called "the Company") will be paid into the Trust Fund (hereinafter called "the Fund") established under the terms of the Trust Agreement executed between the Company and Montreal Trust Company and dated July 1, 1959
>
> The Fund will be administered by the Montreal Trust Company until or unless a successor trustee or trustees are appointed. The Trustee shall invest the fund in securities and loans of a class permitted by The Pension Benefits Act, 1967 of Alberta (hereinafter referred to as "the Alberta Act") and any regulations thereunder or any amendment thereto.

131 Johnston Terminals retained all of the other responsibilities for the management and operation of the pension plan. Montreal Trust is not mentioned anywhere else in the plan.

132 Under Clause 11 of the pension plan Johnston Terminals covenanted each year to make a contribution to the pension fund sufficient in amount, when added to the value of the assets of the fund and the employee contributions, to fund the pension

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plan liabilities:

> **Company Contributions**
>
> 11. The Company shall from time to time but not less frequently than annually, contribute such amounts as are not less than those certified to by an Actuary as necessary to provide for payment of the pension benefits accruing to members during the current year pursuant to the Plan and shall make provision for the proper amortization of any initial un-funded liability or experience deficiency with respect to benefits previously accrued to the credit of members after taking into account the assets of the Fund, the contributions of the members during the year and such other factors as may be deemed relevant.

133 As the annual contribution of Johnston Terminals turned in part upon the value of the pension fund assets, the investment performance of the pension fund was of significant interest to Johnston Terminals. Over time it became dissatisfied with the investment performance and finally, on May 23, 1985, it transferred the investment responsibilities from Montreal Trust to M. K. Wong Associates. It is common ground that a precipitous fall in stock market values in October of 1987 had a seriously adverse impact on the value of the assets in the pension fund.

134 With the removal of the investment responsibilities Montreal Trust was left, in terms of the pension plan and at the critical times, only with the obligation to administer the pension fund.

135 After 1986 Johnston Terminals made only sporadic contributions to the pension fund. The fund was not sufficiently endowed to be self funding in the long term although the trial judge found as a fact, not disputed by either party, that there would have been sufficient to meet the plan requirements if the fund had been wound up in 1987 or 1988. Under Clause 23 of the pension plan Johnston Terminals was empowered to terminate the plan and distribute the fund by resolution of the board of directors. That formal termination step was not undertaken until March of 1992.

136 The allegations of breach of duty against Montreal Trust are contained in paras. 6, 17 and 21 of the statement of claim. There are three, all expressed as breach of trust or, alternatively, negligence:

> 1) failure to ensure that the plan was fully funded;
>
> 2) failure to warn plan members of the failure of Johnston Terminals sufficiently to fund, and
>
> 3) purchase of annuities in a reduced amount without the consent of the appellant and knowing of his "claim".

137 Here is the precise text of the relevant paragraphs of the statement of claim:

> 6. By virtue of s. 11 of the Johnston Pension Plan and the defendant's position as trustee, or, in the alternative, the duty of care owed to the plaintiff by the defendant, it was the defendant's obligation:
>
> (1) to take the necessary steps to ensure that the Plan was fully funded or, in the alternative,
>
> (2) to notify the members of the Plan, the cestuis que trustent, including the plaintiff, of Johnston's failure to fund.
>
> . . . . .
>
> 17. The defendant committed a breach of trust, or in the alternative, was negligent, in failing to fulfill its obligations as

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> set out in paragraph 6 above in response to Johnston's failure to fund its Pension Plan after 1986, and as a result, the Plaintiff has suffered loss and damage.
>
> . . . . .
>
> 21. The defendant purchased the annuities in breach of trust or, in the alternative, negligently, without the plaintiff's knowledge or consent, with knowledge of the plaintiff's claim, and thereby made it impossible for the plaintiff to receive from the funds held in trust for the Johnston Pension Plan the amounts the plaintiff was entitled to receive.

138 A significant aspect of these alleged breaches of duty is that none of the three is specifically imposed upon Montreal Trust in either the pension plan or the separate contract between Johnston Terminals and Montreal Trust. It follows that the duties alleged to have been breached must flow from the common law and attach by necessary implication to the duties that are specifically imposed by the trust instrument. It is upon this basis that the appellant rests his case, contending that the pension plan is the trust instrument and, in para. 4 of the statement of claim, that "The defendant [Montreal Trust] is the trustee of the Johnston Pension Plan". However, the liability structure collapses if these latter contentions are not supported by the evidence, and they are not, at least to the extent of rendering Montreal Trust liable.

139 On the evidence this is not a traditional trust case where there is a single trust instrument and a single trustee duty bound to follow the terms of the trust instrument. Here there are two trust instruments each with a scope different from the other and each with its own trustee. At p. 104 of the *Law of Trusts in Canada*, 2 Ed., 1984, Dr. D.W.M. Waters described the relationship when there are two trustees with responsibilities divided between them, as is the case, and in the circumstances present, in the case at bar:

> The custodian trustee is a person, natural or corporate, who is vested with title to the trust property, while the management of the trust is left in the hands of other trustees who are known as the managing trustees. In Canada the term is used in connection with pension or other investment trusts when the portfolio is vested in so-called custodian trustee, but the investment policy and decisions are determined by investment managers or consultants.

140 The Montreal Trust responsibilities were confined by Clause 2 of the pension plan to administration of the trust fund created by contributions. It was, therefore, the custodian trustee vested with title to trust property. The management of the trust (the pension plan) was left with Johnston Terminals which thereby fulfilled the role of managing trustee.

141 It is obvious from this division that the burden on the appellant at trial was to fix Montreal Trust with liability notwithstanding the limited role allotted to it. The appellant sought to discharge the burden by contending that Montreal Trust became trustee of the pension plan by way of incorporation of the pension plan by reference into the separate agreement through the wording of the first recital in the separate agreement:

> WHEREAS the Company has adopted a Profit Sharing Pension Plan for certain of its employees (hereinafter referred to as "the Plan"), a copy of which as amended from time to time is attached hereto and forms a part hereof;
>
> . . . . .

142 The contention cannot be sustained. The reference does no more than fix Montreal Trust with knowledge, constructive or actual, of the terms of the pension plan. It does not purport to impose pension plan trustee (managing trustee) duties upon Montreal Trust. Neither do any of the other provisions of the separate agreement or the pension plan. There are, therefore, no duties specifically allotted by either the separate agreement or the pension plan to Montreal Trust to which the common law duties alleged in the statement of claim to have been breached can attach by necessary implication. The consequence is that the appellant has not, on the evidence, made out the case advanced in the statement of claim. The trial judge came to the same

conclusion although he reached it by a different route, commencing with a misunderstanding of the nature of the appellant's case.

143 It is apparent from para. 9 of his reasons that the trial judge thought that the appellant's case against Montreal Trust was based upon the separate agreement whereas it was not. The claim was made entirely upon the pension plan and the proposition that Montreal Trust was the trustee of the pension plan. There is no mention of the separate agreement in the statement of claim. However, the trial judge's misapprehension about the foundation for the claim led him to analyze the separate agreement and in the process to perform the very useful function of assessing the validity of the alleged breaches of duty against the background of the specific provisions of the separate agreement.

144 The trial judge concluded that he should be guided in his analysis by a passage from the judgment of McLachlin, J. at p. 703 of *Schmidt v. Air Products of Canada Ltd.*, [1994] 2 S.C.R. 611, and by a passage from p. 557 of the judgment of Egbert, J. in *Merrill Petroleums Ltd. v. Seaboard Oil Co.* (1957), 22 W.W.R. 529 (Alta. T.D.).

145 In *Schmidt* McLachlin, J. said:

> The primary rule in construing an agreement or defining the terms of a trust is respect for the intention of the parties or, in the case of a trust, the intention of the settlor. The task of the court is to examine the language of the documents to ascertain what, on a fair reading, the parties intended. Unless there is a legal reason preventing it, the courts will seek to give effect to that intention. The search for an answer to the problem before us must therefore focus primarily on the documents relating to the plans and the intention of the parties, if any, with respect to a surplus arising under a defined benefits plan.

146 Applying the primary construction rule from *Schmidt* there can be no doubt that neither the settlor nor the parties intended Montreal Trust to be trustee of the pension plan. The clear intention was that Montreal Trust would be confined to the role of fiscal agent and that is what the trial judge found Montreal Trust to be after the investment responsibilities were taken away in 1985:

> It is true that the functions of Montreal Trust from 1985 were clerical and might as easily have been carried out by a bookkeeper with a cheque writing machine as by a big trust company. (Para.26)

147 The passage from *Merrill Petroleums* describes the priority sequence of a trustee's duties as between those imposed by the trust instrument and those imposed by general principles of the common law:

> While it is also true that there are certain general obligations imposed by law on any trustee (e.g., the duty not to profit from the trust at the expense of the beneficiaries) the more specific obligations and duties of a trustee are set forth in the instrument creating the trust -- in other words, except for those general duties imposed by law on all trustees, the terms of a trust are to be found within the four corners of the trust instrument. The three-way agreement sets forth in considerable detail the right, duties and obligations of the "operator" or trustee, and the trustee is bound to follow the provisions of this agreement even though the instrument might in some instances run counter to the general law of trusteeship. In other words, the first duty of this trustee (as of all trustees) was to follow implicitly the terms of the trust instrument, and, secondly, to observe those general principles of trustee law which did not run counter to the express terms of the trust.

148 The emphasis in this excerpt is upon the duty of the trustee "to follow implicitly the terms of the trust instrument", and to observe general principles of trustee law which do not "run counter to the express terms of the trust". Although there are no provisions in the separate agreement which impose on Montreal Trust the affirmative duties alleged in the statement of claim to have been breached, some of the provisions are instructive in the sense that they tend to negative the notion of implied duties of

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the kind alleged because such implied duties would "run counter" to express terms in the separate agreement.

149 For example, clause FIRST and the third paragraph of clause NINTH of the separate agreement stand in stark contrast to the alleged duty to ensure that the plan was fully funded:

> FIRST: The Trustee shall receive any contributions paid to it in cash or other property acceptable to it. All contributions so received together with the income therefrom (hereinafter referred to as "the Trust Fund") shall be held, managed and administered pursuant to the terms of this Agreement. *The Trustee shall not be responsible for the collection of funds required by the Plan to be paid to the Trustee.* [Emphasis added]
>
> . . . . .
>
> The Trustee shall not be liable for the proper application of any part of the Trust Fund, if payments are made in accordance with the written directions of the Company certified to be in accordance with the terms of the Plan as herein provided, *nor shall the Trustee be responsible for the adequacy of the Trust Fund to meet and discharge any and all payments and liabilities under the Plan.* All persons dealing with the Trustee are released from inquiry into the decision or authority of the Trustee and from seeing to the application of any moneys, securities or other property paid or delivered to the Trustee. [Emphasis added]

150 And likewise Clause TWELFTH is a complete answer to the alleged breach in respect to the purchase of annuities. Montreal Trust purchased annuities as directed by Johnston Terminals. In so doing it "followed implicitly the terms of the trust instrument" in the words of *Merrill Petroleums*. Clause TWELFTH required it to obey Johnston Terminals instructions:

> TWELFTH: This trust and Agreement may be terminated any time by the Company and upon the termination of the trust and Agreement or upon the dissolution or liquidation of the Company the Trust Fund shall be paid out by the Trustee as directed by the Company subject to the provisions of Article THIRD hereof.

151 As for the alleged breach by way of failure to warn the trial judge was unable to find any such obligation either in law or in equity. Moreover, his findings of fact are to the effect that even if there were such a duty Montreal Trust was not sufficiently informed to be aware of the existence of circumstances which would warrant warnings about the sufficiency of the employer's funding:

> 28 Since Montreal Trust kept track of both company and employee contributions, it must be taken to have been aware of the fluctuations of the company contributions. However, I am unable to find that Montreal Trust was in a position to recognize the implications of them. First, the company was entitled to take contribution holidays under the terms of the plan. That it did so was not necessarily sinister. Secondly, the level of company contributions was not on its face significant. The object of the managers of a pension plan of this kind is to keep it in a position where its assets are sufficient to cover present and future liabilities. This is where the actuary comes in: it sets the level of employer contributions.
>
> 29 Analyzing the viability of a pension fund is an inexact exercise, involving much prediction. Short-term fluctuations in the value of the fund may be tolerable. Additionally, depending on the attrition rate among potential beneficiaries and changes in the employment structure of the company, fairly large employer contribution fluctuations may not be in themselves meaningful. Montreal Trust did not have a context in which what it knew or ought to have known was recognizably a warning signal: in particular, it was not privy to the periodic reports of the actuary.

152 It follows from the above that even on the *Merrill Petroleums* concept of "general principles of trustee law" the allegations of breach in the statement of claim cannot be sustained.

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153 It is unfortunate that this case took a wrong turning in the court below such that the real issues seem to have gone out of focus. As pointed out earlier, the trial judge mistakenly understood the action to be based upon the separate agreement which he regarded as a collection of "exonerations" of Montreal Trust. Consequently, his judgment was not directed first to determining whether the claim had been established and then, only if necessary, considering the "exonerations". Instead he dealt primarily with the "exoneration" provisions and found against the plaintiff. That approach led the appellant to rest two of the three grounds of appeal on what the trial judge decided about the effect of what the appellant referred to as "insulating provisions" (exonerations) in the separate agreement. Only the third ground directly addressed a head of liability advanced in the statement of claim, namely, the failure to warn.

154 With respect to the duty to warn ground the appellant relied heavily upon the description of the duties of a trustee found in *Fales v. Canada Permanent Trust Co.* (1976), [1977] 2 S.C.R. 302. Obviously *Fales* is an important case in the continuing development of the law relating to trustees, but it is of no assistance to the appellant here. What is says applies in the circumstances of this case with full force to the managing trustee of the pension plan, Johnston Terminals, but has no application to Montreal Trust in its limited, subsidiary, custodian trustee capacity.

155 Notwithstanding the confusion which crept into this case, the real issues became apparent on the appeal and were sufficiently and adequately canvassed. In that connection, even though not all of the trial judge's reasoning is germane, he did make valuable findings of fact and draw conclusions which were generally on point and relevant to the allegations of fault in the statement of claim. And he made the correct disposition of the case even though he arrived at the end result by an unorthodox route.

156 The burden was on the appellant in this appeal to demonstrate that he ought to have had judgment in the court below. In my opinion he has failed to discharge that burden and so the appeal must stand dismissed.

157 There is one further observation to be made and that is that nothing in these reasons is to be understood as subscribing to the personal opinions of the trial judge which he saw fit to pronounce in paras. 52 and 53 of his judgment.

Appeal allowed.

END OF DOCUMENT

** Preliminary Version **

Case Name:

BCE Inc. v. 1976 Debentureholders

BCE Inc. and Bell Canada, Appellants/Respondents on cross-appeals;

v.

A Group of 1976 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Manitoba Civil Service Superannuation Board, TD Asset Management Inc. and Manulife Financial Corporation;

A Group of 1996 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Insurance (Canada) Limited, CIBC Global Asset Management Inc., Manitoba Civil Service Superannuation Board and TD Asset Management Inc.;

A Group of 1997 Debentureholders composed of: Addenda Capital Management Inc., Manulife Financial Corporation, Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Wawanesa Life Insurance Company, TD Asset Management Inc., Franklin Templeton Investments Corp. and Barclays Global Investors Canada Limited, Respondents/Appellants on cross-appeals, and

Computershare Trust Company of Canada and CIBC Mellon Trust Company, Respondents, and

Director Appointed Pursuant to the CBCA, Catalyst Asset Management Inc. and Matthew Stewart, Interveners.

And between

6796508 Canada Inc., Appellant/Respondent on cross-appeals;

v.

A Group of 1976 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Manitoba Civil Service Superannuation Board, TD Asset Management Inc. and Manulife Financial Corporation;
A Group of 1996 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Insurance (Canada) Limited, CIBC Global Asset Management Inc., Manitoba Civil Service Superannuation Board and TD Asset Management Inc.;
A Group of 1997 Debentureholders composed of: Addenda Capital Management Inc., Manulife Financial Corporation, Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Wawanesa Life Insurance Company, TD Asset Management Inc., Franklin Templeton Investments Corp. and Barclays Global Investors Canada Limited, Respondents/Appellants on cross-appeals, and
Computershare Trust Company of Canada and CIBC Mellon Trust Company, Respondents, and
Director Appointed Pursuant to the CBCA, Catalyst Asset Management Inc. and Matthew Stewart, Interveners.

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2008 CarswellQue 12595

File No.: 32647.

Supreme Court of Canada

Heard: June 17, 2008;
Judgment: June 20, 2008.
Reasons delivered: December 19, 2008.

Present: McLachlin C.J. and Bastarache*, Binnie, LeBel, Deschamps, Abella and Charron JJ.
(paras. 167)

Appeal From:

ON APPEAL FROM THE COURT OF APPEAL FOR QUEBEC

Corporations and associations -- Companies -- Actions -- Against corporations and directors -- Oppressive conduct -- The debentureholders did not establish that they had a reasonable expectation that the directors of BCE would protect their economic interests by putting forth a plan of arrangement that would maintain the investment grade trading value of their debentures -- Appeals allowed and cross-appeals dismissed -- Canada Business Corporations Act, s. 241.

Corporations and associations -- Companies -- Fundamental changes -- Arrangement -- Although in some circumstances interests that are not strictly legal can be considered under s. 192 of the Canada Business Corporations Act, the debentureholders did not constitute an affected class under s. 192 since only their economic interests were affected by the proposed transaction, not their legal rights, and since they did not fall within an exceptional situation where non-legal interests should be considered -- The plan of arrangement for the purchase of the shares of BCE Inc. must be approved -- Appeals allowed and cross-appeals dismissed -- Canada Business Corporations Act, s. 192.

Appeal from BCE and Bell Canada of a decision from the Quebec Court of Appeal which overturned the trial judge's approval of a plan of arrangement that contemplates the purchase of the shares of BCE Inc. ("BCE") by a consortium of purchasers ("the Purchaser") by way of a leveraged buyout. The plan of arrangement was approved by 97.93 percent of BCE's shareholders, but was opposed by a group of financial and other institutions that hold debentures issued by Bell Canada. These debentureholders sought relief under the oppression remedy under s. 241 of the Canada Business Corporations Act ("CBCA"). They also alleged that the arrangement was not "fair and reasonable" and opposed court approval of the arrangement under s. 192 of the CBCA. The crux of

their complaints is that, upon the completion of the arrangement, the short-term trading value of the debentures would decline by an average of 20 percent and could lose investment grade status. The Quebec Superior Court approved the arrangement as fair and dismissed the claim for oppression. The Court of Appeal set aside that decision, finding the arrangement should not have been approved under s. 192. Since the requirements of s. 192 of the CBCA were not met, the court found it unnecessary to consider the oppression claim. The debentureholders cross-appealed the dismissal of the claims for oppression.

HELD: Appeals allowed and cross-appeals dismissed. In assessing a claim of oppression, a court must determine whether the evidence supports the reasonable expectation asserted by the claimant and whether the reasonable expectation was violated by conduct falling within the terms "oppression", "unfair prejudice" or "unfair disregard" of a relevant interest. Here, the debentureholders did not establish that they had a reasonable expectation that the directors of BCE would protect their economic interests by putting forth a plan of arrangement that would maintain the investment grade trading value of their debentures. The content of the directors' fiduciary duty to act in the best interests of the corporation was affected by the various interests at stake in the context of the auction process and by the fact that they might have to approve transactions that were in the best interests of the corporation but which benefited some groups at the expense of others. The directors considered the interests of debentureholders, and concluded that while the contractual terms of the debentures would be honoured, no further commitments could be made. As for s. 192, to approve a plan of arrangement as fair and reasonable, courts must be satisfied that the arrangement has a valid business purpose, and the objections of those whose legal rights are being arranged are being resolved in a fair and balanced way. Although in some circumstances interests that are not strictly legal can be considered, the debentureholders did not constitute an affected class under s. 192 since only their economic interests were affected by the proposed transaction, not their legal rights, and since they did not fall within an exceptional situation where non-legal interests should be considered.

Statutes, Regulations and Rules Cited:

Canada Business Corporations Act, R.S.C. 1985, c. C-44, s. 102(1), s. 122, s. 122(1)(a), s. 122(1)(b) C s. 192, s. 192(1), s. 192(1)(f), s. 192(3), s. 192(4)(c), s. 239, s. 241, s. 241(2)

Companies Act Amending Act, 1923, S.C. 1923, c. 39, s. 4

Prior History

* Bastarache J. joined in the judgment of June 20, 2008, but took no part in these reasons for judgment.

Subsequent History:

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

Court Catchwords:

Commercial law -- Corporations -- Oppression -- Fiduciary duty of directors of corporation to act in accordance with best interests of corporation -- Reasonable expectation of security holders of fair treatment -- Directors approving change of control transaction which would affect economic

interests of security holders -- Whether evidence supported reasonable expectations asserted by security holders -- Whether reasonable expectation was violated by conduct found to be oppressive, unfairly prejudicial or that unfairly disregards a relevant interest -- Canada Business Corporations Act, R.S.C. 1985, c. C-44, ss. 122(1)(a), 241.

Commercial law -- Corporations -- Plan of arrangement -- Proposed plan of arrangement not arranging rights of security holders but affecting their economic interests -- Whether plan of arrangement was fair and reasonable -- Canada Business Corporations Act, R.S.C. 1985, c. C-44, s. 192.

Court Summary:

At issue is a plan of arrangement that contemplates the purchase of the shares of BCE Inc. ("BCE") by a consortium of purchasers ("the Purchaser") by way of a leveraged buyout. After BCE was put "in play", an auction process was held and offers were submitted by three groups. All three offers contemplated the addition of a substantial amount of new debt for which Bell Canada, a wholly-owned subsidiary of BCE, would be liable. BCE's board of directors found that the Purchaser's offer was in the best interests of BCE and BCE's shareholders. Essentially, the arrangement provides for the compulsory acquisition of all of BCE's outstanding shares. The price to be paid by the Purchaser represents a premium of approximately 40 percent over the market price of BCE shares at the relevant time. The total capital required for the transaction is approximately $52 billion, $38.5 billion of which will be supported by BCE. Bell Canada will guarantee approximately $30 billion of BCE's debt. The Purchaser will invest nearly $8 billion of new equity capital in BCE.

The plan of arrangement was approved by 97.93 percent of BCE's shareholders, but was opposed by a group of financial and other institutions that hold debentures issued by Bell Canada. These debentureholders sought relief under the oppression remedy under s. 241 of the *Canada Business Corporations Act* ("*CBCA*"). They also alleged that the arrangement was not "fair and reasonable" and opposed court approval of the arrangement under s. 192 of the *CBCA*. The crux of their complaints is that, upon the completion of the arrangement, the short-term trading value of the debentures would decline by an average of 20 percent and could lose investment grade status.

The Quebec Superior Court approved the arrangement as fair and dismissed the claim for oppression. The Court of Appeal set aside that decision, finding the arrangement had not been shown to be fair and held that it should not have been approved. It held that the directors had not only the duty to ensure that the debentureholders' contractual rights would be respected, but also to consider their reasonable expectations which, in its view, required directors to consider whether the adverse impact on debentureholders' economic interests could be alleviated. Since the requirements of s. 192 of the *CBCA* were not met, the court found it unnecessary to consider the oppression claim. BCE and Bell Canada appealed the overturning of the trial judge's approval of the plan of arrangement, and the debentureholders cross-appealed the dismissal of the claims for oppression.

Held: The appeals should be allowed and the cross-appeals dismissed.

The s. 241 oppression action and the s. 192 requirement for court approval of a change to the corporate structure are different types of proceedings, engaging different inquiries. The Court of Appeal's decision rested on an approach that erroneously combined the substance of the s. 241 oppression remedy with the onus of the s. 192 arrangement approval process, resulting in a conclusion that could not have been sustained under either provision, read on its own terms. [para. 47] [para. 165]

1. The Section 241 Oppression Remedy

The oppression remedy focuses on harm to the legal and equitable interests of a wide range of stakeholders affected by oppressive acts of a corporation or its directors. This remedy gives a court a broad jurisdiction to enforce not just what is legal but what is fair. Oppression is also fact specific: what is just and equitable is judged by the reasonable expectations of the stakeholders in the context and in regard to the relationships at play. [para. 45] [paras. 58-59]

In assessing a claim of oppression, a court must answer two questions: (1) Does the evidence support the reasonable expectation asserted by the claimant? and (2) Does the evidence establish that the reasonable expectation was violated by conduct falling within the terms "oppression", "unfair prejudice" or "unfair disregard" of a relevant interest? For the first question, useful factors from the case law in determining whether a reasonable expectation exists include: general commercial practice; the nature of the corporation; the relationship between the parties; past practice; steps the claimant could have taken to protect itself; representations and agreements; and the fair resolution of conflicts between corporate stakeholders. For the second question, a claimant must show that the failure to meet the reasonable expectation involved unfair conduct and prejudicial consequences under s. 241. [para. 68] [para. 72] [para. 89] [para. 95]

Where conflicting interests arise, it falls to the directors of the corporation to resolve them in accordance with their fiduciary duty to act in the best interests of the corporation. The cases on oppression, taken as a whole, confirm that this duty comprehends a duty to treat individual stakeholders affected by corporate actions equitably and fairly. There are no absolute rules and no principle that one set of interests should prevail over another. In each case, the question is whether, in all the circumstances, the directors acted in the best interests of the corporation, having regard to all relevant considerations, including - but not confined to - the need to treat affected stakeholders in a fair manner, commensurate with the corporation's duties as a responsible corporate citizen. Where it is impossible to please all stakeholders, it will be irrelevant that the directors rejected alternative transactions that were no more beneficial than the chosen one. [paras. 81-83]

Here, the debentureholders did not establish that they had a reasonable expectation that the directors of BCE would protect their economic interests by putting forth a plan of arrangement that would maintain the investment grade trading value of their debentures. The trial judge concluded that this expectation was not made out on the evidence, given the overall context of the relationship, the nature of the corporation, its situation as the target of a bidding war, the fact that the claimants could have protected themselves against reductions in market value by negotiating appropriate contractual terms, and that any statements by Bell Canada suggesting a commitment to retain investment grade ratings for the debentures were accompanied by warnings precluding such expectations. The trial judge recognized that the content of the directors' fiduciary duty to act in the best interests of the corporation was affected by the various interests at stake in the context of the auction process, and that they might have to approve transactions that were in the best interests of the corporation but which benefited some groups at the expense of others. All three competing bids required Bell Canada to assume additional debt. Under the business judgment rule, deference should be accorded to the business decisions of directors acting in good faith in performing the functions they were elected to perform. In this case, there was no error in the principles applied by the trial judge nor in his findings of fact. [paras. 96-100]

The debentureholders also did not establish that they had a reasonable expectation that the directors would consider their economic interests in maintaining the trading value of the debentures. While

the evidence, objectively viewed, supports a reasonable expectation that the directors would consider the position of the debentureholders in making their decisions on the various offers under consideration, it is apparent that the directors considered the interests of debentureholders, and concluded that while the contractual terms of the debentures would be honoured, no further commitments could be made. This fulfilled the duty of the directors to consider the debentureholders' interests and did not amount to "unfair disregard" of the interests of debentureholders. What the claimants contend is, in reality, an expectation that the directors would take positive steps to restructure the purchase in a way that would provide a satisfactory price to shareholders and preserve the high market value of the debentures. There was no evidence that it was reasonable to suppose this could be achieved, since all three bids involved a substantial increase in Bell Canada's debt. Commercial practice and reality also undermine their claim. Leveraged buyouts are not unusual or unforeseeable, and the debentureholders could have negotiated protections in their contracts. Given the nature and the corporate history of Bell Canada, it should not have been outside the contemplation of debentureholders that plans of arrangements could occur in the future. While the debentureholders rely on the past practice of maintaining the investment grade rating of the debentures, the events precipitating the leveraged buyout transaction were market realities affecting what were reasonable practices. No representations had been made to debentureholders upon which they could reasonably rely. [para. 96] [para. 102] [paras. 104-106] [paras. 108-110]

With respect to the duty on directors to resolve the conflicting interests of stakeholders in a fair manner that reflected the best interests of the corporation, the corporation's best interests arguably favoured acceptance of the offer at the time. The trial judge accepted the evidence that Bell Canada needed to undertake significant changes to be successful, and the momentum of the market made a buyout inevitable. Considering all the relevant factors, the debentureholders failed to establish a reasonable expectation that could give rise to a claim for oppression. [paras. 111-113]

2. The Section 192 Approval Process

The s. 192 approval process is generally applicable to change of control transactions where the arrangement is sponsored by the directors of the target company and the goal is to require some or all shareholders to surrender their shares. The approval process focuses on whether the arrangement, viewed objectively, is fair and reasonable. Its purpose is to permit major changes in corporate structure to be made while ensuring that individuals whose rights may be affected are treated fairly, and its spirit is to achieve a fair balance between conflicting interests. In seeking court approval of an arrangement, the onus is on the corporation to establish that (1) the statutory procedures have been met; (2) the application has been put forth in good faith; and (3) the arrangement is "fair and reasonable". [para. 119] [para. 126] [para. 128] [para. 137]

To approve a plan of arrangement as fair and reasonable, courts must be satisfied that (a) the arrangement has a valid business purpose, and (b) the objections of those whose legal rights are being arranged are being resolved in a fair and balanced way. Whether these requirements are met is determined by taking into account a variety of relevant factors, including the necessity of the arrangement to the corporation's continued existence, the approval, if any, of a majority of shareholders and other security holders entitled to vote, and the proportionality of the impact on affected groups. Where there has been no vote, courts may consider whether an intelligent and honest business person, as a member of the class concerned and acting in his or her own interest, might reasonably approve of the plan. Courts must focus on the terms and impact of the arrangement itself, rather than the process by which it was reached, and must be satisfied that the burden imposed by

the arrangement on security holders is justified by the interests of the corporation. Courts on a s. 192 application should refrain from substituting their views of the "best" arrangement, but should not surrender their duty to scrutinize the arrangement. [para. 136] [para. 138] [para. 145] [para. 151] [paras. 154-155]

The purpose of s. 192 suggests that only security holders whose legal rights stand to be affected by the proposal are envisioned. It is the fact that the corporation is permitted to alter individual rights that places the matter beyond the power of the directors and creates the need for shareholder and court approval. However, in some circumstances, interests that are not strictly legal could be considered. The fact that a group whose legal rights are left intact faces a reduction in the trading value of its securities generally does not, without more, constitute a circumstance where non-legal interests should be considered on a s. 192 application. [paras. 133-135]

Here, the debentureholders no longer argue that the arrangement lacks a valid business purpose. The debate focuses on whether the objections of those whose rights are being arranged were resolved in a fair and balanced way. Since only their economic interests were affected by the proposed transaction, not their legal rights, and since they did not fall within an exceptional situation where non-legal interests should be considered under s. 192, the debentureholders did not constitute an affected class under s. 192, and the trial judge was correct in concluding that they should not be permitted to veto almost 98 percent of the shareholders simply because the trading value of their securities would be affected. Although not required, it remained open to the trial judge to consider the debentureholders' economic interests, and he did not err in concluding that the arrangement addressed the debentureholders' interests in a fair and balanced way. The arrangement did not fundamentally alter the debentureholders' rights, as the investment and return they contracted for remained intact. It was well known that alteration in debt load could cause fluctuations in the trading value of the debentures, and yet the debentureholders had not contracted against this contingency. It was clear to the judge that the continuance of the corporation required acceptance of an arrangement that would entail increased debt and debt guarantees by Bell Canada. No superior arrangement had been put forward and BCE had been assisted throughout by expert legal and financial advisors. Recognizing that there is no such thing as a perfect arrangement, the trial judge correctly concluded that the arrangement had been shown to be fair and reasonable. [para. 157] [para. 161] [paras. 163-164]

Cases Cited

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Ward Broome Ltd. (2001), 12 B.L.R. (3d) 275; *SCI Systems Inc. v. Gornitzki Thompson & Little Co.* (1997), 147 D.L.R. (4th) 300, var'd (1998), 110 O.A.C. 160; *Downtown Eatery (1993) Ltd. v. Ontario* (2001), 200 D.L.R. (4th) 289, leave to appeal refused, [2002] 2 S.C.R. vi; *Re Ferguson and Imax Systems Corp.* (1983), 150 D.L.R. (3d) 718; *Gibbons v. Medical Carriers Ltd.* (2001), 17 B.L.R. (3d) 280, 2001 MBQB 229; *Alberta Treasury Branches v. Seven Way Capital Corp.* (1999), 50 B.L.R. (2d) 294, aff'd (2000), 8 B.L.R. (3d) 1, 2000 ABCA 194; *Lyall v. 147250 Canada Ltd.* (1993), 106 D.L.R. (4th) 304; *Tsui v. International Capital Corp.*, [1993] 4 W.W.R. 613, aff'd (1993), 113 Sask. R. 3; *Deutsche Bank Canada v. Oxford Properties Group Inc.* (1998), 40 B.L.R. (2d) 302; *Themadel Foundation v. Third Canadian Investment Trust Ltd.* (1995), 23 O.R. (3d) 7, var'd (1998), 38 O.R. (3d) 749; *Revlon Inc. v. MacAndrews & Forbes Holdings Inc.*, 506 A.2d 173 (1985); *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (1985); *Trizec Corp., Re* (1994), 21 Alta. L.R. (3d) 435; *Pacifica Papers Inc. v. Johnstone* (2001) 15 B.L.R. (3d) 249, 2001 BCSC 1069; *Abitibi-Consolidated Inc. (Arrangement relatif à)*, [2007] Q.J. No. 16158 (QL), 2007 QCCS 6830; *Canadian Pacific Ltd. (Re)* (1990), 73 O.R. (2d) 212; *Cinar Corp. v. Shareholders of Cinar Corp.* (2004), 4 C.B.R. (5th) 163; *PetroKazakhstan Inc. v. Lukoil Overseas Kumkol B.V.* (2005), 12 B.L.R. (4th) 128, 2005 ABQB 789; *St. Lawrence & Hudson Railway Co. (Re)*, [1998] O.J. No. 3934 (QL); *Re Alabama, New Orleans, Texas and Pacific Junction Railway Co.*, [1891] 1 Ch. 213; *Stelco Inc. (Re)* (2006), 18 C.B.R. (5th) 173; *UPM-Kymmene Corp. v. UPM-Kymmene Miramichi Inc.* (2002), 214 D.L.R. (4th) 496, aff'd (2004), 42 B.L.R. (3d) 34.

Statutes and Regulations Cited

Canada Business Corporations Act, R.S.C. 1985, c. C-44, ss. 102(1), 122, 192, 239, 241.

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History and Disposition:

APPEALS and CROSS-APPEALS from judgments of the Quebec Court of Appeal (Robert C.J. and Otis, Nuss, Pelletier and Dalphond JJ.A.), [2008] R.J.Q. 1298, 43 B.L.R. (4th) 157, [2008] Q.J. No. 4173 (QL), 2008 CarswellQue 4179, 2008 QCCA 935; [2008] Q.J. No. 4170 (QL), 2008 QCCA 930; [2008] Q.J. No. 4171 (QL), 2008 QCCA 931; [2008] Q.J. No. 4172 (QL), 2008 QCCA 932; [2008] Q.J. No. 4174 (QL), 2008 QCCA 933; [2008] Q.J. No. 4175 (QL), 2008 QCCA 934, setting aside decisions by Silcoff J., [2008] R.J.Q. 1029, 43 B.L.R. (4th) 39, [2008] Q.J. No. 4376 (QL), CarswellQue. 1805, 2008 QCCS 898; (2008), 43 B.L.R.(4th) 69, [2008] Q.J. No. 1728 (QL), CarswellQue 2226, 2008 QCCS 899; [2008] R.J.Q. 1097, 43 B.L.R. (4th) 1, [2008] Q.J. No. 1788 (QL), 2008 CarswellQue 2227, 2008 QCCS 905; (2008), 43 B.L.R. (4th) 135, [2008] Q.J. No. 1789 (QL), CarswellQue 2228, 2008 QCCS 906; [2008] R.J.Q. 1119, 43 B.L.R.(4th) 79, [2008] Q.J. No. 1790 (QL), 2008 CarswellQue 2229, 2008 QCCS 907. Appeals allowed and cross-appeals dismissed.

Counsel:

Guy Du Pont, Kent E. Thomson, William Brock, James Doris, Louis-Martin O'Neill, Pierre Bienvenu and *Steve Tenai*, for the appellants/respondents on cross-appeals BCE Inc. and Bell Canada.

Benjamin Zarnett, Jessica Kimmel, James A. Woods and *Christopher L. Richter*, for the appellant/respondent on cross-appeals 6796508 Canada Inc.

John Finnigan, John Porter, Avram Fishman and *Mark Meland*, for the respondents/appellants on cross-appeals Group of 1976 Debentureholders and Group of 1996 Debentureholders.

Markus Koehnen, Max Mendelsohn, Paul Macdonald, Julien Brazeau and *Erin Cowling*, for the respondent/appellant on cross-appeals Group of 1997 Debentureholders.

Written submissions only by *Robert Tessier* and *Ronald Auclair*, for the respondent Computershare Trust Company of Canada.

Christian S. Tacit, for the intervener Catalyst Asset Management Inc.

Raynold Langlois, Q.C., and *Gerald Apostolatos*, for the intervener Matthew Stewart.

The following is the judgment delivered by

THE COURT:--

I. Introduction

1 These appeals arise out of an offer to purchase all shares of BCE Inc. ("BCE"), a large telecommunications corporation, by a group headed by the Ontario Teachers Pension Plan Board ("Teachers"), financed in part by the assumption by Bell Canada, a wholly owned subsidiary of BCE, of a $30 billion debt. The leveraged buyout was opposed by debentureholders of Bell Canada on the ground that the increased debt contemplated by the purchase agreement would reduce the value of their bonds. Upon request for court approval of an arrangement under s. 192 of the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 ("*CBCA*"), the debentureholders argued that it

should not be found to be fair. They also opposed the arrangement under s. 241 of the *CBCA* on the ground that it was oppressive to them.

2 The Quebec Superior Court, *per* Silcoff J., approved the arrangement as fair under the *CBCA* and dismissed the claims for oppression. The Quebec Court of Appeal found that the arrangement had not been shown to be fair and held that it should not have been approved. Thus, it found it unnecessary to consider the oppression claim.

3 On June 20, 2008, this Court allowed the appeals from the Court of Appeal's disapproval of the arrangement and dismissed two cross-appeals from the dismissal of the claims for oppression, with reasons to follow. These are those reasons.

II. Facts

4 At issue is a plan of arrangement valued at approximately $52 billion, for the purchase of the shares of BCE by way of a leveraged buyout. The arrangement was opposed by a group, comprised mainly of financial institutions, that hold debentures issued by Bell Canada. The crux of their complaints is that the arrangement would diminish the trading value of their debentures by an average of 20 percent, while conferring a premium of approximately 40 percent on the market price of BCE shares.

5 Bell Canada was incorporated in 1880 by a special Act of the Parliament of Canada. The corporation was subsequently continued under the *CBCA*. BCE, a management holding company, was incorporated in 1970 and continued under the *CBCA* in 1979. Bell Canada became a wholly owned subsidiary of BCE in 1983 pursuant to a plan of arrangement under which Bell Canada's shareholders surrendered their shares in exchange for shares of BCE. BCE and Bell Canada are separate legal entities with separate charters, articles and bylaws. Since January 2003, however, they have shared a common set of directors and some senior officers.

6 At the time relevant to these proceedings, Bell Canada had $7.2 billion in outstanding long-term debt comprised of debentures issued pursuant to three trust indentures: the 1976, the 1996 and the 1997 trust indentures. The trust indentures contain neither change of control nor credit rating covenants, and specifically allow Bell Canada to incur or guarantee additional debt subject to certain limitations.

7 Bell Canada's debentures were perceived by investors to be safe investments and, up to the time of the proposed leveraged buyout, had maintained an investment grade rating. The debentureholders are some of Canada's largest and most reputable financial institutions, pension funds and insurance companies. They are major participants in the debt markets and possess an intimate and historic knowledge of the financial markets.

8 A number of technological, regulatory and competitive changes have significantly altered the industry in which BCE operates. Traditionally highly regulated and focused on circuit-switch line telephone service, the telecommunication industry is now guided primarily by market forces and characterized by an ever-expanding group of market participants, substantial new competition and increasing expectations regarding customer service. In response to these changes, BCE developed a new business plan by which it would focus on its core business, telecommunications, and divest its interest in unrelated businesses. This new business plan, however, was not as successful as anticipated. As a result, the shareholder returns generated by BCE remained significantly less than the ones generated by its competitors.

9 Meanwhile, by the end of 2006, BCE had large cash flows and strong financial indicators, characteristics perceived by market analysts to make it a suitable target for a buyout. In November 2006, BCE was made aware that Kohlberg Kravis Roberts & Co. ("KKR"), a United States private equity firm, might be interested in a transaction involving BCE. Mr. Michael Sabia, President and Chief Executive Officer of BCE, contacted KKR to inform them that BCE was not interested in pursuing such a transaction at that time.

10 In February 2007, new rumours surfaced that KKR and the Canada Pension Plan Investment Board were arranging financing to initiate a bid for BCE. Shortly thereafter, additional rumours began to circulate that an investment banking firm was assisting Teachers with a potential transaction involving BCE. Mr. Sabia, after meeting with BCE's board of directors ("Board"), contacted the representatives of both KKR and Teachers to reiterate that BCE was not interested in pursuing a "going-private" transaction at the time because it was set on creating shareholder value through the execution of its 2007 business plan.

11 On March 29, 2007, after an article appeared on the front page of the *Globe and Mail* that inaccurately described BCE as being in discussions with a consortium comprised of KKR and Teachers, BCE issued a press release confirming that there were no ongoing discussions being held with private equity investors with respect to a "going-private" transaction for BCE.

12 On April 9, 2007, Teachers filed a report (Schedule 13D) with the United States Securities and Exchange Commission reflecting a change from a passive to an active holding of BCE shares. This filing heightened press speculation concerning a potential privatization of BCE.

13 Faced with renewed speculation and BCE having been put "in play" by the filing by Teachers of the Schedule 13D report, the Board met with its legal and financial advisors to assess strategic alternatives. It decided that it would be in the best interests of BCE and its shareholders to have competing bidding groups and to guard against the risk of a single bidding group assembling such a significant portion of available debt and equity that the group could preclude potential competing bidding groups from participating effectively in an auction process.

14 In a press release dated April 17, 2007, BCE announced that it was reviewing its strategic alternatives with a view to further enhancing shareholder value. On the same day, a Strategic Oversight Committee ("SOC") was created. None of its members had ever been part of management at BCE. Its mandate was, notably, to set up and supervise the auction process.

15 Following the April 17 press release, several debentureholders sent letters to the Board voicing their concerns about a potential leveraged buyout transaction. They sought assurance that their interests would be considered by the Board. BCE replied in writing that it intended to honour the contractual terms of the trust indentures.

16 On June 13, 2007, BCE provided the potential participants in the auction process with bidding rules and the general form of a definitive transaction agreement. The bidders were advised that, in evaluating the competitiveness of proposed bids, BCE would consider the impact that their proposed financing arrangements would have on BCE and on Bell Canada's debentureholders and, in particular, whether their bids respected the debentureholders' contractual rights under the trust indentures.

17 Offers were submitted by three groups. All three offers contemplated the addition of a substantial amount of new debt for which Bell Canada would be liable. All would have likely resulted

in a downgrade of the debentures below investment grade. The initial offer submitted by the appellant 6796508 Canada Inc. ("the Purchaser"), a corporation formed by Teachers and affiliates of Providence Equity Partners Inc. and Madison Dearborn Partners LLC, contemplated an amalgamation of Bell Canada that would have triggered the voting rights of the debentureholders under the trust indentures. The Board informed the Purchaser that such an amalgamation made its offer less competitive. The Purchaser submitted a revised offer with an alternative structure for the transaction that did not involve an amalgamation of Bell Canada. Also, the Purchaser's revised offer increased the initial price per share from $42.25 to $42.75.

18 The Board, after a review of the three offers and based on the recommendation of the SOC, found that the Purchaser's revised offer was in the best interests of BCE and BCE's shareholders. In evaluating the fairness of the consideration to be paid to the shareholders under the Purchaser's offer, the Board and the SOC received opinions from several reputable financial advisors. In the meantime, the Purchaser agreed to cooperate with the Board in obtaining a solvency certificate stating that BCE would still be solvent (and hence in a position to meet its obligations after completion of the transaction). The Board did not seek a fairness opinion in respect of the debentureholders, taking the view that their rights were not being arranged.

19 On June 30, 2007, the Purchaser and BCE entered into a definitive agreement. On September 21, 2007, BCE's shareholders approved the arrangement by a majority of 97.93 percent.

20 Essentially, the arrangement provides for the compulsory acquisition of all of BCE's outstanding shares. The price to be paid by the Purchaser is $42.75 per common share, which represents a premium of approximately 40 percent to the closing price of the shares as of March 28, 2007. The total capital required for the transaction is approximately $52 billion, $38.5 billion of which will be supported by BCE. Bell Canada will guarantee approximately $30 billion of BCE's debt. The Purchaser will invest nearly $8 billion of new equity capital in BCE.

21 As a result of the announcement of the arrangement, the credit ratings of the debentures by the time of trial had been downgraded from investment grade to below investment grade. From the perspective of the debentureholders, this downgrade was problematic for two reasons. First, it caused the debentures to decrease in value by an average of approximately 20 percent. Second, the downgrade could oblige debentureholders with credit-rating restrictions on their holdings to sell their debentures at a loss.

22 The debentureholders at trial opposed the arrangement on a number of grounds. First, the debentureholders sought relief under the oppression provision in s. 241 of the *CBCA*. Second, they opposed court approval of the arrangement, as required by s. 192 of the *CBCA*, alleging that the arrangement was not "fair and reasonable" because of the adverse effect on their economic interests. Finally, the debentureholders brought motions for declaratory relief under the terms of the trust indentures, which are not before us ((2008), 43 B.L.R. (4th) 39, 2008 QCCS 898; (2008), 43 B.L.R. (4th) 69, 2008 QCCS 899).

III. Judicial History

23 The trial judge reviewed the s. 241 oppression claim as lying against both BCE and Bell Canada, since s. 241 refers to actions by the "corporation or any of its affiliates". He dismissed the claims for oppression on the grounds that the debt guarantee to be assumed by Bell Canada had a valid business purpose; that the transaction did not breach the reasonable expectations of the de-

bentureholders; that the transaction was not oppressive by reason of rendering the debentureholders vulnerable; and that BCE and its directors had not unfairly disregarded the interests of the debentureholders: (2008), 43 B.L.R. (4th) 79, 2008 QCCS 907; (2008), 43 B.L.R. (4th) 135, 2008 QCCS 906.

24 In arriving at these conclusions, the trial judge proceeded on the basis that the BCE directors had a fiduciary duty under s. 122 of the *CBCA* to act in the best interests of the corporation. He held that while the best interests of the corporation are not to be confused with the interests of the shareholders or other stakeholders, corporate law recognizes fundamental differences between shareholders and debt security holders. He held that these differences affect the content of the directors' fiduciary duty. As a result, the directors' duty to act in the best interests of the corporation might require them to approve transactions that, while in the interests of the corporation, might also benefit some or all shareholders at the expense of other stakeholders. He also noted that in accordance with the business judgment rule, Canadian courts tend to accord deference to business decisions of directors taken in good faith and in the performance of the functions they were elected to perform by shareholders.

25 The trial judge held that the debentureholders' reasonable expectations must be assessed on an objective basis and, absent compelling reasons, must derive from the trust indentures and the relevant prospectuses issued in connection with the debt offerings. Statements by Bell Canada indicating a commitment to retaining investment grade ratings did not assist the debentureholders, since these statements were accompanied by warnings, repeated in the prospectuses pursuant to which the debentures were issued, that negated any expectation that this policy would be maintained indefinitely. The reasonableness of the alleged expectation was further negated by the fact that the debentureholders could have guarded against the business risks arising from a change of control by negotiating protective contract terms. The fact that the shareholders stood to benefit from the transaction and that the debentureholders were prejudiced did not in itself give rise to a conclusion that the directors had breached their fiduciary duty to the corporation. All three competing bids required Bell Canada to assume additional debt, and there was no evidence that the bidders were prepared to treat the debentureholders any differently. The materialization of certain risks as a result of decisions taken by the directors in accordance with their fiduciary duty to the corporation did not constitute oppression against the debentureholders or unfair disregard of their interests.

26 Having dismissed the claim for oppression, the trial judge went on to consider BCE's application for approval of the transaction under s. 192 of the *CBCA* ((2008), 43 B.L.R. (4th) 1, 2008 QCCS 905). He dismissed the debentureholders' claim for voting rights on the arrangement on the ground that their legal interests were not compromised by the arrangement and that it would be unfair to allow them in effect to veto the shareholder vote. However, in determining whether the arrangement was fair and reasonable - the main issue on the application for approval - he considered the fairness of the transaction with respect to both the shareholders and the debentureholders, and concluded that the arrangement was fair and reasonable. He considered the necessity of the arrangement for Bell Canada's continued operations; that the Board, comprised almost entirely of independent directors, had determined the arrangement was fair and reasonable and in the best interests of BCE and the shareholders; that the arrangement had been approved by over 97 percent of the shareholders; that the arrangement was the culmination of a robust strategic review and auction process; the assistance the Board received throughout from leading legal and financial advisors; the absence of a superior proposal; and the fact that the proposal did not alter or arrange the debentureholders' legal rights. While the proposal stood to alter the debentureholders' economic interests, in

the sense that the trading value of their securities would be reduced by the added debt load, their contractual rights remained intact. The trial judge noted that the debentureholders could have protected themselves against this eventuality through contract terms, but had not. Overall, he concluded that taking all relevant matters into account, the arrangement was fair and reasonable and should be approved.

27 The Court of Appeal allowed the appeals on the ground that BCE had failed to meet its onus on the test for approval of an arrangement under s. 192, by failing to show that the transaction was fair and reasonable to the debentureholders. Basing its analysis on this Court's decision in *Peoples Department Stores Inc. (Trustee of) v. Wise*, [2004] 3 S.C.R. 461, 2004 SCC 68, the Court of Appeal found that the directors were required to consider the non-contractual interests of the debentureholders. It held that representations made by Bell Canada over the years could have created reasonable expectations above and beyond the contractual rights of the debentureholders. In these circumstances, the directors were under a duty, not simply to accept the best offer, but to consider whether the arrangement could be restructured in a way that provided a satisfactory price to the shareholders while avoiding an adverse effect on the debentureholders. In the absence of such efforts, BCE had not discharged its onus under s. 192 of showing that the arrangement was fair and reasonable. The Court of Appeal therefore overturned the trial judge's order approving the plan of arrangement: (2008), 43 B.L.R. (4th) 157, 2008 QCCA 930, 2008 QCCA 931, 2008 QCCA 932, 2008 QCCA 933, 2008 QCCA 934, 2008 QCCA 935.

28 The Court of Appeal found it unnecessary to consider the s. 241 oppression claim, holding that its rejection of the s. 192 approval application effectively disposed of the oppression claim. In its view, where approval is sought under s. 192 and opposed, there is generally no need for an affected security holder to assert an oppression remedy under s. 241.

29 BCE and Bell Canada appeal to this Court arguing that the Court of Appeal erred in overturning the trial judge's approval of the plan of arrangement. While formally cross-appealing on s. 241, the debentureholders argue that the Court of Appeal was correct to consider their complaints under s. 192, such that their appeals under s. 241 became moot.

IV. Issues

30 The issues, briefly stated, are whether the Court of Appeal erred in dismissing the debentureholders' s. 241 oppression claim and in overturning the Superior Court's s. 192 approval of the plan of arrangement. These questions raise the issue of what is required to establish oppression of debentureholders in a situation where a corporation is facing a change of control, and how a judge on an application for approval of an arrangement under s. 192 of the *CBCA* should treat claims such as those of the debentureholders in these actions. These reasons will consider both issues.

31 In order to situate these issues in the context of Canadian corporate law, it may be useful to offer a preliminary description of the remedies provided by the *CBCA* to shareholders and stakeholders in a corporation facing a change of control.

32 Accordingly, these reasons will consider:

(1) the rights, obligations and remedies under the *CBCA* in overview;
(2) the debentureholders' entitlement to relief under the s. 241 oppression remedy;

(3) the debentureholders' entitlement to relief under the requirement for court approval of an arrangement under s. 192.

33 We note that it is unnecessary for the purposes of these appeals to distinguish between the conduct of the directors of BCE, the holding company, and the conduct of the directors of Bell Canada. The same directors served on the boards of both corporations. While the oppression remedy was directed at both BCE and Bell Canada, the courts below considered the entire context in which the directors of BCE made their decisions, which included the obligations of Bell Canada in relation to its debentureholders. It was not found by the lower courts that the directors of BCE and Bell Canada should have made different decisions with respect to the two corporations. Accordingly, the distinct corporate character of the two entities does not figure in our analysis.

V. Analysis

A. *Overview of Rights, Obligations and Remedies under the CBCA*

34 An essential component of a corporation is its capital stock, which is divided into fractional parts, the shares: *Bradbury v. English Sewing Cotton Co.*, [1923] A.C. 744 (H.L.), at p. 767; *Zwicker v. Stanbury*, [1953] 2 S.C.R. 438. While the corporation is ongoing, shares confer no right to its underlying assets.

35 A share "is not an isolated piece of property ... [but] a 'bundle of inter-related rights and liabilities": *Sparling v. Quebec (Caisse de dépôt et placement du Québec)*, [1988] 2 S.C.R. 1015, at p. 1025, *per* La Forest J. These rights include the right to a proportionate part of the assets of the corporation upon winding-up and the right to oversee the management of the corporation by its board of directors by way of votes at shareholder meetings.

36 The directors are responsible for the governance of the corporation. In the performance of this role, the directors are subject to two duties: a fiduciary duty to the corporation under s. 122(1)(*a*) (the fiduciary duty); and a duty to exercise the care, diligence and skill of a reasonably prudent person in comparable circumstances under s. 122(1)(*b*) (the duty of care). The second duty is not at issue in these proceedings as this is not a claim against the directors of the corporation for failing to meet their duty of care. However, this case does involve the fiduciary duty of the directors to the corporation, and particularly the "fair treatment" component of this duty, which, as will be seen, is fundamental to the reasonable expectations of stakeholders claiming an oppression remedy.

37 The fiduciary duty of the directors to the corporation originated in the common law. It is a duty to act in the best interests of the corporation. Often the interests of shareholders and stakeholders are co-extensive with the interests of the corporation. But if they conflict, the directors' duty is clear - it is to the corporation: *Peoples Department Stores*.

38 The fiduciary duty of the directors to the corporation is a broad, contextual concept. It is not confined to short-term profit or share value. Where the corporation is an ongoing concern, it looks to the long-term interests of the corporation. The content of this duty varies with the situation at hand. At a minimum, it requires the directors to ensure that the corporation meets its statutory obligations. But, depending on the context, there may also be other requirements. In any event, the fiduciary duty owed by directors is mandatory; directors must look to what is in the best interests of the corporation.

39 In *Peoples Department Stores*, this Court found that although directors *must* consider the best interests of the corporation, it may also be appropriate, although *not mandatory*, to consider the impact of corporate decisions on shareholders or particular groups of stakeholders. As stated by Major and Deschamps JJ., at para. 42:

> We accept as an accurate statement of law that in determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, *inter alia*, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.

As will be discussed, cases dealing with claims of oppression have further clarified the content of the fiduciary duty of directors with respect to the range of interests that should be considered in determining what is in the best interests of the corporation, acting fairly and responsibly.

40 In considering what is in the best interests of the corporation, directors may look to the interests of, *inter alia*, shareholders, employees, creditors, consumers, governments and the environment to inform their decisions. Courts should give appropriate deference to the business judgment of directors who take into account these ancillary interests, as reflected by the business judgment rule. The "business judgment rule" accords deference to a business decision, so long as it lies within a range of reasonable alternatives: see *Maple Leaf Foods Inc. v. Schneider Corp.* (1998), 42 O.R. (3d) 177 (C.A.); *Kerr v. Danier Leather Inc.*, [2007] 3 S.C.R. 331, 2007 SCC 44. It reflects the reality that directors, who are mandated under s. 102(1) of the *CBCA* to manage the corporation's business and affairs, are often better suited to determine what is in the best interests of the corporation. This applies to decisions on stakeholders' interests, as much as other directorial decisions.

41 Normally only the beneficiary of a fiduciary duty can enforce the duty. In the corporate context, however, this may offer little comfort. The directors who control the corporation are unlikely to bring an action against themselves for breach of their own fiduciary duty. The shareholders cannot act in the stead of the corporation; their only power is the right to oversee the conduct of the directors by way of votes at shareholder assemblies. Other stakeholders may not even have that.

42 To meet these difficulties, the common law developed a number of special remedies to protect the interests of shareholders and stakeholders of the corporation. These remedies have been affirmed, modified and supplemented by the *CBCA*.

43 The first remedy provided by the *CBCA* is the s. 239 derivative action, which allows stakeholders to enforce the directors' duty to the corporation when the directors are themselves unwilling to do so. With leave of the court, a complainant may bring (or intervene in) a derivative action in the name and on behalf of the corporation or one of its subsidiaries to enforce a right of the corporation, including the rights correlative with the directors' duties to the corporation. (The requirement of leave serves to prevent frivolous and vexatious actions, and other actions which, while possibly brought in good faith, are not in the interest of the corporation to litigate.)

44 A second remedy lies against the directors in a civil action for breach of duty of care. As noted, s. 122(1)(*b*) of the *CBCA* requires directors and officers of a corporation to "exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances". This duty, unlike the s. 122(1)(*a*) fiduciary duty, is not owed solely to the corporation, and

thus may be the basis for liability to other stakeholders in accordance with principles governing the law of tort and extracontractual liability: *Peoples Department Stores.* Section 122(1)(*b*) does not provide an independent foundation for claims. However, applying the principles of *The Queen in right of Canada v. Saskatchewan Wheat Pool*, [1983] 1 S.C.R. 205, courts may take this statutory provision into account as to the standard of behaviour that should reasonably be expected.

45 A third remedy, grounded in the common law and endorsed by the *CBCA*, is a s. 241 action for oppression. Unlike the derivative action, which is aimed at enforcing a right of the corporation itself, the oppression remedy focuses on harm to the legal and equitable interests of stakeholders affected by oppressive acts of a corporation or its directors. This remedy is available to a wide range of stakeholders - security holders, creditors, directors and officers.

46 Additional "remedial" provisions are found in provisions of the *CBCA* providing for court approval in certain cases. An arrangement under s. 192 of the *CBCA* is one of these. While s. 192 cannot be described as a remedy *per se*, it has remedial-like aspects. It is directed at the situation of corporations seeking to effect fundamental changes to the corporation that affects stakeholder rights. The Act provides that such arrangements require the approval of the court. Unlike the civil action and oppression, which focus on the conduct of the directors, a s. 192 review requires a court approving a plan of arrangement to be satisfied that: (i) the statutory procedures have been met; (ii) the application has been put forth in good faith; and (iii) the arrangement is fair and reasonable. If the corporation fails to discharge its burden of establishing these elements, approval will be withheld and the proposed change will not take place. In assessing whether the arrangement should be approved, the court will hear arguments from opposing security holders whose rights are being arranged. This provides an opportunity for security holders to argue against the proposed change.

47 Two of these remedies are in issue in these actions: the action for oppression and approval of an arrangement under s. 192. The trial judge treated these remedies as involving distinct considerations and concluded that the debentureholders had failed to establish entitlement to either remedy. The Court of Appeal, by contrast, viewed the two remedies as substantially overlapping, holding that both turned on whether the directors had properly considered the debentureholders' expectations. Having found on this basis that the requirements of s. 192 were not met, the Court of Appeal concluded that the action for oppression was moot. As will become apparent, we do not endorse this approach. In our view, the s. 241 oppression action and the s. 192 requirement for court approval of a change to the corporate structure are different types of proceedings, engaging different inquiries. Accordingly, we find it necessary to consider both the claims for oppression and the s. 192 application for approval.

48 The debentureholders have formally cross-appealed on the oppression remedy. However, due to the Court of Appeal's failure to consider this issue, the debentureholders did not advance separate arguments before this Court. As certain aspects of their position are properly addressed within the context of an analysis of oppression under s. 241, we have considered them here.

49 Against this background, we turn to a more detailed consideration of the claims.

B. *The Section 241 Oppression Remedy*

50 The debentureholders in these appeals claim that the directors acted in an oppressive manner in approving the sale of BCE, contrary to s. 241 of the *CBCA.*

51 Security holders of a corporation or its affiliates fall within the class of persons who may be permitted to bring a claim for oppression under s. 241 of the *CBCA*. The trial judge permitted the debentureholders to do so, although in the end he found the claim had not been established. The question is whether the trial judge erred in dismissing the claim.

52 We will first set out what must be shown to establish the right to a remedy under s. 241, and then review the conduct complained of in the light of those requirements.

(1) The Law

53 Section 241(2) provides that a court may make an order to rectify the matters complained of where

> (*a*) any act or omission of the corporation or any of its affiliates effects a result,
>
> (*b*) the business or affairs of the corporation or any of its affiliates are or have been carried on or conducted in a manner, or
>
> (*c*) the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer....

54 Section 241 jurisprudence reveals two possible approaches to the interpretation of the oppression provisions of the *CBCA*: M. Koehnen, *Oppression and Related Remedies* (2004), at pp. 79-80 and 84. One approach emphasizes a strict reading of the three types of conduct enumerated in s. 241 (oppression, unfair prejudice and unfair disregard): see *Scottish Co-operative Wholesale Society Ltd. v. Meyer*, [1959] A.C. 324 (H.L.); *Diligenti v. RWMD Operations Kelowna Ltd.* (1976), 1 B.C.L.R. 36 (S.C.); *Stech v. Davies*, [1987] 5 W.W.R. 563 (Alta. Q.B.). Cases following this approach focus on the precise content of the categories "oppression", "unfair prejudice" and "unfair disregard". While these cases may provide valuable insight into what constitutes oppression in particular circumstances, a categorical approach to oppression is problematic because the terms used cannot be put into watertight compartments or conclusively defined. As Koehnen puts it (at p. 84), "[t]he three statutory components of oppression are really adjectives that try to describe inappropriate conduct .... The difficulty with adjectives is they provide no assistance in formulating principles that should underline court intervention."

55 Other cases have focused on the broader principles underlying and uniting the various aspects of oppression: see *First Edmonton Place Ltd. v. 315888 Alberta Ltd.* (1988), 40 B.L.R. 28 (Alta. Q.B.), var'd (1989), 45 B.L.R. 110 (Alta. C.A.); *820099 Ontario Inc. v. Harold E. Ballard Ltd.* (1991), 3 B.L.R. (2d) 113 (Ont. Div. Ct.); *Westfair Foods Ltd. v. Watt* (1991), 79 D.L.R. (4th) 48 (Alta. C.A.).

56 In our view, the best approach to the interpretation of s. 241(2) is one that combines the two approaches developed in the cases. One should look first to the principles underlying the oppression remedy, and in particular the concept of reasonable expectations. If a breach of a reasonable expectation is established, one must go on to consider whether the conduct complained of amounts to "oppression", "unfair prejudice" or "unfair disregard" as set out in s. 241(2) of the *CBCA*.

57 We preface our discussion of the twin prongs of the oppression inquiry by two preliminary observations that run throughout all the jurisprudence.

58 First, oppression is an equitable remedy. It seeks to ensure fairness - what is "just and equitable". It gives a court broad, equitable jurisdiction to enforce not just what is legal but what is fair: *Wright v. Donald S. Montgomery Holdings Ltd.* (1998), 39 B.L.R. (2d) 266 (Ont. Ct. (Gen. Div.)), at p. 273; *Re Keho Holdings Ltd. and Noble* (1987), 38 D.L.R. (4th) 368 (Alta. C.A.), at p. 374; see, more generally, Koehnen, at pp. 78-79. It follows that courts considering claims for oppression should look at business realities, not merely narrow legalities: *Scottish Co-operative Wholesale Society*, at p. 343.

59 Second, like many equitable remedies, oppression is fact-specific. What is just and equitable is judged by the reasonable expectations of the stakeholders in the context and in regard to the relationships at play. Conduct that may be oppressive in one situation may not be in another.

60 Against this background, we turn to the first prong of the inquiry, the principles underlying the remedy of oppression. In *Ebrahimi v. Westbourne Galleries Ltd.*, [1973] A.C. 360 (H.L.), at p. 379, Lord Wilberforce, interpreting s. 222 of the U.K. *Companies Act, 1948*, described the remedy of oppression in the following seminal terms:

> The words ["just and equitable"] are a recognition of the fact that a limited company is more than a mere legal entity, with a personality in law of its own: that there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se which are not necessarily submerged in the company structure.

61 Lord Wilberforce spoke of the equitable remedy in terms of the "rights, expectations and obligations" of individuals. "Rights" and "obligations" connote interests enforceable at law without recourse to special remedies, for example, through a contractual suit or a derivative action under s. 239 of the *CBCA*. It is left for the oppression remedy to deal with the "expectations" of affected stakeholders. The reasonable expectations of these stakeholders is the cornerstone of the oppression remedy.

62 As denoted by "reasonable", the concept of reasonable expectations is objective and contextual. The actual expectation of a particular stakeholder is not conclusive. In the context of whether it would be "just and equitable" to grant a remedy, the question is whether the expectation is reasonable having regard to the facts of the specific case, the relationships at issue, and the entire context, including the fact that there may be conflicting claims and expectations.

63 Particular circumstances give rise to particular expectations. Stakeholders enter into relationships, with and within corporations, on the basis of understandings and expectations, upon which they are entitled to rely, provided they are reasonable in the context: see *820099 Ontario*; *Main v. Delcan Group Inc.* (1999), 47 B.L.R. (2d) 200 (Ont. S.C.J.). These expectations are what the remedy of oppression seeks to uphold.

64 Determining whether a particular expectation is reasonable is complicated by the fact that the interests and expectations of different stakeholders may conflict. The oppression remedy recognizes that a corporation is an entity that encompasses and affects various individuals and groups, some of whose interests may conflict with others. Directors or other corporate actors may make corporate decisions or seek to resolve conflicts in a way that abusively or unfairly maximizes a par-

ticular group's interest at the expense of other stakeholders. The corporation and shareholders are entitled to maximize profit and share value, to be sure, but not by treating individual stakeholders unfairly. Fair treatment - the central theme running through the oppression jurisprudence - is most fundamentally what stakeholders are entitled to "reasonably expect".

65 Section 241(2) speaks of the "act or omission" of the corporation or any of its affiliates, the conduct of "business or affairs" of the corporation and the "powers of the directors of the corporation or any of its affiliates". Often, the conduct complained of is the conduct of the corporation or of its directors, who are responsible for the governance of the corporation. However, the conduct of other actors, such as shareholders, may also support a claim for oppression: see Koehnen, at pp. 109-10; *GATX Corp. v. Hawker Siddeley Canada Inc.* (1996), 27 B.L.R. (2d) 251 (Ont. Ct. (Gen. Div.)). In the appeals before us, the claims for oppression are based on allegations that the directors of BCE and Bell Canada failed to comply with the reasonable expectations of the debentureholders, and it is unnecessary to go beyond this.

66 The fact that the conduct of the directors is often at the centre of oppression actions might seem to suggest that directors are under a direct duty to individual stakeholders who may be affected by a corporate decision. Directors, acting in the best interests of the corporation, may be obliged to consider the impact of their decisions on corporate stakeholders, such as the debentureholders in these appeals. This is what we mean when we speak of a director being required to act in the best interests of the corporation viewed as a good corporate citizen. However, the directors owe a fiduciary duty to the corporation, and only to the corporation. People sometimes speak in terms of directors owing a duty to both the corporation and to stakeholders. Usually this is harmless, since the reasonable expectations of the stakeholder in a particular outcome often coincides with what is in the best interests of the corporation. However, cases (such as these appeals) may arise where these interests do not coincide. In such cases, it is important to be clear that the directors owe their duty to the corporation, not to stakeholders, and that the reasonable expectation of stakeholders is simply that the directors act in the best interests of the corporation.

67 Having discussed the concept of reasonable expectations that underlies the oppression remedy, we arrive at the second prong of the s. 241 oppression remedy. Even if reasonable, not every unmet expectation gives rise to claim under s. 241. The section requires that the conduct complained of amount to "oppression", "unfair prejudice" or "unfair disregard" of relevant interests. "Oppression" carries the sense of conduct that is coercive and abusive, and suggests bad faith. "Unfair prejudice" may admit of a less culpable state of mind, that nevertheless has unfair consequences. Finally, "unfair disregard" of interests extends the remedy to ignoring an interest as being of no importance, contrary to the stakeholders' reasonable expectations: see Koehnen, at pp. 81-88. The phrases describe, in adjectival terms, ways in which corporate actors may fail to meet the reasonable expectations of stakeholders.

68 In summary, the foregoing discussion suggests conducting two related inquiries in a claim for oppression: (1) Does the evidence support the reasonable expectation asserted by the claimant? and (2) Does the evidence establish that the reasonable expectation was violated by conduct falling within the terms "oppression", "unfair prejudice" or "unfair disregard" of a relevant interest?

69 Against the background of this overview, we turn to a more detailed discussion of these inquiries.

(a) *Proof of a Claimant's Reasonable Expectations*

70 At the outset, the claimant must identify the expectations that he or she claims have been violated by the conduct at issue and establish that the expectations were reasonably held. As stated above, it may be readily inferred that a stakeholder has a reasonable expectation of fair treatment. However, oppression, as discussed, generally turns on particular expectations arising in particular situations. The question becomes whether the claimant stakeholder reasonably held the particular expectation. Evidence of an expectation may take many forms depending on the facts of the case.

71 It is impossible to catalogue exhaustively situations where a reasonable expectation may arise due to their fact-specific nature. A few generalizations, however, may be ventured. Actual unlawfulness is not required to invoke s. 241; the provision applies "where the impugned conduct is wrongful, even if it is not actually unlawful": Dickerson Committee (R. W. V. Dickerson, J. L. Howard and L. Getz), *Proposals for a New Business Corporations Law for Canada* (1971), vol. 1, at p. 163. The remedy is focused on concepts of fairness and equity rather than on legal rights. In determining whether there is a reasonable expectation or interest to be considered, the court looks beyond legality to what is fair, given all of the interests at play: *Re Keho Holdings Ltd. and Noble*. It follows that not all conduct that is harmful to a stakeholder will give rise to a remedy for oppression as against the corporation.

72 Factors that emerge from the case law that are useful in determining whether a reasonable expectation exists include: general commercial practice; the nature of the corporation; the relationship between the parties; past practice; steps the claimant could have taken to protect itself; representations and agreements; and the fair resolution of conflicting interests between corporate stakeholders.

(i) Commercial Practice

73 Commercial practice plays a significant role in forming the reasonable expectations of the parties. A departure from normal business practices that has the effect of undermining or frustrating the complainant's exercise of his or her legal rights will generally (although not inevitably) give rise to a remedy: *Adecco Canada Inc. v. J. Ward Broome Ltd.* (2001), 12 B.L.R. (3d) 275 (Ont. S.C.J.); *SCI Systems Inc. v. Gornitzki Thompson & Little Co.*, (1997), 147 D.L.R. (4th) 300 (Ont. Ct. (Gen. Div.)), var'd (1998), 110 O.A.C. 160 (Div. Ct.); *Downtown Eatery (1993) Ltd. v. Ontario* (2001), 200 D.L.R. (4th) 289, leave to appeal refused, [2002] 2 S.C.R. vi.

(ii) The Nature of the Corporation

74 The size, nature and structure of the corporation are relevant factors in assessing reasonable expectations: *First Edmonton Place*; G. Shapira, "Minority Shareholders' Protection - Recent Developments" (1982), 10 *N.Z. Univ. L. Rev.* 134, at pp. 138 and 145-46. Courts may accord more latitude to the directors of a small, closely held corporation to deviate from strict formalities than to the directors of a larger public company.

(iii) Relationships

75 Reasonable expectations may emerge from the personal relationships between the claimant and other corporate actors. Relationships between shareholders based on ties of family or friendship may be governed by different standards than relationships between arm's length shareholders in a widely held corporation. As noted in *Re Ferguson and Imax Systems Corp.*, (1983), 150 D.L.R. (3d)

718 (Ont. C.A.), "when dealing with a close corporation, the court may consider the relationship between the shareholders and not simply legal rights as such" (p. 727).

(iv) Past Practice

76 Past practice may create reasonable expectations, especially among shareholders of a closely held corporation on matters relating to participation of shareholders in the corporation's profits and governance: *Gibbons v. Medical Carriers Ltd.* (2001), 17 B.L.R. (3d) 280, 2001 MBQB 229; *820099 Ontario*. For instance, in *Gibbons*, the court found that the shareholders had a legitimate expectation that all monies paid out of the corporation would be paid to shareholders in proportion to the percentage of shares they held. The authorization by the new directors to pay fees to themselves, for which the shareholders would not receive any comparable payments, was in breach of those expectations.

77 It is important to note that practices and expectations can change over time. Where valid commercial reasons exist for the change and the change does not undermine the complainant's rights, there can be no reasonable expectation that directors will resist a departure from past practice: *Alberta Treasury Branches v. SevenWay Capital Corp.* (1999), 50 B.L.R. (2d) 294 (Alta. Q.B.), aff'd (2000), 8 B.L.R. (3d) 1, 2000 ABCA 194.

(v) Preventive Steps

78 In determining whether a stakeholder expectation is reasonable, the court may consider whether the claimant could have taken steps to protect itself against the prejudice it claims to have suffered. Thus it may be relevant to inquire whether a secured creditor claiming oppressive conduct could have negotiated protections against the prejudice suffered: *First Edmonton Place*; *SCI Systems*.

(vi) Representations and Agreements

79 Shareholder agreements may be viewed as reflecting the reasonable expectations of the parties: *Main*; *Lyall v. 147250 Canada Ltd.* (1993), 106 D.L.R. (4th) 304 (B.C.C.A.).

80 Reasonable expectations may also be affected by representations made to stakeholders or to the public in promotional material, prospectuses, offering circulars and other communications: *Tsui v. International Capital Corp.*, [1993] 4 W.W.R. 613 (Sask. Q.B.), aff'd (1993), 113 Sask. R. 3 (C.A.); *Deutsche Bank Canada v. Oxford Properties Group Inc.* (1998), 40 B.L.R. (2d) 302 (Ont. Ct. (Gen. Div.)); *Themadel Foundation v. Third Canadian Investment Trust Ltd.* (1995), 23 O.R. (3d) 7 (Gen. Div.), var'd (1998), 38 O.R. (3d) 749 (C.A.).

(vii) Fair Resolution of Conflicting Interests

81 As discussed, conflicts may arise between the interests of corporate stakeholders *inter se* and between stakeholders and the corporation. Where the conflict involves the interests of the corporation, it falls to the directors of the corporation to resolve them in accordance with their fiduciary duty to act in the best interests of the corporation, viewed as a good corporate citizen.

82 The cases on oppression, taken as a whole, confirm that the duty of the directors to act in the best interests of the corporation comprehends a duty to treat individual stakeholders affected by corporate actions equitably and fairly. There are no absolute rules. In each case, the question is

whether, in all the circumstances, the directors acted in the best interests of the corporation, having regard to all relevant considerations, including, but not confined to, the need to treat affected stakeholders in a fair manner, commensurate with the corporation's duties as a responsible corporate citizen.

83 Directors may find themselves in a situation where it is impossible to please all stakeholders. The "fact that alternative transactions were rejected by the directors is irrelevant unless it can be shown that a particular alternative was definitely available and clearly more beneficial to the company than the chosen transaction": *Maple Leaf Foods, per* Weiler J.A., at p. 192.

84 There is no principle that one set of interests - for example the interests of shareholders - should prevail over another set of interests. Everything depends on the particular situation faced by the directors and whether, having regard to that situation, they exercised business judgment in a responsible way.

85 On these appeals, it was suggested on behalf of the corporations that the "*Revlon* line" of cases from Delaware support the principle that where the interests of shareholders conflict with the interests of creditors, the interests of shareholders should prevail.

86 The "*Revlon* line" refers to a series of Delaware corporate takeover cases, the two most important of which are *Revlon Inc. v. MacAndrews & Forbes Holdings Inc.*, 506 A.2d 173 (Del. 1985), and *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (Del. 1985). In both cases, the issue was how directors should react to a hostile takeover bid. *Revlon* suggests that in such circumstances, shareholder interests should prevail over those of other stakeholders, such as creditors. *Unocal* tied this approach to situations where the corporation will not continue as a going concern, holding that although a board facing a hostile takeover "may have regard for various constituencies in discharging its responsibilities, ... such concern for non-stockholder interests is inappropriate when ... the object no longer is to protect or maintain the corporate enterprise but to sell it to the highest bidder" (p. 182).

87 What is clear is that the *Revlon* line of cases has not displaced the fundamental rule that the duty of the directors cannot be confined to particular priority rules, but is rather a function of business judgment of what is in the best interests of the corporation, in the particular situation it faces. In a review of trends in Delaware corporate jurisprudence, former Delaware Supreme Court Chief Justice E. Norman Veasey put it this way:

> [It] is important to keep in mind the precise content of this "best interests" concept - that is, to whom this duty is owed and when. Naturally, one often thinks that directors owe this duty to both the corporation and the stockholders. That formulation is harmless in most instances because of the confluence of interests, in that what is good for the corporate entity is usually derivatively good for the stockholders. There are times, of course, when the focus is directly on the interests of the stockholders [i.e., as in *Revlon*]. But, in general, the directors owe fiduciary duties to the *corporation*, not to the stockholders. [Emphasis in original.]
>
> (E. Norman Veasey with Christine T. Di Guglielmo, "What Happened in Delaware Corporate Law and Governance from 1992-2004? A Retrospective on Some Key Developments" (2005), 153 *U. Pa. L. Rev.* 1399, at p. 1431)

88 Nor does this Court's decision in *Peoples Department Stores* suggest a fixed rule that the interests of creditors must prevail. In *Peoples Department Stores*, the Court had to consider whether, in the case of a corporation under threat of bankruptcy, creditors deserved special consideration (para. 46). The Court held that the fiduciary duty to the corporation did not change in the period preceding the bankruptcy, but that if the directors breach their duty of care to a stakeholder under s. 122(1)(*b*) of the *CBCA*, such a stakeholder may act upon it (para. 66).

(b) *Conduct which is Oppressive, is Unfairly Prejudicial or Unfairly Disregards the Claimant's Relevant Interests*

89 Thus far we have discussed how a claimant establishes the first element of an action for oppression - a reasonable expectation that he or she would be treated in a certain way. However, to complete a claim for oppression, the claimant must show that the failure to meet this expectation involved unfair conduct and prejudicial consequences within s. 241 of the *CBCA*. Not every failure to meet a reasonable expectation will give rise to the equitable considerations that ground actions for oppression. The court must be satisfied that the conduct falls within the concepts of "oppression", "unfair prejudice" or "unfair disregard" of the claimant's interest, within the meaning of s. 241 of the *CBCA*. Viewed in this way, the reasonable expectations analysis that is the theoretical foundation of the oppression remedy, and the particular types of conduct described in s. 241, may be seen as complementary, rather than representing alternative approaches to the oppression remedy, as has sometimes been supposed. Together, they offer a complete picture of conduct that is unjust and inequitable, to return to the language of *Ebrahimi.*

90 In most cases, proof of a reasonable expectation will be tied up with one or more of the concepts of oppression, unfair prejudice, or unfair disregard of interests set out in s. 241, and the two prongs will in fact merge. Nevertheless, it is worth stating that as in any action in equity, wrongful conduct, causation and compensable injury must be established in a claim for oppression.

91 The concepts of oppression, unfair prejudice and unfairly disregarding relevant interests are adjectival. They indicate the type of wrong or conduct that the oppression remedy of s. 241 of the *CBCA* is aimed at. However, they do not represent watertight compartments, and often overlap and intermingle.

92 The original wrong recognized in the cases was described simply as oppression, and was generally associated with conduct that has variously been described as "burdensome, harsh and wrongful", "a visible departure from standards of fair dealing", and an "abuse of power" going to the probity of how the corporation's affairs are being conducted: see Koehnen, at p. 81. It is this wrong that gave the remedy its name, which now is generally used to cover all s. 241 claims. However, the term also operates to connote a particular type of injury within the modern rubric of oppression generally - a wrong of the most serious sort.

93 The *CBCA* has added "unfair prejudice" and "unfair disregard" of interests to the original common law concept, making it clear that wrongs falling short of the harsh and abusive conduct connoted by "oppression" may fall within s. 241. "[U]nfair prejudice" is generally seen as involving conduct less offensive than "oppression". Examples include squeezing out a minority shareholder, failing to disclose related party transactions, changing corporate structure to drastically alter debt ratios, adopting a "poison pill" to prevent a takeover bid, paying dividends without a formal declaration, preferring some shareholders with management fees and paying directors' fees higher than the industry norm: see Koehnen, at pp. 82-83.

94 "[U]nfair disregard" is viewed as the least serious of the three injuries, or wrongs, mentioned in s. 241. Examples include favouring a director by failing to properly prosecute claims, improperly reducing a shareholder's dividend, or failing to deliver property belonging to the claimant: see Koehnen, at pp. 83-84.

(2) Application to these Appeals

95 As discussed above (at para. 68), in assessing a claim for oppression a court must answer two questions: (1) Does the evidence support the reasonable expectation the claimant asserts? and (2) Does the evidence establish that the reasonable expectation was violated by conduct falling within the terms "oppression", "unfair prejudice" or "unfair disregard" of a relevant interest?

96 The debentureholders in this case assert two alternative expectations. Their highest position is that they had a reasonable expectation that the directors of BCE would protect their economic interests as debentureholders in Bell Canada by putting forward a plan of arrangement that would maintain the investment grade trading value of their debentures. Before this Court, however, they argued a softer alternative - a reasonable expectation that the directors would consider their economic interests in maintaining the trading value of the debentures.

97 As summarized above (at para. 25), the trial judge proceeded on the debentureholders' alleged expectation that the directors would act in a way that would preserve the investment grade status of their debentures. He concluded that this expectation was not made out on the evidence, since the statements by Bell Canada suggesting a commitment to retaining investment grade ratings were accompanied by warnings that explicitly precluded investors from reasonably forming such expectations, and the warnings were included in the prospectuses pursuant to which the debentures were issued.

98 The absence of a reasonable expectation that the investment grade of the debentures would be maintained was confirmed, in the trial judge's view, by the overall context of the relationship, the nature of the corporation, its situation as the target of a bidding war, as well as by the fact that the claimants could have protected themselves against reduction in market value by negotiating appropriate contractual terms.

99 The trial judge situated his consideration of the relevant factors in the appropriate legal context. He recognized that the directors had a fiduciary duty to act in the best interests of the corporation and that the content of this duty was affected by the various interests at stake in the context of the auction process that BCE was undergoing. He emphasized that the directors, faced with conflicting interests, might have no choice but to approve transactions that, while in the best interests of the corporation, would benefit some groups at the expense of others. He held that the fact that the shareholders stood to benefit from the transaction and that the debentureholders were prejudiced did not in itself give rise to a conclusion that the directors had breached their fiduciary duty to the corporation. All three competing bids required Bell Canada to assume additional debt, and there was no evidence that bidders were prepared to accept less leveraged debt. Under the business judgment rule, deference should be accorded to business decisions of directors taken in good faith and in the performance of the functions they were elected to perform by the shareholders.

100 We see no error in the principles applied by the trial judge nor in his findings of fact, which were amply supported by the evidence. We accordingly agree that the first expectation advanced in

this case - that the investment grade status of the debentures would be maintained - was not established.

101 The alternative, softer, expectation advanced is that the directors would consider the interests of the bondholders in maintaining the trading value of the debentures. The Court of Appeal, albeit in the context of its reasons on the s. 192 application, accepted this as a reasonable expectation. It held that the representations made over the years, while not legally binding, created expectations beyond contractual rights. It went on to state that in these circumstances, the directors were under a duty, not simply to accept the best offer, but to consider whether the arrangement could be restructured in a way that provided a satisfactory price to the shareholders while avoiding an adverse effect on debentureholders.

102 The evidence, objectively viewed, supports a reasonable expectation that the directors would consider the position of the debentureholders in making their decisions on the various offers under consideration. As discussed above, reasonable expectations for the purpose of a claim of oppression are not confined to legal interests. Given the potential impact on the debentureholders of the transactions under consideration, one would expect the directors, acting in the best interests of the corporation, to consider their short and long-term interests in the course of making their ultimate decision.

103 Indeed, the evidence shows that the directors did consider the interests of the debentureholders. A number of debentureholders sent letters to the Board, expressing concern about the proposed leveraged buyout and seeking assurances that their interests would be considered. One of the directors, Mr. Pattison, met with Phillips, Hager & North, representatives of the debentureholders. The directors' response to these overtures was that the contractual terms of the debentures would be met, but no additional assurances were given.

104 It is apparent that the directors considered the interests of the debentureholders and, having done so, concluded that while the contractual terms of the debentures would be honoured, no further commitments could be made. This fulfilled the duty of the directors to consider the debentureholders' interests. It did not amount to "unfair disregard" of the interests of the debentureholders. As discussed above, it may be impossible to satisfy all stakeholders in a given situation. In this case, the Board considered the interests of the claimant stakeholders. Having done so, and having considered its options in the difficult circumstances it faced, it made its decision, acting in what it perceived to be the best interests of the corporation.

105 What the claimants contend for on this appeal, in reality, is not merely an expectation that their interests be considered, but an expectation that the Board would take further positive steps to restructure the purchase in a way that would provide a satisfactory purchase price to the shareholders and preserve the high market value of the debentures. At this point, the second, softer expectation asserted approaches the first alleged expectation of maintaining the investment grade rating of the debentures.

106 The difficulty with this proposition is that there is no evidence that it was reasonable to suppose it could have been achieved. BCE, facing certain takeover, acted reasonably to create a competitive bidding process. The process attracted three bids. All of the bids were leveraged, involving a substantial increase in Bell Canada's debt. It was this factor that posed the risk to the trading value of the debentures. There is no evidence that BCE could have done anything to avoid that risk. Indeed, the evidence is to the contrary.

107 We earlier discussed the factors to consider in determining whether an expectation is reasonable on a s. 241 oppression claim. These include commercial practice; the size, nature and structure of the corporation; the relationship between the parties; past practice; the failure to negotiate protections; agreements and representations; and the fair resolution of conflicting interests. In our view, all these factors weigh against finding an expectation beyond honouring the contractual obligations of the debentures in this particular case.

108 Commercial practice - indeed commercial reality - undermines the claim that a way could have been found to preserve the trading position of the debentures in the context of the leveraged buyout. This reality must have been appreciated by reasonable debentureholders. More broadly, two considerations are germane to the influence of general commercial practice on the reasonableness of the debentureholders' expectations. First, leveraged buyouts of this kind are not unusual or unforeseeable, although the transaction at issue in this case is noteworthy for its magnitude. Second, trust indentures can include change of control and credit rating covenants where those protections have been negotiated. Protections of that type would have assured debentureholders a right to vote, potentially through their trustee, on the leveraged buyout, as the trial judge pointed out. This failure to negotiate protections was significant where the debentureholders, it may be noted, generally represent some of Canada's largest and most reputable financial institutions, pension funds and insurance companies.

109 The nature and size of the corporation also undermine the reasonableness of any expectation that the directors would reject the offers that had been presented and seek an arrangement that preserved the investment grade rating of the debentures. As discussed above (at para. 74), courts may accord greater latitude to the reasonableness of expectations formed in the context of a small, closely held corporation, rather than those relating to interests in a large, public corporation. Bell Canada had become a wholly owned subsidiary of BCE in 1983, pursuant to a plan of arrangement which saw the shareholders of Bell Canada surrender their shares in exchange for shares of BCE. Based upon the history of the relationship, it should not have been outside the contemplation of debentureholders acquiring debentures of Bell Canada under the 1996 and 1997 trust indentures, that arrangements of this type had occurred and could occur in the future.

110 The debentureholders rely on past practice, suggesting that investment grade ratings had always been maintained. However, as noted, reasonable practices may reflect changing economic and market realities. The events that precipitated the leveraged buyout transaction were such realities. Nor did the trial judge find in this case that representations had been made to debentureholders upon which they could have reasonably relied.

111 Finally, the claim must be considered from the perspective of the duty on the directors to resolve conflicts between the interests of corporate stakeholders in a fair manner that reflected the best interests of the corporation.

112 The best interests of the corporation arguably favoured acceptance of the offer at the time. BCE had been put in play, and the momentum of the market made a buyout inevitable. The evidence, accepted by the trial judge, was that Bell Canada needed to undertake significant changes to continue to be successful, and that privatization would provide greater freedom to achieve its long-term goals by removing the pressure on short-term public financial reporting, and bringing in equity from sophisticated investors motivated to improve the corporation's performance. Provided that, as here, the directors' decision is found to have been within the range of reasonable choices that

they could have made in weighing conflicting interests, the court will not go on to determine whether their decision was the perfect one.

113 Considering all the relevant factors, we conclude that the debentureholders have failed to establish a reasonable expectation that could give rise to a claim for oppression. As found by the trial judge, the alleged expectation that the investment grade of the debentures would be maintained is not supported by the evidence. A reasonable expectation that the debentureholders' interests would be considered is established, but was fulfilled. The evidence does not support a further expectation that a better arrangement could be negotiated that would meet the exigencies that the corporation was facing, while better preserving the trading value of the debentures.

114 Given that the debentureholders have failed to establish that the expectations they assert were reasonable, or that they were not fulfilled, it is unnecessary to consider in detail whether conduct complained of was oppressive, unfairly prejudicial, or unfairly disregarded the debentureholders' interests within the terms of s. 241 of the *CBCA*. Suffice it to say that "oppression" in the sense of bad faith and abuse was not alleged, much less proved. At best, the claim was for "unfair disregard" of the interests of the debentureholders. As discussed, the evidence does not support this claim.

C. *The Section 192 Approval Process*

115 The second remedy relied on by the debentureholders is the approval process for complex corporate arrangements set out under s. 192 of the *CBCA*. BCE brought a petition for court approval of the plan under s. 192. At trial, the debentureholders were granted standing to contest such approval. The trial judge concluded that "[i]t seemed "only logical and 'fair' to conduct this analysis having regard to the interests of BCE and those of its shareholders and other stakeholders, if any, whose interests are being arranged or affected" ((2008), 43 B.L.R. (4th) 1, 2008 QCCS 905, at para. 151). On the basis of Corporations Canada's *Policy concerning Arrangements under Section 192 of the CBCA*, November 2003 ("Policy Statement 15.1"), the trial judge held that the s. 192 approval did not require the Board to afford the debentureholders the right to vote. He nonetheless considered their interests in assessing the fairness of the arrangement. After a full hearing, he approved the arrangement as "fair and reasonable", despite the debentureholders' objections that the arrangement would adversely affect the trading value of their securities.

116 The Court of Appeal reversed this decision, essentially on the ground that the directors had not given adequate consideration to the debentureholders' reasonable expectations. These expectations, in its view, extended beyond the debentureholders' legal rights and required the directors to consider whether the adverse impact on the debentureholders' economic interests could be alleviated or attenuated. The court held that the corporation had failed to discharge the burden of showing that it was impossible to structure the sale in a manner that avoided the adverse economic effect on debentureholdings, and consequently had failed to establish that the proposed plan of arrangement was fair and reasonable.

117 Before considering what must be shown to obtain approval of an arrangement under s. 192, it may be helpful to briefly return to the differences between an action for oppression under s. 241 of the *CBCA* and a motion for approval of an arrangement under s. 192 of the *CBCA* alluded to earlier.

118 As we have discussed (at para. 47), the reasoning of the Court of Appeal effectively incorporated the s. 241 oppression claim into the s. 192 approval proceeding, converting it into an inquiry based on reasonable expectations.

119 As we view the matter, the s. 241 oppression remedy and the s. 192 approval process are different proceedings, with different requirements. While a conclusion that the proposed arrangement has an oppressive result may support the conclusion that the arrangement is not fair and reasonable under s. 192, it is important to keep in mind the differences between the two remedies. The oppression remedy is a broad and equitable remedy that focuses on the reasonable expectations of stakeholders, while the s. 192 approval process focuses on whether the arrangement, objectively viewed, is fair and reasonable and looks primarily to the interests of the parties whose legal rights are being arranged. Moreover, in an oppression proceeding, the onus is on the claimant to establish oppression or unfairness, while in a s. 192 proceeding, the onus is on the corporation to establish that the arrangement is "fair and reasonable".

120 These differences suggest that it is possible that a claimant might fail to show oppression under s. 241, but might succeed under s. 192 by establishing that the corporation has not discharged its onus of showing that the arrangement in question is fair and reasonable. For this reason, it is necessary to consider the debentureholders' s. 192 claim on these appeals, notwithstanding our earlier conclusion that the debentureholders have not established oppression.

121 Whether the converse is true is not at issue in these proceedings and need not detain us. It might be argued that in theory, a finding of s. 241 oppression could be coupled with approval of an arrangement as fair and reasonable under s. 192, given the different allocations of burden of proof in the two actions and the different perspectives from which the assessment is made. On the other hand, common sense suggests, as did the Court of Appeal, that a finding of oppression sits ill with the conclusion that the arrangement involved is fair and reasonable. We leave this interesting question to a case where it arises.

(1) The Requirements for Approval under Section 192

122 We will first describe the nature and purpose of the s. 192 approval process. We will then consider the philosophy that underlies s. 192 approval; the interests at play in the process; and the criteria to be applied by the judge on a s. 192 proceeding.

(a) *The Nature and Purpose of the Section 192 Procedure*

123 The s. 192 approval process has its genesis in 1923 legislation designed to permit corporations to modify their share capital: *Companies Act Amending Act, 1923*, S.C. 1923, c. 39, s. 4. The legislation's concern was to permit changes to shareholders' rights, while offering shareholders protection. In 1974, plans of arrangements were omitted from the *CBCA* because Parliament considered them superfluous and feared that they could be used to squeeze out minority shareholders. Upon realizing that arrangements were a practical and flexible way to effect complicated transactions, an arrangement provision was reintroduced in the *CBCA* in 1978: Consumer and Corporate Affairs Canada, *Detailed background paper for an Act to amend the Canada Business Corporations Act* (1977), p. 5 ("Detailed Background Paper").

124 In light of the flexibility it affords, the provision has been broadened to deal not only with reorganization of share capital, but corporate reorganization more generally. Section 192(1) of the

present legislation defines an arrangement under the provision as including amendments to articles, amalgamation of two or more corporations, division of the business carried on by a corporation, privatization or "squeeze-out" transactions, liquidation or dissolution, or any combination of these.

125 This list of transactions is not exhaustive and has been interpreted broadly by courts. Increasingly, s. 192 has been used as a device for effecting changes of control because of advantages it offers the purchaser: C. C. Nicholls, *Mergers, Acquisitions, and Other Changes of Corporate Control* (2007), at p. 76. One of these advantages is that it permits the purchaser to buy shares of the target company without the need to comply with provincial takeover bid rules.

126 The s. 192 process is generally applicable to change of control transactions that share two characteristics: the arrangement is sponsored by the directors of the target company; and the goal of the arrangement is to require some or all of the shareholders to surrender their shares to either the purchaser or the target company.

127 Fundamentally, the s. 192 procedure rests on the proposition that where a corporate transaction will alter the rights of security holders, this impact takes the decision out of the scope of management of the corporation's affairs, which is the responsibility of the directors. Section 192 overcomes this impediment through two mechanisms. First, proposed arrangements generally can be submitted to security holders for approval. Although there is no explicit requirement for a security holder vote in s. 192, as will be discussed below, these votes are an important feature of the process for approval of plans of arrangement. Second, the plan of arrangement must receive court approval after a hearing in which parties whose rights are being affected may partake.

(b) *The Philosophy Underlying Section 192*

128 The purpose of s. 192, as we have seen, is to permit major changes in corporate structure to be made, while ensuring that individuals and groups whose rights may be affected are treated fairly. In conducting the s. 192 inquiry, the judge must keep in mind the spirit of s. 192, which is to achieve a fair balance between conflicting interests. In discussing the objective of the arrangement provision introduced into the *CBCA* in 1978, the Minister of Consumer and Corporate Affairs stated:

> ... the Bill seeks to achieve a fair balance between flexible management and equitable treatment of minority shareholders in a manner that is consonant with the other fundamental change institutions set out in Part XIV.
>
> (Detailed Background Paper, at p. 6)

129 Although s. 192 was initially conceived as permitting and has principally been used to permit useful restructuring while protecting minority shareholders against adverse effects, the goal of ensuring a fair balance between different constituencies applies with equal force when considering the interests of non-shareholder security holders recognized under s. 192. Section 192 recognizes that major changes may be appropriate, even where they have an adverse impact on the rights of particular individuals or groups. It seeks to ensure that the interests of these rights holders are considered and treated fairly, and that in the end the arrangement is one that should proceed.

(c) *Interests Protected by Section 192*

130 The s. 192 procedure originally was aimed at protecting shareholders affected by corporate restructuring. That remains a fundamental concern. However, this aim has been subsequently broadened to protect other security holders in some circumstances.

131 Section 192 clearly contemplates the participation of security holders in certain situations. Section 192(1)(*f*) specifies that an arrangement may include an exchange of securities for property. Section 192(4)(*c*) provides that a court can make an interim order "requiring a corporation to call, hold and conduct a meeting of holders of securities ...". The Director appointed under the *CBCA* takes the view that, at a minimum, all security holders whose legal rights stand to be affected by the transaction should be permitted to vote on the arrangement: Policy Statement 15.1, s. 3.08.

132 A difficult question is whether s. 192 applies only to security holders whose *legal rights* stand to be affected by the proposal, or whether it applies to security holders whose legal rights remain intact but whose *economic interests* may be prejudiced.

133 The purpose of s. 192, discussed above, suggests that only security holders whose legal rights stand to be affected by the proposal are envisioned. As we have seen, the s. 192 procedure was conceived and has traditionally been viewed as aimed at permitting a corporation to make changes that affect the *rights* of the parties. It is the fact that rights are being altered that places the matter beyond the power of the directors and creates the need for shareholder and court approval. The distinction between the focus on legal rights under arrangement approval and reasonable expectations under the oppression remedy is a crucial one. The oppression remedy is grounded in unfair treatment of stakeholders, rather than on legal rights in their strict sense.

134 This general rule, however, does not preclude the possibility that in some circumstances, for example threat of insolvency or claims by certain minority shareholders, interests that are not strictly legal should be considered: see Policy Statement 15.1, s. 3.08, referring to "extraordinary circumstances".

135 It is not necessary to decide on these appeals precisely what would amount to "extraordinary circumstances" permitting consideration of non-legal interests on a s. 192 application. In our view, the fact that a group whose legal rights are left intact faces a reduction in the trading value of its securities would generally not, without more, constitute such a circumstance.

(d) *Criteria for Court Approval*

136 Section 192(3) specifies that the corporation must obtain court approval of the plan. In determining whether a plan of arrangement should be approved, the court must focus on the terms and impact of the arrangement itself, rather than on the process by which it was reached. What is required is that the arrangement itself, viewed substantively and objectively, be suitable for approval.

137 In seeking approval of an arrangement, the corporation bears the onus of satisfying the court that: (1) the statutory procedures have been met; (2) the application has been put forward in good faith; and (3) the arrangement is fair and reasonable: see *Trizec Corp., Re* (1994), 21 Alta. L.R. (3d) 435 (Q.B.), at p. 444. This may be contrasted with the s. 241 oppression action, where the onus is on the claimant to establish its case. On these appeals, it is conceded that the corporation satisfied the first two requirements. The only question is whether the arrangement is fair and reasonable.

138 In reviewing the directors' decision on the proposed arrangement to determine if it is fair and reasonable under s. 192, courts must be satisfied that (a) the arrangement has a valid business purpose, and (b) the objections of those whose legal rights are being arranged are being resolved in a fair and balanced way. It is through this two-pronged framework that courts can determine whether a plan is fair and reasonable.

139 In the past, some courts have answered the question of whether an arrangement is fair and reasonable by applying what is referred to as the business judgment test, that is whether an intelligent and honest business person, as a member of the voting class concerned and acting in his or her own interest would reasonably approve the arrangement: see *Trizec*, at p. 444; *Pacifica Papers Inc. v. Johnstone* (2001), 15 B.L.R. (3d) 249, 2001 BCSC 1069. However, while this consideration may be important, it does not constitute a useful or complete statement of what must be considered on a s. 192 application.

140 First, the fact that the business judgment test referred to here and the business judgment rule discussed above (at para. 40) are so similarly named leads to confusion. The business judgment *rule* expresses the need for deference to the business judgment of directors as to the best interests of the corporation. The business judgment *test* under s. 192, by contrast, is aimed at determining whether the proposed arrangement is fair and reasonable, having regard to the corporation and relevant stakeholders. The two inquiries are quite different. Yet the use of the same terminology has given rise to confusion. Thus, courts have on occasion cited the business judgment test while saying that it stands for the principle that arrangements do not have to be perfect, i.e. as a deference principle: see *Abitibi-Consolidated Inc. (Arrangement relatif à)*, [2007] Q.J. No. 16158 (QL), 2007 QCCS 6830. To conflate the business judgment test and the business judgment rule leads to difficulties in understanding what "fair and reasonable" means and how an arrangement may satisfy this threshold.

141 Second, in instances where affected security holders have voted on a plan of arrangement, it seems redundant to ask what an intelligent and honest business person, as a member of the voting class concerned and acting in his or her own interest, would do. As will be discussed below (at para. 150), votes on arrangements are an important indicator of whether a plan is fair and reasonable. However, the business judgment test does not provide any more information than does the outcome of a vote. Section 192 makes it clear that the reviewing judge must delve beyond whether a reasonable business person would approve of a plan to determine whether an arrangement is fair and reasonable. Insofar as the business judgment test suggests that the judge need only consider the perspective of the majority group, it is incomplete.

142 In summary, we conclude that the business judgment test is not useful in the context of a s. 192 application, and indeed may lead to confusion.

143 The framework proposed in these reasons reformulates the s. 192 test for what is fair and reasonable in a way that reflects the logic of s. 192 and the authorities. Determining what is fair and reasonable involves two inquiries: first, whether the arrangement has a valid business purpose; and second, whether it resolves the objections of those whose rights are being arranged in a fair and balanced way. In approving plans of arrangement, courts have frequently pointed to factors that answer these two questions as discussed more fully below: *Canadian Pacific Ltd. (Re)* (1990), 73 O.R. (2d) 212 (H.C.); *Cinar Corp. v. Shareholders of Cinar Corp.* (2004), 4 C.B.R. (5th) 163 (Que. Sup. Ct.); *PetroKazakhstan Inc. v. Lukoil Overseas Kumkol B.V.* (2005), 12 B.L.R. (4th) 128, 2005 ABQB 789.

144 We now turn to a more detailed discussion of the two prongs.

145 The valid business purpose prong of the fair and reasonable analysis recognizes the fact that there must be a positive value to the corporation to offset the fact that rights are being altered. In other words, courts must be satisfied that the burden imposed by the arrangement on security holders is justified by the interests of the corporation. The proposed plan of arrangement must further the interests of the corporation as an ongoing concern. In this sense, it may be narrower than the "best interests of the corporation" test that defines the fiduciary duty of directors under s. 122 of the *CBCA* (see paras. 38-40).

146 The valid purpose inquiry is invariably fact-specific. Thus, the nature and extent of evidence needed to satisfy this requirement will depend on the circumstances. An important factor for courts to consider when determining if the plan of arrangement serves a valid business purpose is the necessity of the arrangement to the continued operations of the corporation. Necessity is driven by the market conditions that a corporation faces, including technological, regulatory and competitive conditions. Indicia of necessity include the existence of alternatives and market reaction to the plan. The degree of necessity of the arrangement has a direct impact on the court's level of scrutiny. Austin J. in *Canadian Pacific* concluded that

> while courts are prepared to assume jurisdiction notwithstanding a lack of necessity on the part of the company, the lower the degree of necessity, the higher the degree of scrutiny that should be applied. [Emphasis added; p. 223.]

If the plan of arrangement is necessary for the corporation's continued existence, courts will more willingly approve it despite its prejudicial effect on some security holders. Conversely, if the arrangement is not mandated by the corporation's financial or commercial situation, courts are more cautious and will undertake a careful analysis to ensure that it was not in the sole interest of a particular stakeholder. Thus, the relative necessity of the arrangement may justify negative impact on the interests of affected security holders.

147 The second prong of the fair and reasonable analysis focuses on whether the objections of those whose rights are being arranged are being resolved in a fair and balanced way.

148 An objection to a plan of arrangement may arise where there is tension between the interests of the corporation and those of a security holder, or there are conflicting interests between different groups of affected rights holders. The judge must be satisfied that the arrangement strikes a fair balance, having regard to the ongoing interests of the corporation and the circumstances of the case. Often this will involve complex balancing, whereby courts determine whether appropriate accommodations and protections have been afforded to the concerned parties. However, as noted by Forsyth J. in *Trizec*, at para. 36:

> [T]he court must be careful not to cater to the special needs of one particular group but must strive to be fair to all involved in the transaction depending on the circumstances that exist. The overall fairness of any arrangement must be considered as well as fairness to various individual stakeholders.

149 The question is whether the plan, viewed in this light, is fair and reasonable. In answering this question, courts have considered a variety of factors, depending on the nature of the case at

hand. None of these alone is conclusive, and the relevance of particular factors varies from case to case. Nevertheless, they offer guidance.

150 An important factor is whether a majority of security holders has voted to approve the arrangement. Where the majority is absent or slim, doubts may arise as to whether the arrangement is fair and reasonable; however, a large majority suggests the converse. Although the outcome of a vote by security holders is not determinative of whether the plan should receive the approval of the court, courts have placed considerable weight on this factor. Voting results offer a key indication of whether those affected by the plan consider it to be fair and reasonable: *St. Lawrence & Hudson Railway Co. (Re)*, [1998] O.J. No. 3934 (QL) (Ont. Ct. (Gen. Div.)).

151 Where there has been no vote, courts may consider whether an intelligent and honest business person, as a member of the class concerned and acting in his or her own interest, might reasonably approve of the plan: *Re Alabama, New Orleans, Texas and Pacific Junction Railway Co.*, [1891] 1 Ch. 213 (C.A.); *Trizec.*

152 Other indicia of fairness are the proportionality of the compromise between various security holders, the security holders' position before and after the arrangement and the impact on various security holders' rights: see *Canadian Pacific*; *Trizec*. The court may also consider the repute of the directors and advisors who endorse the arrangement and the arrangement's terms. Thus, courts have considered whether the plan has been approved by a special committee of independent directors; the presence of a fairness opinion from a reputable expert; and the access of shareholders to dissent and appraisal remedies: see *Stelco Inc. (Re)* (2006), 18 C.B.R. (5th) 173 (Ont. S.C.J.); *Cinar*; *St. Lawrence & Hudson Railway*; *Trizec*; *Pacifica Papers*; *Canadian Pacific.*

153 This review of factors represents considerations that have figured in s. 192 cases to date. It is not meant to be exhaustive, but simply to provide an overview of some factors considered by courts in determining if a plan has reasonably addressed the objections and conflicts between different constituencies. Many of these factors will also indicate whether the plan serves a valid business purpose. The overall determination of whether an arrangement is fair and reasonable is fact-specific and may require the assessment of different factors in different situations.

154 We arrive then at this conclusion: in determining whether a plan of arrangement is fair and reasonable, the judge must be satisfied that the plan serves a valid business purpose and that it adequately responds to the objections and conflicts between different affected parties. Whether these requirements are met is determined by taking into account a variety of relevant factors, including the necessity of the arrangement to the corporation's continued existence, the approval, if any, of a majority of shareholders and other security holders entitled to vote, and the proportionality of the impact on affected groups.

155 As has frequently been stated, there is no such thing as a perfect arrangement. What is required is a reasonable decision in light of the specific circumstances of each case, not a perfect decision: *Trizec*; *Maple Leaf Foods*. The court on a s. 192 application should refrain from substituting their views of what they consider the "best" arrangement. At the same time, the court should not surrender their duty to scrutinize the arrangement. Because s. 192 facilitates the alteration of legal rights, the Court must conduct a careful review of the proposed transactions. As Lax J. stated in *UPM-Kymmene Corp. v. UPM-Kymmene Miramichi Inc.* (2002), 214 D.L.R. (4th) 496 (Ont. S.C.J.), at para. 153: "Although Board decisions are not subject to microscopic examination with the perfect vision of hindsight, they are subject to examination."

(2) Application to these Appeals

156 As discussed above (at paras. 137-38), the corporation on a s. 192 application must satisfy the court that: (1) the statutory procedures are met; (2) the application is put forward in good faith; and (3) the arrangement is fair and reasonable, in the sense that: (a) the arrangement has a valid business purpose; and (b) the objections of those whose rights are being arranged are resolved in a fair and balanced way.

157 The first and second requirements are clearly satisfied in this case. On the third element, the debentureholders no longer argue that the arrangement lacks a valid business purpose. The debate before this Court focuses on whether the objections of those whose rights are being arranged were resolved in a fair and balanced way.

158 The debentureholders argue that the arrangement does not address their rights in a fair and balanced way. Their main contention is that the process adopted by the directors in negotiating and concluding the arrangement failed to consider their interests adequately, in particular the fact that the arrangement, while upholding their contractual rights, would reduce the trading value of their debentures and in some cases downgrade them to below investment grade rating.

159 The first question that arises is whether the debentureholders' economic interest in preserving the trading value of their bonds was an interest that the directors were required to consider on the s. 192 application. We earlier concluded that authority and principle suggest that s. 192 is generally concerned with legal rights, absent exceptional circumstances. We further suggested that the fact that a group whose legal rights are left intact faces a reduction in the trading value of its securities would generally not constitute such a circumstance.

160 Relying on Policy Statement 15.1, the trial judge in these proceedings concluded that the debentureholders were not entitled to vote on the plan of arrangement because their legal rights were not being arranged; "[t]o do so would unjustly give [them] a veto over a transaction with an aggregate common equity value of approximately $35 billion that was approved by over 97% of the shareholders" (para. 166). Nevertheless, the trial judge went on to consider the debentureholders' perspective.

161 We find no error in the trial judge's conclusions on this point. Since only their economic interests were affected by the proposed transaction, not their legal rights, and since they did not fall within an exceptional situation where non-legal interests should be considered under s. 192, the debentureholders did not constitute an affected class under s. 192. The trial judge was thus correct in concluding that they should not be permitted to veto almost 98 percent of the shareholders simply because the trading value of their securities would be affected. Although not required, it remained open to the trial judge to consider the debentureholders' economic interests in his assessment of whether the arrangement was fair and reasonable under s. 192, as he did.

162 The next question is whether the trial judge erred in concluding that the arrangement addressed the debentureholders' interests in a fair and balanced way. The trial judge emphasized that the arrangement preserved the contractual rights of the debentureholders as negotiated. He noted that it was open to the debentureholders to negotiate protections against increased debt load or the risks of changes in corporate structure, had they wished to do so. He went on to state:

> ... the evidence discloses that [the debentureholders'] rights were in fact considered and evaluated. The Board concluded, justly so, that the terms of the 1976, 1996 and 1997 Trust Indentures do not contain change of control provisions, that there was not a change of control of Bell Canada contemplated and that, accordingly, the Contesting Debentureholders could not reasonably expect BCE to reject a transaction that maximized shareholder value, on the basis of any negative impact [on] them.
>
> ((2008), 43 B.L.R. (4th) 1, 2008 QCCS 905, at para. 162, quoting (2008), 43 B.L.R. (4th) 79, 2008 QCCS 907, at para. 199)

163 We find no error in these conclusions. The arrangement does not fundamentally alter the debentureholders' rights. The investment and the return contracted for remain intact. Fluctuation in the trading value of debentures with alteration in debt load is a well-known commercial phenomenon. The debentureholders had not contracted against this contingency. The fact that the trading value of the debentures stood to diminish as a result of the arrangement involving new debt was a foreseeable risk, not an exceptional circumstance. It was clear to the judge that the continuance of the corporation required acceptance of an arrangement that would entail increased debt and debt guarantees by Bell Canada: necessity was established. No superior arrangement had been put forward, and BCE had been assisted throughout by expert legal and financial advisors, suggesting that the proposed arrangement had a valid business purpose.

164 Based on these considerations, and recognizing that there is no such thing as a perfect arrangement, the trial judge concluded that the arrangement had been shown to be fair and reasonable. We see no error in this conclusion.

165 The Court of Appeal's contrary conclusion rested, as suggested above, on an approach that incorporated the s. 241 oppression remedy with its emphasis on reasonable expectations into the s. 192 arrangement approval process. Having found that the debentureholders' reasonable expectations (that their interests would be considered by the Board) were not met, the court went on to combine that finding with the s. 192 onus on the corporation. The result was to combine the substance of the oppression action with the onus of the s. 192 approval process. From this hybrid flowed the conclusion that the corporation had failed to discharge its burden of showing that it could not have met the alleged reasonable expectations of the debentureholders. This result could not have obtained under s. 241, which places the burden of establishing oppression on the claimant. By combining s. 241's substance with the reversed onus of s. 192, the Court of Appeal arrived at a conclusion that could not have been sustained under either provision, read on its own terms.

VI. Conclusion

166 We conclude that the debentureholders have failed to establish either oppression under s. 241 of the *CBCA* or that the trial judge erred in approving the arrangement under s. 192 of the *CBCA*.

167 For these reasons, the appeals are allowed, the decision of the Court of Appeal set aside, and the trial judge's approval of the plan of arrangement is affirmed with costs throughout. The cross-appeals are dismissed with costs throughout.

Solicitors:

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Solicitors for the appellant/respondent on cross-appeals 6796508 Canada Inc.: Woods & Partners, Montréal.

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cp/e/qlecl/qlaxc/qlaxw/qlana/qlrxg/qlhcs/qlbrl/qlced/qlhcs

[2006] W.D.F.L. 3681, 56 C.C.P.B. 1, 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 26 B.L.R. (4th) 43

2006 CarswellOnt 6292

Ivaco Inc., Re

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36.

AND IN THE MATTER OF A Plan or Plans of Compromise or Arrangement of **Ivaco Inc.** and the Applicants listed in Schedule "A"

Ontario Court of Appeal

J. Laskin, M. Rosenberg, J. Simmons JJ.A.

Heard: February 22, **2006**
Judgment: October 17, **2006**
Docket: CA C44455

Proceedings: affirming *Ivaco Inc., Re* (2005), 2005 CarswellOnt 3445, 47 C.C.P.B. 62, 12 C.B.R. (5th) 213 (Ont. S.C.J. [Commercial List])

Counsel: Frederick L. Myers, Jason Wadden for Appellant, Superintendent of Finance Services (Ontario)

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Peter F.C. Howard for Monitor, Ernst & Young Inc.

Subject: Insolvency; Estates and Trusts; Family; Property; Corporate and Commercial; Civil Practice and Procedure

[2006] W.D.F.L. 3681, 56 C.C.P.B. 1, 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 26 B.L.R. (4th) 43

Bankruptcy and insolvency --- Property of bankrupt -- Trust property -- General principles

Pension funds -- I Inc. and related companies, collectively I Group, had established various registered pension plans for their employees -- I Group became insolvent in 2003, and obtained protection under Companies' Creditors Arrangement Act ("CCAA") -- To facilitate restructuring of I Group, order was issued suspending unpaid past-service payments and special contributions I Group had been making to certain underfunded pension plans -- Restructuring was unsuccessful -- I Group's assets were sold -- Superintendent brought unsuccessful motion for order directing that portions of sale proceeds be used to satisfy unpaid pension obligations, which companies are deemed to hold in trust for beneficiaries of pension plans under Pension Benefits Act ("PBA") or, alternatively, for order segregating this amount in separate account -- Some of I Group's financial creditors brought partially successful motions for order lifting stay under CCAA and petitioning I Group into bankruptcy -- Stay was lifted, and bankruptcy petitions were allowed to proceed -- Superintendent appealed from dismissal of its motion -- Appeal dismissed -- Motions judge did not err in law in refusing to order immediate payment of amount of deemed trusts under PBA or in refusing to segregate that amount -- Combination of wording of s. 57 of PBA, paragraph 4 of pension stay order, and limited role of Monitor refuted Superintendent's argument that funds should have been segregated -- CCAA itself did not require motions judge to execute deemed trusts -- Because Federal legislative regime under CCAA and Bankruptcy and Insolvency Act determines claims of creditors of insolvent company, if rights of pension claimants are to be given greater priority, Parliament, not courts, must do so.

Pensions --- Payment of pension -- Bankruptcy or insolvency of employer -- Registered plans

I Inc. and related companies, collectively I Group, had established various registered pension plans for their employees -- I Group became insolvent in 2003, and obtained protection under Companies' Creditors Arrangement Act ("CCAA") -- To facilitate restructuring of I Group, order was issued suspending unpaid past-service payments and special contributions I Group had been making to certain underfunded pension plans -- Restructuring was unsuccessful -- I Group's assets were sold -- Superintendent brought unsuccessful motion for order directing that portions of sale proceeds be used to satisfy unpaid pension obligations, which companies are deemed to hold in trust for beneficiaries of pension plans under Pension Benefits Act ("PBA") or, alternatively, for order segregating this amount in separate account -- Some of I Group's financial creditors brought partially successful motions for order lifting stay under CCAA and petitioning I Group into bankruptcy -- Stay was lifted, and bankruptcy petitions were allowed to proceed -- Superintendent appealed from dismissal of its motion -- Appeal dismissed -- Motions judge did not err in law in refusing to order immediate payment of amount of deemed trusts under PBA or in refusing to segregate that amount -- Combination of wording of s. 57 of PBA, paragraph 4 of pension stay order, and limited role of Monitor refuted Superintendent's argument that funds should have been segregated -- Because Federal legislative regime under CCAA and Bankruptcy and Insolvency Act determines claims of creditors of insolvent company, if rights of pension claimants are to be given greater priority, Parliament, not courts, must do so -- Motions judge did not err in exercising his discretion to lift stay under CCAA and permit bankruptcy petition to proceed -- Superintendent's unfairness argument was not accepted.

Bankruptcy and insolvency --- Bankruptcy petitions for receiving orders -- Stay of petition -- General principles

I Inc. and related companies, collectively I Group, had established various registered pension plans for their employees -- I Group became insolvent in 2003, and obtained protection under Companies' Creditors Arrangement Act ("CCAA") -- To facilitate restructuring of I Group, order was issued suspending unpaid past-service payments and special contributions I Group had been making to certain underfunded pension plans -- Restructuring was unsuccessful -- I Group's assets were sold -- Superintendent brought unsuccessful motion for order directing that portions of sale proceeds be used to satisfy unpaid pension obligations, which companies are deemed to hold in trust for benefi-

ciaries of pension plans under Pension Benefits Act ("PBA") or, alternatively, for order segregating this amount in separate account -- Some of I Group's financial creditors brought partially successful motions for order lifting stay under CCAA and petitioning I Group into bankruptcy -- Stay was lifted, and bankruptcy petitions were allowed to proceed -- Superintendent appealed from dismissal of its motion -- Appeal dismissed -- Motions judge did not err in exercising his discretion to lift stay under CCAA and permit bankruptcy petition to proceed -- Motion judge's order lifting stay was discretionary order, and appellate review of discretionary order under CCAA is justified only for error in principle or unreasonable exercise of discretion -- Superintendent's unfairness argument was not accepted -- Numerous conditions supported motions judge's decision to lift stay and permit bankruptcy petitions to proceed -- Motions judge would have gone beyond his role as referee in CCAA proceedings if he had given effect to Superintendent's claim.

Bankruptcy and insolvency --- Practice and procedure in courts -- Orders -- Miscellaneous issues

I Inc. and related companies, collectively I Group, had established various registered pension plans for their employees -- I Group became insolvent in 2003, and obtained protection under Companies' Creditors Arrangement Act ("CCAA") -- To facilitate restructuring of I Group, order was issued suspending unpaid past-service payments and special contributions I Group had been making to certain underfunded pension plans -- Restructuring was unsuccessful and I Group's assets were sold -- Superintendent brought unsuccessful motion for order directing that portions of sale proceeds be used to satisfy unpaid pension obligations, which companies are deemed to hold in trust for beneficiaries of pension plans under Pension Benefits Act ("PBA") or, alternatively, for order segregating this amount in separate account -- Some of I Group's financial creditors brought partially successful motions for order lifting stay under CCAA and petitioning I Group into bankruptcy -- Stay was lifted, and bankruptcy petitions were allowed to proceed -- Motions judge made ancillary order to facilitate bankruptcy petitions, which ordered that head offices of two I Group companies be transferred from cities in Quebec to Toronto -- Superintendent appealed from ancillary order on basis that motions judge lacked jurisdiction under CCAA to make such order or, alternatively, improperly exercised his discretion in doing so -- Appeal dismissed -- Motions judge did not err in ordering that head offices of companies in question be transferred from Quebec to Toronto -- Argument that CCAA did not give motions judge jurisdiction to order transfer was accepted, but it was also accepted that transfer was not made to facilitate CCAA restructuring; instead, it was made to facilitate future bankruptcy proceedings -- Nonetheless, motions judge did not need to resort to CCAA because he had express authority to order transfer under Canada Business Corporations Act ("CBCA") -- Section 191 of CBCA gives court express authority to order transfer of head office of company that is subject to order under CCAA -- Motions judge properly exercised his discretion in ordering transfer.

Cases considered by *J. Laskin J.A.*:

> *Abraham v. Canadian Admiral Corp. (Receiver of)* (1998), 2 C.B.R. (4th) 243, 1998 CarswellOnt 1475, 158 D.L.R. (4th) 65, (sub nom. *Abraham v. Canadian Admiral Corp. (Receivership))* 109 O.A.C. 36, 39 O.R. (3d) 176, 37 C.C.E.L. (2d) 276, 19 C.C.P.B. 1, 13 P.P.S.A.C. (2d) 334 (Ont. C.A.) -- referred to
>
> *Air Canada, Re* (2003), 43 C.B.R. (4th) 1, 66 O.R. (3d) 257, 229 D.L.R. (4th) 687, 174 O.A.C. 201, 2003 CarswellOnt 2925 (Ont. C.A.) -- referred to
>
> *Algoma Steel Inc. v. Union Gas Ltd.* (2003), 169 O.A.C. 89, 39 C.B.R. (4th) 5, 2003 CarswellOnt 115, 63 O.R. (3d) 78 (Ont. C.A.) -- referred to
>
> *Bank of Montreal v. Scott Road Enterprises Ltd.* (1989), 36 B.C.L.R. (2d) 118, 73 C.B.R. (N.S.) 273, [1989] 4 W.W.R. 566, 57 D.L.R. (4th) 623, 1989 CarswellBC 337 (B.C. C.A.) -- referred to

Beatrice Foods Inc., Re (1996), 43 C.B.R. (4th) 10, 1996 CarswellOnt 5598 (Ont. Gen. Div. [Commercial List]) -- referred to

British Columbia v. Henfrey Samson Belair Ltd. (1989), 1989 CarswellBC 711, [1989] 1 T.S.T. 2164, 75 C.B.R. (N.S.) 1, [1989] 2 S.C.R. 24, 34 E.T.R. 1, [1989] 5 W.W.R. 577, 59 D.L.R. (4th) 726, 97 N.R. 61, 38 B.C.L.R. (2d) 145, 2 T.C.T. 4263, 1989 CarswellBC 351 (S.C.C.) -- considered

Dallas/North Group Inc., Re (1999), 17 C.B.R. (4th) 56, 1999 CarswellOnt 4720, 46 O.R. (3d) 602 (Ont. Gen. Div.) -- referred to

General Chemical Canada Ltd., Re (2005), 51 C.C.P.B. 297, 2005 CarswellOnt 7306, C.E.B. & P.G.R. 8179 (Ont. S.C.J.) -- considered

GMAC Commercial Credit Corp. - Canada v. TCT Logistics Inc. (2005), (sub nom. *TCT Logistics Inc. (Bankrupt), Re)* 194 O.A.C. 360, 2005 CarswellOnt 636, 7 C.B.R. (5th) 202, 74 O.R. (3d) 382 (Ont. C.A.) -- distinguished

Harrop of Milton Inc., Re (1979), 1979 CarswellOnt 185, 92 D.L.R. (3d) 535, 29 C.B.R. (N.S.) 289, 22 O.R. (2d) 239 (Ont. Bktcy.) -- referred to

Husky Oil Operations Ltd. v. Minister of National Revenue (1995), 1995 CarswellSask 739, 1995 CarswellSask 740, 188 N.R. 1, 24 C.L.R. (2d) 131, 35 C.B.R. (3d) 1, 128 D.L.R. (4th) 1, 137 Sask. R. 81, 107 W.A.C. 81, [1995] 3 S.C.R. 453, [1995] 10 W.W.R. 161 (S.C.C.) -- referred to

Ivaco Inc., Re (2004), 2004 CarswellOnt 3561 (Ont. S.C.J. [Commercial List]) -- referred to

Lambert, Re (2002), (sub nom. *Lambert (Bankrupt), Re)* 162 O.A.C. 132, 216 D.L.R. (4th) 330, 2002 CarswellOnt 2659, 36 C.B.R. (4th) 256, (sub nom. *Buth-na-bodhiaga Inc. v. Lambert)* 60 O.R. (3d) 787 (Ont. C.A.) -- referred to

Royal Crest Lifecare Group Inc., Re (2004), 2004 CarswellOnt 190, 181 O.A.C. 115, 46 C.B.R. (4th) 126, (sub nom. *Canadian Union of Public Employees, Locals 1712, 3009, 2225-05, 2225-06 & 2225-12 v. Ernst & Young Inc. (as trustee for Royal Crest Lifecare Group Inc.))* 2004 C.L.L.C. 220-014, (sub nom. *C.U.P.E., Locals 1712, 3009, 2225-05, 2225-06, 22512 v. Royal Crest Lifecare Group Inc. (Trustee of))* 98 C.L.R.B.R. (2d) 210 (Ont. C.A.) -- referred to

Stelco Inc., Re (2005), 253 D.L.R. (4th) 109, 75 O.R. (3d) 5, 2 B.L.R. (4th) 238, 9 C.B.R. (5th) 135, 2005 CarswellOnt 1188, 196 O.A.C. 142 (Ont. C.A.) -- distinguished

Toronto Dominion Bank v. Usarco Ltd. (1991), 42 E.T.R. 235, 1991 CarswellOnt 540 (Ont. Gen. Div.) -- distinguished

United Maritime Fishermen Co-op., Re (1988), 68 C.B.R. (N.S.) 170, 1988 CarswellNB 20, 87 N.B.R. (2d) 333, 221 A.P.R. 333 (N.B. Q.B.) -- referred to

Statutes considered:

Bank Act, S.C. 1991, c. 46

s. 427 -- referred to

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3

Generally -- referred to

s. 11(3) -- referred to

s. 11(4) -- referred to

s. 43(5) -- referred to

s. 43(7) -- referred to

s. 67(1)(a) -- referred to

Canada Business Corporations Act, R.S.C. 1985, c. C-44

s. 109(1) -- referred to

s. 173 -- referred to

s. 173(1)(b) -- considered

s. 191 -- considered

s. 191(1) -- considered

s. 191(1)(c) -- considered

s. 191(2) -- considered

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

Generally -- considered

s. 2 "debtor company" -- referred to

s. 11 -- referred to

s. 11.7(1) [en. 1997, c. 12, s. 124] -- referred to

s. 11.7(3) [en. 1997, c. 12, s. 124] -- referred to

s. 13 -- referred to

Pension Benefits Act, 1987, S.O. 1987, c. 35

Generally -- referred to

Pension Benefits Act, R.S.O. 1990, c. P.8

Generally -- referred to

s. 57 -- referred to

s. 57(3) -- considered

s. 57(4) -- considered

s. 57(5) -- considered

Wage Earner Protection Program Act, S.C. 2005, c. 47

Generally -- referred to

Regulations considered:

Truck Transportation Act, R.S.O. 1990, c. T.22

Load Brokers, O. Reg. 556/92

s. 15 -- referred to

s. 15(2) -- referred to

APPEAL by Superintendent from judgment, reported at *Ivaco Inc., Re* (2005), 2005 CarswellOnt 3445, 47 C.C.P.B. 62, 12 C.B.R. (5th) 213 (Ont. S.C.J. [Commercial List]), dismissing Superintendent's motion for order.

***J. Laskin J.A.*:**

A. Introduction

1 This appeal arises out of a priorities dispute between two groups of creditors of an insolvent company, Ivaco Inc., and its related group of companies. The dispute is over the sale proceeds of the assets of Ivaco. On one side of the dispute are the employees and retirees in Ivaco's underfunded non-union pension plans. They claim under the deemed trust and lien provisions of Ontario's *Pension Benefits Act*, R.S.O. 1990, c. P.8, ss. 57(3), (4) ("PBA"), and seek to recover unpaid contributions to the plans outside of bankruptcy. On the other side of the dispute are Ivaco's financial and trade creditors. They wish to put Ivaco into bankruptcy in order to take advantage of the scheme of distribution

under the federal *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("BIA"). The dispute arises because provincial deemed trusts do not, by virtue of that legislative designation, enjoy priority under the federal bankruptcy statute.

2 Ivaco and its related group of companies (collectively "the Companies") became insolvent in 2003. In September 2003, the Companies sought and obtained court-ordered protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("CCAA"). All claims of creditors were stayed. A later order stayed the Companies' obligation to pay the outstanding past service contributions and special payments to the non-union pension plans. (Past service contributions are monies due to fund benefits or benefit enhancements for pension members' past service; special payments are extraordinary payments made because a pension plan is underfunded).

3 The main purpose of CCAA proceedings is to facilitate the restructuring of an insolvent company so that it may stay in business. The Companies, however, were unable to restructure. In late 2004, virtually all of their assets were sold. All that remains is a pool of money: the proceeds of sale. All that remains to be done is to distribute this pool of money among the creditors.

4 The Superintendent of Financial Services, representing the employees and retirees, brought a motion for an order that part of the sale proceeds be used to satisfy the unpaid past service and special contributions, which the Companies are deemed to hold in trust for the beneficiaries of the pension plans under the PBA. Alternatively, the Superintendent sought an order segregating this amount in a separate account. The Quebec Pension Committee ("QPC"), the administrator of the largest non-union plan, supported the Superintendent's motion. Two of the Companies' lenders, the Bank of Nova Scotia and the National Bank, brought motions for an order lifting the stay under the CCAA and petitioning the Companies into bankruptcy.

5 Farley J., who had supervised these CCAA proceedings for over two and a half years, heard all three motions. By order dated July 18, 2005 he dismissed the Superintendent's motion and partly granted the banks' motions. He lifted the stay and permitted the bankruptcy petitions to proceed, but he did not put the Companies into bankruptcy.

6 The Superintendent appeals. She argues that the motions judge erred either in law or in the exercise of his discretion. The Superintendent submits that the motions judge erred in law by failing to order immediate payment of the amount of the deemed trusts or in failing to segregate this amount. The Superintendent contends that the PBA legally required that the deemed trusts for unpaid past service contributions and special payments be executed or protected before bankruptcy.

7 Alternatively, the Superintendent submits that the motions judge erred by exercising his discretion to lift the stay under the CCAA and permit the bankruptcy petitions to proceed without first protecting the claims of the pension beneficiaries. The Superintendent contends that the motions judge exercised his discretion on a wrong principle because he ignored the unfairness and prejudice to the Companies' most vulnerable creditors.

8 The Superintendent also appeals an ancillary order made by the motions judge. To facilitate the bankruptcy petitions, the motions judge ordered that the head offices of two of the Companies be transferred from cities in Quebec to Toronto. The Superintendent and the QPC submit that the motions judge had no jurisdiction under the CCAA to do so, or alternatively, improperly exercised his discretion in doing so.

9 This court granted leave to appeal under s. 13 of the CCAA. The court also stayed the two orders in favour of the banks pending the disposition of the appeal.

B. Relevant Facts and Chronology

[2006] W.D.F.L. 3681, 56 C.C.P.B. 1, 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 26 B.L.R. (4th) 43

a) The Companies

10 Six related corporations were granted protection under the CCAA: Ivaco Inc., Ivaco Rolling Mills Ltd. ("IRM"), Ifastgroupe Inc., Docap (1985) Corporation, Florida Sub One Holdings Inc. and 3632610 Canada Inc. Four of these corporations -- Ivaco, IRM, Ifastgroupe and Docap -- established the non-union pension plans in issue on this appeal.

11 Ivaco, IRM and Ifastgroupe ceased operations after their assets were sold. Only Docap now has any operating assets. Its assets consist mainly of inventory and accounts receivable that have not yet been sold. Docap is a small entity. Neither restructuring it nor selling it as a going concern seems a viable option. The National Bank, Docap's principal secured creditor, wishes to put the company into bankruptcy and liquidate its assets.

b) The non-union pension plans

12 The Companies had both a unionized and non-unionized workforce. They established various registered pension plans for their employees. These included four non-union plans: the Ivaco Salaried Plan, which is registered in Quebec and has both Quebec and Ontario members, the Designated Employees Plan, the Ingersoll Plan and the Docap Plan, all registered in Ontario.

13 The QPC administers the Ivaco Salaried Plan, which is the largest of the four plans. Ivaco formerly administered the other three plans. However, the Superintendent appointed PricewaterhouseCoopers Inc. as administrator of the Designated Employees Plan and the Ingersoll Plan. A former Ivaco employee administers the Docap Plan for Ivaco.

c) The initial stay under the CCAA

14 After their operations became financially troubled, the Companies sought and were granted protection from their creditors under the CCAA. On September 16, the motions judge granted a comprehensive stay of all creditor claims up to that time. He appointed Ernst & Young Inc. as Monitor. As a result of the stay, debts of the Companies existing on the date of the initial stay order have not been paid.

15 During the CCAA proceedings the Companies continued to pay the wages and benefits of all active employees. The Companies also continued to pay their current contributions to their various pension plans.

d) The pension stay order

16 When the Companies began CCAA proceedings, the non-union pension plans were underfunded. Before the initial stay order the Companies had been making both special payments and past services contributions to rectify this underfunding. Under the PBA, past service contributions accrue daily and are to be paid monthly.

17 Early in the CCAA proceedings, the Monitor concluded that the Companies would jeopardize their ability to restructure if they were required to continue making past service contributions and special payments. Because of the magnitude of these payments, the creditors would not agree to permit the DIP (debtor in possession) loan to be used for funding the pension plans. In their view, and in the view of the Monitor, doing so would imperil the possibility of restructuring. Relying on the Monitor's opinion, the Companies sought, and on November 28, 2003, were granted a pension stay order.

18 The motions judge relieved the Companies from making past service contributions or special payments to the underfunded non-union pension plans during the CCAA stay. No interested party, including both the Superintendent

and the QPC, opposed the order. All parties thought that relieving the Companies from making these payments would assist their restructuring efforts. The Companies still remained obligated to make current contributions to the non-union plans.

19 Paragraph 4 of the pension stay order stipulated that none of the Companies would incur any obligation because of the failure to make these past service contributions and special payments during the stay period:

> THIS COURT ORDERS that none of the Applicants or Partnerships, or their respective officers or directors shall incur any obligation, whether by way of debt, damages for breach of any duty, whether statutory, fiduciary, common law or otherwise, or for breach of trust, nor shall any trust be recognized, whether express, implied, constructive, resulting, deemed or otherwise, as a result of the failure of any person to make any contribution or payments other than current cost contribution obligations ("Current Contributions") during the Stay Period that they might otherwise have become required to make to any pension plans maintained by an Applicant or Partnership.

20 Paragraph 5 of the pension stay order expressly recognized that statutory deemed trust, liens or other charges may arise because the Companies were relieved from paying past service contributions but that they would not have priority over the charges in the initial stay order:

> THIS COURT ORDERS that if any claim, lien, charge or trust arises as a result of the failure of any Person to make any contribution or payment (other than Current Contributions) during the Stay Period that such Person might otherwise have become required to make to any pension plans maintained by an Applicant or Partnership but for the stay provided for herein, no such claim, lien, charge or trust shall be recognized in this proceeding or in any subsequent receivership, interim receivership or bankruptcy of any of the Applicants or Partnerships as having priority over the claims of the Charges as set out in the Amended and Restated order.

21 Paragraph 6 of the order recognized that the pension stay did not compromise the Companies' obligations under their non-union pension plans:

> Nothing in this Order shall be taken to extinguish or compromise the obligations of the Applicants and Partnerships, if any, regarding payments under the Pension Plans.

e) The sale to Heico

22 As the Companies were unable to restructure, they began to pursue a second option: selling their assets in a going concern sale. On August 18, 2004, the motions judge approved the sale of the assets of Ivaco, Ifastgroupe and IRM to the Heico Companies. As part of the transaction, the purchaser hired the Companies' unionized workforce and assumed the Companies' obligations to their unionized pension plans. The purchaser also hired almost all of the Companies' non-unionized workforce, but it was unwilling to assume the Companies' obligations to the four non-union pension plans. These obligations remained with the Companies.

23 Nonetheless, the Monitor supported the sale. In the Monitor's view, the sale gave the creditors and workers greater recovery and benefits than they would obtain in either a bankruptcy or a liquidation. Again, no party, including both the Superintendent and the QPC, opposed the sale.

24 The motions judge made two orders -- on August 18, 2004 [2004 CarswellOnt 3561 (Ont. S.C.J. [Commercial List])] and November 30, 2004 -- vesting the assets in the purchaser. These orders expressly preserved all claims that might have been made against the assets by providing that these claims could be made against the sale proceeds. In

accordance with these orders, the Monitor is holding the sale proceeds in various trust accounts.

25 In December 2004, Ivaco, IRM and Ifastgroupe wound-up their non-union pension plans. Under the PBA, they are obligated to fund the wind-up liabilities of these plans.

f) The pension claims

26 The Companies' non-union pension plans have been severely underfunded and the deficit has increased during the stay period. At the beginning of the CCAA proceedings in September 2003, unpaid past service contributions to the non-union plans totalled about $1.4 million and the solvency deficiency amounted to approximately $11.1 million. By December 2004 these figures had grown to approximately $11.6 million and $29.1 million respectively. They continued to grow while the pension stay order remained in place.

27 The potential loss of benefits for each pensioner is significant. Counsel for the Superintendent advised the court that the average pensioner in the non-union plans is sixty-seven years old and earns a pension of $14,000 per year. These pensioners will receive their full pension only if the full wind-up deficit is paid. For example, if the plans do not recover the past service contributions suspended by the pension stay order, the average monthly pension will be reduced by 26 per cent from approximately $1,200 to $888. If only unpaid contributions are recovered, and not the full solvency deficiency, the average pension will be reduced by 17 per cent to $996 monthly.

g) The claims of the financial creditors

28 The outstanding claims of the financial creditors of the Companies are also significant. We were told that the sale proceeds of the Companies' assets are insufficient to satisfy all claims, and are certainly insufficient to satisfy the unsecured claims.

29 The Bank of Nova Scotia was the lender to IRM. By October 2003, IRM owed the Bank about $40 million. IRM had ceased to meet its liabilities generally as they became due, and had given notice to its creditors that it had suspended payment of its debts. On October 3, 2003 the Bank issued a petition for a receiving order against IRM. The issuance of the petition was permitted by the initial stay order, but that proceeding was otherwise stayed. The order under appeal lifted the stay and permitted the Bank of Nova Scotia to proceed with its petition.

30 The National Bank lent money to Ivaco, Ifastgroupe and Docap. As of March 2005 it had a secured claim against Ivaco for $17 million,[FN1] and against Docap for $55,622 U.S. and $4.2 million Canadian. It also had an unsecured claim against Ifastgroupe for $45.5 million Canadian. Ifastgoupe is also indebted to La Caisse for $14.9 million.

31 A large number of other creditors also have claims against the Companies: Ivaco has 792 creditors with claims totalling $554.9 million; Docap has 82 creditors with claims totalling $111.1 million; and Ifastgroupe has 645 creditors with claims totalling $253.3 million.

C. Analysis

a) What is in issue on this appeal

32 The scope of this appeal is quite narrow. There are three issues:

1) Did the motions judge err in law in failing to order immediate payment of the amount of the deemed

trusts under the PBA or in failing to segregate this amount in a separate account?

2) Did the motions judge err in the exercise of his discretion by lifting the stay and permitting the bankruptcy petitions to proceed, without protecting the claims of the pension beneficiaries?

3) Did the motions judge err in law or in the exercise of his discretion by ordering the transfer of Ivaco's and Ifastgroupe's head offices from Quebec to Toronto?

b) What is not in issue on this appeal

33 There are also three issues raised by the parties that do not need to be decided on this appeal: (1) whether, outside of bankruptcy, the deemed trusts under the PBA have priority over the Bank of Nova Scotia's security under s. 427 of the *Bank Act*, S.C. 1991, c.46; (2) whether the Superintendent can show "sufficient cause" under s. 43(7) of the BIA to deny the application for a bankruptcy order; and, (3) whether the deemed trusts under the PBA also meet the requirements for a common law trust and thus on bankruptcy should be excluded from the property of the Companies under s. 67(1)(a) of the BIA.

34 On my view of the appeal, the first of these issues does not have to be resolved. It may become relevant at the bankruptcy hearing, and, if so, should be dealt with by the bankruptcy judge. See *Abraham v. Canadian Admiral Corp. (Receiver of)* (1998), 39 O.R. (3d) 176 (Ont. C.A.). The second and third issues, I assume, will be dealt with at the hearing of the bankruptcy petitions. Admittedly, the motions judge made some observations on these two issues. However, he also said, at para. 20 of his reasons, that he was not deciding either one:

> However, in the circumstances, I do not find it appropriate to allow (indeed direct) that there be an assignment in bankruptcy on a "voluntary basis" as there is the s. 43(7) issue to be determined. Similarly with respect to the balance of declarations requested by the National Bank, while I have made some general observations as to reversing priorities, it would not be appropriate to determine with finality the priorities of various claims on the record before me at this time.

35 In their written and oral submissions, the Superintendent and the QPC argued that some of the motions judge's general observations on these issues were wrong. I do not propose to consider these arguments because, as the motions judge recognized, they should be addressed at the hearing of the bankruptcy petitions. Instead, I will make a few brief observations of my own.

36 In my view, the motions judge appropriately considered what would likely happen at the bankruptcy hearing. He did so because the likely implications of lifting the stay were relevant considerations to the exercise of his discretion.

37 The motions judge observed, at para. 14, that the discretion to refuse to make a bankruptcy order under s. 43(7) typically is exercised in two categories of cases: where the petitioner has an ulterior motive in seeking the order, or where the order would not serve any meaningful purpose. This observation reflects the current state of the case law under s. 43(7). See for example *Dallas/North Group Inc., Re* (1999), 46 O.R. (3d) 602 (Ont. Gen. Div.); *Lambert, Re* (2002), 60 O.R. (3d) 787 (Ont. C.A.). Although the motions judge added that the Superintendent's claim does not appear to come within either category, he left the final determination of that question for the bankruptcy judge.

38 The motions judge also observed, at para. 11 of his reasons, that a provincially created deemed trust does not by that fact alone enjoy priority under the BIA. This is not a contentious proposition. In a series of cases, the Supreme Court of Canada has repeatedly said that a province cannot, by legislating a deemed trust, alter the scheme of priorities under the federal statute. See for example *British Columbia v. Henfrey Samson Belair Ltd.* , [1989] 2 S.C.R. 24

(S.C.C.); *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453 (S.C.C.). Indeed, it is this jurisprudence that undoubtedly prompted the Superintendent's original motion and appeal to this court.

39 The motions judge also correctly observed, at para. 11 of his reasons, that a provincial deemed trust will retained its priority in bankruptcy only if it also meets the three attributes -- the three certainties -- of a common law trust: certainty of intent; certainty of subject matter; and certainty of object. Only a trust that has these three attributes is a "true trust" that will be exempt from the bankrupt's estate under s. 67(1)(a) of the BIA. See for example *Henfrey Sampson, supra.* Whether the Superintendent can establish a true trust for unpaid past service contributions, even though the proceeds of the Heico sale have been commingled, will be decided at the bankruptcy hearing.

40 I now turn to the issues that do arise on this appeal.

c) Did the motions judge err in law in failing to order immediate payment of the amount of the deemed trusts or in failing to segregate this amount?

41 The Superintendent's principal submission is that the motions judge erred in law in failing to order payment of the amount of the deemed trusts before bankruptcy or in failing to order the Monitor to segregate this amount during the CCAA proceedings. The submission that the motions judge was legally required to order payment or segregation of the amount of the deemed trusts was not advanced before him. The Superintendent advanced this submission for the first time in this court. I do not agree with it.

42 I will deal first with whether the motions judge should have required the Monitor, Ernst & Young, to segregate the amount of the deemed trusts. The Superintendent contends that the Companies, and in their place the Monitor, had a statutory and fiduciary obligation to segregate. As the Monitor was an officer of the court, the motions judge should have compelled it to fulfill these duties. This contention faces three obstacles: the language of the PBA; the terms of the pension stay order; and the status and role of the Monitor.

43 The deemed trusts for unpaid past service and special contributions are found in ss. 57(3) and (4) of the PBA. Subsection (3) is the basic provision that creates a deemed trust for unpaid employer contributions. Subsection (4) stipulates that on the wind up of a pension plan, employer contributions accrued but not yet due because of the timing of the wind up are also deemed to be held in trust:

> s. 57(3) An employer who is required to pay contributions to a pension fund shall be deemed to hold in trust for the beneficiaries of the pension plan an amount of money equal to the employer contributions due and not paid into the pension fund.
>
> s. 57(4) Where a pension plan is wound up in whole or in part, an employer who is required to pay contributions to the pension fund shall be deemed to hold in trust for the beneficiaries of the pension plan an amount of money equal to employer contributions accrued to the date of the wind up but not yet due under the plan or regulations.

44 At para. 11 of his decision, the motions judge said that both unpaid contributions and wind-up liabilities are deemed to be held in trust under s. 57(3). In his earlier decision in *Toronto Dominion Bank v. Usarco Ltd.* (1991), 42 E.T.R. 235 (Ont. Gen. Div.), Farley J. said, at para. 25, that the equivalent legislation then in force under the *Pension Benefits Act, 1987*, S.O. 1987, c.35 referred only to unpaid contributions, not to wind-up liabilities. I think that the statement in *Usarco Ltd.* is correct, but I do not need to resolve the issue on this appeal.

45 Under s. 57(5) of the PBA the plan administrator has a lien and charge on the assets of the employer for the

amount of any deemed trust. The lien and charge permit the administrator to enforce the deemed trust.

> s. 57(5) The administrator of the pension plan has a lien and charge on the assets of the employer in an amount equal to the amounts deemed to be held in trust under subsections (1), (3) and (4).

46 The Superintendent argues that these provisions required the Companies, and in their place the Monitor, to keep the unpaid contributions in a separate account. However, the language of s. 57 does not require the employer to hold the contributions separately. A "deemed trust" is, in a sense, a legal fiction. Outside of bankruptcy it does create a priority for pension contributions, a priority that would not exist but for the designation. Yet, as I have already said, this legislative designation by itself does not create a true trust. If the province wants to require an employer to keep its unpaid contributions to a pension plan in a separate account it must legislate that separation. It has not done so.

47 The Superintendent argues that the pension stay order supports her position because para. 5 the order, *supra*, recognized that a deemed trust for unpaid contributions may arise during the stay period and that para. 6 of the stay order, *supra*, did not compromise the Companies' obligation to make these contributions. This argument fails to take account of para. 4 of the pension stay order. Paragraph 4 stipulates that during the stay the Companies will not incur any obligation -- statutory, fiduciary or otherwise -- for failing to make contributions to the plan. In my view, the Superintendent's argument amounts to an impermissible collateral attack on para. 4 of the pension stay order.

48 The Superintendent also tries to buttress her position by arguing that the Monitor stands in the shoes of the Companies, and like the Companies, has a fiduciary duty to the pension beneficiaries. I disagree.

49 The Monitor was appointed under s. 11.7(1) of the CCAA to "monitor the business and financial affairs" of the Companies, and was given the functions set out in s. 11.7(3) of that statute: to examine the Companies' property, report to the court on the Companies' business and financial affairs and keep the creditors informed. Although the motions judge gave the Monitor additional powers, they were limited. The Monitor was given authority to deal with day-to-day administrative matters, to finalize the sale to Heico and to receive and control the proceeds of sale. I do not think it can be fairly said that the Monitor "stands in the shoes of the Companies".

50 Equally important, the Monitor does not owe a fiduciary duty to the pension beneficiaries. The Superintendent's attempt to impose an obligation on the Monitor to segregate the contributions to the non-union plans depends at least on establishing that the Monitor acts as a fiduciary of the employees in those plans. Both the role of the Monitor and the initial stay order preclude the Superintendent's assertion.

51 Pension plan administrators do owe a fiduciary duty to plan members. See E.E. Gillese, *The Fiduciary Liability of the Employer as Pension Plan Administrator* (Toronto: The Canadian Institute, November 18, 1996, pp. 1-25). But the Monitor was not given that role. It is not an administrator of any of the four non-union plans. Indeed, the Superintendent never asked the court to give the Monitor responsibility for administering these plans.

52 Moreover, para. 59 of the initial stay order expressly states that the Monitor is not to be considered either a successor or related employer.

> THIS COURT ORDERS that nothing in this Order shall result in the Monitor being or being deemed or considered to be a successor or related employer, sponsor or payor with respect to any Applicant or any employees or former employees of any Applicant under any legislation, including ... the *Pension Benefits Act* (Ontario) ... or under any other provincial or federal legislation, regulation or rule of law or equity applicable to employees or pensions, or otherwise.

[Emphasis added].

As the Monitor was neither a plan administrator nor a successor employer, it can owe no fiduciary duty to the members of the four plans.

53 Therefore, the combination of the wording of s. 57 of the PBA, para. 4 of the pension stay order and the limited role of the Monitor, refute the Superintendent's segregation argument. The Superintendent, however, submits that two cases, the decision of this court in *GMAC Commercial Credit Corp. - Canada v. TCT Logistics Inc.* (2005), 74 O.R. (3d) 382 (Ont. C.A.) [hereinafter *TCT Logistics*] and an earlier decision of the motions judge in *Usarco Ltd.*, *supra*, support the argument for segregation. In my view, both cases are distinguishable.

54 In *TCT Logistics*, this court held that an interim receiver, who was both an officer of the court and stood in the shoes of the debtor, had a statutory duty under the legislation then in force, s. 15 of the *Load Brokers Regulation*, O.Reg. 556/92 (passed under the *Truck Transportation Act*, R.S.O. 1990, c. T.- 22) to hold carriers' fees that it had collected in a separate trust account. *TCT Logistics* and this case differ in three critical ways.

55 First, the interim receiver in *TCT Logistics*, was not just an officer of the court, it stood in the place of the debtor company. Here, although the Monitor is an officer of the court, it does not stand in the place of the Companies. For the reasons outlined in para. 49 its role is far more limited.

56 Second, in *TCT Logistics* the court order authorized the interim receiver to hold the carriers' fees in a separate bank account until entitlement to that money was decided. Here, the pension stay order prohibited the Companies from making any past service or special contributions during the stay period.

57 Third, and perhaps most important, the applicable legislation in *TCT Logistics*, s. 15(2) of the *Load Brokers Regulation* required the debtor company to maintain a separate trust account and to keep the fees it collected for the carriers in that account. Here, s. 57 of the PBA does not similarly require an employer to keep its unpaid contributions in a separate trust account. Moreover, in *TCT Logistics*, despite s. 15(2) of the Regulation, this court held that the carrier fees previously collected by the debtor company lost their character as trust money because they had been commingled with other funds. *TCT Logistics* thus does not support the Superintendent's position.

58 In *Usarco Ltd.*, *supra*, at para. 16, Farley J. commented that the deemed trust provisions of the PBA "implied a fiduciary obligation on the part of Usarco", and that "a trustee in bankruptcy stepping into the shoes of Usarco must deal with that fiduciary obligation". These comments do not apply to this case. The Monitor here, unlike the trustee in bankruptcy in *Usarco Ltd.*, did not step into the shoes of the debtor. Thus, *Usarco Ltd.* does not assist the Superintendent.

59 For these reasons, I reject the Superintendent's argument that the motions judge was required in law to order the segregation of the amount of the deemed trusts during the CCAA proceeding. I now turn to the Superintendent's other submission: that the motions judge was required in law to order that the amount of the deemed trust be paid at the end of the CCAA proceedings, but before bankruptcy.

60 The CCAA itself did not require the motions judge to execute the deemed trusts. The Superintendent cannot point to any section of the statute where a legal obligation to order payment of the past service contributions can be found. Moreover, in my view, absent an agreement, I doubt that the CCAA even authorized the motions judge to order this payment. Once restructuring was not possible and the CCAA proceedings were spent, as the motions judge found and all parties acknowledged, I question whether the court had any authority to order a distribution of the sale proceeds. See for example *United Maritime Fishermen Co-op., Re* (1988), 68 C.B.R. (N.S.) 170 (N.B. Q.B.), at 173.

61 The Superintendent's submission that the motions judge was required to order payment of the outstanding contributions rests on the proposition that a gap exists between the CCAA and the BIA in which the provincial deemed trusts can be executed. This proposition runs contrary to the federal bankruptcy and insolvency regime and to the principle that the province cannot reorder priorities in bankruptcy.

62 The federal insolvency regime includes the CCAA and the BIA. The two statutes are related. A debtor company under the CCAA is defined in s. 2 by the company's bankruptcy or insolvency. Section 11(3) authorizes a thirty-day stay of any current or prospective proceedings under the BIA, and s. 11(4) authorizes an extension of the initial thirty-day period. During the stay period, creditor claims and bankruptcy proceedings are suspended. Once the stay is lifted by court order or terminates by its own terms, simultaneously the creditor claims and bankruptcy proceedings are revived and may go forward.

63 For the Superintendent's position to be correct, there would have to be a gap between the end of the CCAA period and bankruptcy proceedings, in which the pension beneficiaries' rights under the deemed trusts crystallize before the rights of all other creditors, including their right to bring a bankruptcy petition. That position is illogical. All rights must crystallize simultaneously at the end of the CCAA period. There is simply no gap in the federal insolvency regime in which the provincial deemed trusts alone can operate. That is obviously so on the facts in this case because the Bank of Nova Scotia had already commenced a petition for bankruptcy, which was stayed by the initial order under the CCAA. Once the motions judge lifted the stay, the petition was revived. In my view, however, the situation would be the same even if no bankruptcy petition was pending.

64 Where a creditor seeks to petition a debtor company into bankruptcy at the end of CCAA proceedings, any claim under a provincial deemed trust must be dealt with in bankruptcy proceedings. The CCAA and the BIA create a complementary and interrelated scheme for dealing with the property of insolvent companies, a scheme that occupies the field and ousts the application of provincial legislation. Were it otherwise, creditors might be tempted to forgo efforts to restructure a debtor company and instead put the company immediately into bankruptcy. That would not be a desirable result.

65 Also, giving effect to the Superintendent's position, in substance, would allow a province to do indirectly what it is precluded from doing directly. Just as a province cannot directly create its own priorities or alter the scheme of distribution of property under the BIA, neither can it do so indirectly. See *Husky Oil*, *supra*, at paras. 32 and 39. At bottom the Superintendent seeks to alter the scheme for distributing an insolvent company's assets under the BIA. It cannot do so.

66 The Superintendent relies on one authority in support of its position: the decision of the motions judge in *Usarco Ltd.*, *supra*. In that case, although a bankruptcy petition had been brought, Farley J. nonetheless ordered the receiver to pay to the pension plan administrator the amount of the deemed trusts under the PBA. However, the facts in *Usarco Ltd.* differed materially from the facts in this case.

67 In *Usarco Ltd.*, CCAA proceedings did not precede the bankruptcy petition. Moreover, in *Usarco Ltd.* the petitioning creditor was not proceeding with its bankruptcy petition because its principal had died, and no other creditor took steps to advance the petition. Thus, unlike in this case, in *Usarco Ltd.* it was unclear whether bankruptcy proceedings would ever take place.

68 Recently in *General Chemical Canada Ltd., Re* (Ont. S.C.J.), Campbell J. relied on this distinction, followed the motions judge's decision in the present case and refused to order payment of the amount of the deemed trusts under the PBA. He wrote at para. 35:

> To conclude otherwise (absent improper motive on the part of Company or a major creditor) would be to negate both CCAA proceedings and bankruptcy proceedings by preventing creditors from pursuing a process of equitable distribution of the debtor's property as they believe it to be when making their decisions.

I agree. The factual differences between *General Chemical Canada Ltd.* and this case on the one hand, and *Usarco Ltd.* on the other, render *Usarco Ltd.* of no assistance to the Superintendent on this appeal.

69 Because the federal legislative regime under the CCAA and the BIA determines the claims of creditors of an insolvent company, if the rights of pension claimants are to be given greater priority, Parliament, not the courts, must do so. And Parliament has at least signalled its intention to do so. Last year it passed the *Wage Earner Protection Program Act*, S.C. 2005 c.47. That Act would amend the BIA and give special priority to unpaid pension contributions of a bankrupt employer. This statute, however, has not been proclaimed in force. That it was passed perhaps shows that under the existing legislative regime, claims like that of the Superintendent must fail. I would reject this ground of appeal.

d) Did the motions judge err in the exercise of his discretion by lifting the stay and permitting the bankruptcy petitions to proceed?

70 In my view, the motions judge's order lifting the stay was a discretionary order. He summarized his reasons for rejecting the Superintendent's position and exercising his discretion to allow the bankruptcy petitions to proceed at para. 18 of his decision:

> In the end result I do not see that the Superintendent has made a compelling case to the effect that the petitions in bankruptcy should not be allowed to proceed in the ordinary course. I have reached that conclusion by weighing the factors pro and con as discussed above, including the relative benefits to all stakeholders (including workers and pensioners) to maintaining the CCAA proceedings (with the benefit of the suspension of past contributions as per the unopposed and un-reconsidered order of November 28, 2003), the fact that no reorganization is now possible as all Ivaco Companies (except Docap) have ceased operations and are without operational assets and that the Ivaco Companies are now essentially in a distribution of proceeds mode.

71 Appellate review of a discretionary order under the CCAA is limited. See *Air Canada, Re* (2003), 66 O.R. (3d) 257 (Ont. C.A.) at para. 25; *Royal Crest Lifecare Group Inc., Re* (2004), 46 C.B.R. (4th) 126 (Ont. C.A.) at para. 23; *Algoma Steel Inc. v. Union Gas Ltd.* (2003), 63 O.R. (3d) 78 (Ont. C.A.) at para. 16. Appellate intervention is justified only for an error in principle or the unreasonable exercise of discretion. The Superintendent submits that the motions judge exercised his discretion improperly -- on a wrong principle -- because he ignored the "unfair and prejudicial" effects of his order on the Companies' most vulnerable class of creditors: the pension beneficiaries. I disagree.

72 The Superintendent argues that the motions judge's order was unfair to the pension beneficiaries in three related ways. First, she points out that the pension beneficiaries agreed to a stay of the past service contributions to keep the Companies afloat, which in turn permitted the going concern sale to Heico. That sale greatly enhanced the return to the creditors. The Superintendent contends that now permitting the bankruptcy petitions to proceed, which would potentially deprive the pension beneficiaries of their rights, produces an unfair outcome.

73 Undoubtedly, and regrettably, the pension beneficiaries stand to suffer from the insolvency of the Companies. However, the Superintendent's argument implicitly assumes that the pension beneficiaries alone made sacrifices to maximize the recovery for all creditors. The motions judge rejected this assumption, which he said at para. 2 of his

reasons, "somewhat overstates the situation". The motions judge accurately concluded:

> [O]ther stakeholders (such as the financial and trade creditors) as a result of the stay also contributed to the financial stability of the Ivaco Companies, fragile as their financial situation was, by not being paid interest as such became due nor for pre-filing indebtedness which was due.

In short, all creditors gave up something to permit the Companies to stay in business so that they could either reorganize or sell their assets in a going concern sale.

74 Second, the Superintendent contends that the motions judge's order undermined his earlier pension stay order, which had expressly preserved the pension beneficiaries' deemed trust rights. I do not accept this contention. Although the pension stay order did not take away these deemed trust rights, it did not provide that the deemed trusts would be paid out of any sale proceeds. Instead, para. 4 of the pension stay order provided that the Companies would not incur any obligation because of their failure to pay past service contributions during the stay period. Moreover, even though the Superintendent and the QPC knew that a petition for bankruptcy (by the Bank of Nova Scotia) was pending when they agreed to the pension stay order, they did not ask that the order be conditional on payment of the amount of the deemed trusts when the stay was lifted.

75 The third aspect of unfairness on which the Superintendent relies is that the motions judge's order fails to take account of the law's "special solicitude" for pensioners. Certainly provincial pension legislation has shown this solicitude. It has recognized the importance of ensuring that retirees have income security. Thus, it has legislated statutory trusts and liens to protect their pension claims. But federal insolvency law has not shown the same solicitude. It does not accord the claims of "sympathetic" creditors more weight than the claims of "unsympathetic" ones. Subject to specified exceptions, the BIA aims to distribute a bankrupt debtor's estate equitably among all of the estate's creditors. There are undoubtedly compelling policy reasons to protect pension rights in an insolvency. But, as I have said, it is for Parliament, not the courts, to do so.

76 Therefore, I do not accept the Superintendent's unfairness argument. Also, in my view, numerous considerations supported the motions judge's decision to lift the stay and permit the bankruptcy petitions to proceed. These considerations include the following:

- The CCAA proceedings are spent. There are no entities to reorganize and no further compromises can be negotiated between the Companies and their creditors. There remains only a pool of money to distribute. The BIA is the regime Parliament has chosen to effect this distribution.

- The petitioning creditors have met the technical requirements for bankruptcy. And their desire to use the BIA to alter priorities is a legitimate reason to seek a bankruptcy order. See for example *Bank of Montreal v. Scott Road Enterprises Ltd.* (1989), 57 D.L.R. (4th) 623 (B.C. C.A.), at 627, 630-631; *Harrop of Milton Inc., Re* (1979), 22 O.R. (2d) 239 (Ont. Bktcy.), at 244- 245.

- The Superintendent and the QPC agreed to the CCAA process. They recognized that it benefitted the pension claimants. Thus, they did not oppose either the pension stay order or the sale to Heico. They did not ask to have the deemed trusts satisfied or an amount to satisfy them set aside, though they knew that bankruptcy was pending. They likely recognized that if they had insisted on a segregation order, the other creditors may not have agreed to the sale. It is now too late for the Superintendent and the QPC to ask for relief that they never sought during the entire CCAA process.

- The motions judge would have gone beyond his role as a referee in the CCAA proceedings if he had given

> effect to the Superintendent's claim. The Superintendent wants to jump ahead of all the other creditors by obtaining an extraordinary payment at the end of a long CCAA process. If the motions judge had ordered this payment, he would have upset the ground rules that all stakeholders agreed to and that he supervised for over two years.

77 The motions judge took into account the likely result of the Superintendent's claims if the Companies are put into bankruptcy. He recognized that bankruptcy would potentially reverse the priority accorded to the pension claims outside bankruptcy. Nonetheless, having weighed all the competing considerations, he exercised his discretion to lift the stay and permit the bankruptcy petitions to proceed. In my view, he exercised his discretion properly. I would not give effect to this ground of appeal.

e) Did the motions judge err by ordering the transfer of Ivaco and Ifastgroupe's head offices from Quebec to Toronto?

78 Ivaco's head office was in Montreal; Ifastgroupe's head office was in Marieville, Quebec. The motions judge ordered that these head offices be transferred to Toronto. He did so in the light of s. 43(5) of the BIA, which states that an application for a bankruptcy petition shall be filed in the court having jurisdiction in the judicial district of the locality of the debtor. The Superintendent, supported by the QPC, submits that the motions judge had no jurisdiction to make this order, or that he improperly exercised his discretion in doing so. I disagree with both submissions.

79 The Superintendent and the QPC contend that the CCAA does not expressly authorize a judge to transfer the location of the head office of a debtor company. And, although a judge in CCAA proceedings has inherent jurisdiction to control the court's processes, the judge does not have a similar jurisdiction to do what the motions judge did here: control the debtor Companies' or the creditors' processes. See *Stelco Inc., Re* (2005), 75 O.R. (3d) 5 (Ont. C.A.) at para. 38.

80 I accept the Superintendent's and the QPC's contention that the CCAA did not give the motions judge jurisdiction to order the transfer. I also accept that the transfer was not made to facilitate a restructuring under the CCAA. Instead it was made to facilitate future bankruptcy proceedings. Nonetheless, in my view, the motions judge did not need to resort to the CCAA because he had express authority to order the transfer in s. 191 of the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44. Sections 191(1) and (2) provide:

> s. 191(1) In this section, "reorganization" means a court order made under;
>
> (a) section 241;
>
> (b) the *Bankruptcy and Insolvency Act* approving a proposal; or
>
> (c) any other Act of Parliament that affects the rights among the corporation, its shareholders and creditors.
>
> s. 191(2) If a corporation is subject to an order referred to in subsection (1), its articles may be amended by such order to effect any change that might be lawfully be made by an amendment under section 173.

81 The applicable section here is section 191(1)(c). The stay order is an order under an Act of Parliament, the CCAA, that affects the rights among the Companies, its shareholders and its creditors. See *Beatrice Foods Inc., Re* (1996), 43 C.B.R. (4th) 10 (Ont. Gen. Div. [Commercial List]). Therefore, as both Ivaco and Ifastgroupe were subject

to an order under s. 191(1)(c) of the CBCA, under s. 191(2) each of its articles may be amended to effect any change that might be made by an amendment under s. 173. Section 173(1)(b) of the statute permits a corporation to change the location of its head office:

> s. 173(1) Subject to sections 176 and 177, the articles of a corporation may by special resolution be amended to
>
> . . . . .
>
> (b) change the province in which its registered office is situated;

82 On my reading of the statute, s. 191 is a stand-alone section that gave the motions judge authority to order the transfer. Provided a corporation is subject to an order under s. 191(1), its articles may be amended. The amending order under s. 191(2) need not serve the purpose of the triggering statute in s. 191(1), in this case the CCAA. If Parliament had wanted to limit amendments to those that would facilitate a reorganization, it could have said so. Thus, the combination of ss. 191(1)(c), 191(2) and 173(1)(b) gave the motions judge the jurisdiction to order the transfer of Ivaco and Ifastgroupe's head offices from Quebec to Toronto. Resort to the CCAA was unnecessary.

83 The Superintendent and the QPC rely on this court's decision in *Stelco Inc., Re* in support of their argument. However, that case differs from the present case in a material way. In *Stelco Inc., Re* the issue was whether a motions judge in CCAA proceedings could order the removal of two members of the company's board of directors under s. 109(1) of the CBCA. The power to remove directors is vested in the shareholders. Blair J.A. held that the motions judge could not rely on the court's discretion under s. 11 of the CCAA to override or supplant the specific power in s. 109(1) of the CBCA. The discretion under s. 11 must be used to control the court's processes, not the company's processes.

84 By contrast, in the present case, s. 191 of the CBCA gives the court express authority to order the transfer of the head office of a company that is subject to an order under the CCAA. Thus, to make a transfer order, the court need not rely on its discretion under s. 11 of the CCAA.

85 However, the jurisdiction in s. 191(2) is discretionary, as evidenced by the use of the word "may". Therefore, the remaining question on this ground of appeal is whether the motions judge properly exercised his discretion in ordering the transfer. I think that he did.

86 Ivaco and Ifastgroupe had not actively carried on business since the sale of their assets to Heico was completed in December 2004. The Monitor holds the proceeds of the sales in bank accounts in Toronto. Because of the lengthy and complex CCAA proceedings, the Ontario Superior Court -- Commercial List is familiar with the affairs of Ivaco and Ifastgroupe. Having all the issues common to all the Companies administered at the same time before the court familiar with these issues will facilitate the most efficient, consistent and just administration and distribution of their estates.

87 The QPC, in particular, objects to these head office transfers. It argues that the motions judge's order will enable the creditors to defeat a future motion to transfer to the Quebec Superior Court the question whether the Companies participating in the Ivaco Salaried Plan are "solidarily liable", that is jointly and severely liable, under Quebec law for satisfying the obligation to fund the plan.

88 The underpinning of the QPC's argument is as follows: the "solidarily liable" provision is unique to Quebec law and therefore should be decided by a Quebec court. Whether the Quebec or the Ontario Superior Court presides over

this future motion will turn on the application of the *forum conveniens* principle. One relevant factor in assessing the *forum conveniens* is the residence or place of business of the parties. According to the QPC, transferring Ivaco's and Ifastgroupe's head offices to Toronto will tip the scales in favour of the Ontario Superior Court hearing the "solidarily liable" motion.

89 It seems to me that this is a weak argument. The QPC has not yet brought this motion. When it does, the Ontario Superior Court can assess the relevant considerations affecting the appropriate forum. Now, however, the motions judge's transfer order just makes good sense. He, therefore, exercised his discretion properly. I would not give effect to this ground of appeal.

D. Conclusion

90 The motions judge did not err in law in refusing to order the immediate payment of the amount of the deemed trusts under the *Pension Benefits Act* or in refusing to segregate that amount. Nor did he err in exercising his discretion to lift the stay under the CCAA and permit the bankruptcy petitions to proceed. Finally, the motions judge did not err in ordering that the head offices of Ivaco and Ifastgroupe be transferred from Quebec to Toronto. Accordingly, I would dismiss the Superintendent's appeal.

91 If the parties cannot agree on the costs of the appeal, they may make written submissions to the court. These submissions should be delivered within 30 days of the release of these reasons.

***M. Rosenberg J.A.*:**

I agree.

***J. Simmons J.A.*:**

I agree.

Appeal dismissed.

FN1. Taking into account a $12 million distribution to the National Bank permitted by the motions judge in December 2004.

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Ontario Supreme Court
Ben-Israel v. Vitacare Medical Products Inc.
Date: 1997-11-06

Ben-Israel

and

Vitacare Medical Products Inc. et al.

Court File No. 90-CU-003097

Ontario Court (General Division) Beaulieu J.

Heard: October 21, 22, 23, 24, 25 and 28, 1996

Judgment rendered: November 6, 1997

Bernard B. Gasee, for plaintiff.

Janet E. Gross, for defendants.

BEAULIEU J.:—

Introduction and Contextual Background

[1] This an action to recover damages for breach of contract, breach of confidence and breach of fiduciary duty, in the context of an arm's length, commercial customer/manufacturer relationship. A claim for passing off was withdrawn. An injunction against the defendants was also requested in the statement of claim, but was not pursued at trial. The plaintiff alleges that there existed between himself and the defendant manufacturers a verbal non-competition agreement, and that the defendants breached this agreement by manufacturing and marketing a product virtually identical to his, using remarkably similar packaging, and targeting the same retailers. He also alleges that the defendants had a duty not to compete against him using confidential information supplied by him, regarding his product and his business and that, because of the nature of their relationship and the power the defendants had to use this information against him, they owed him a fiduciary duty as well.

[2] The defendants filed a counterclaim requesting injunctions against the plaintiff interfering with their business relations with customers, and claiming damages for slander. The counterclaim was dismissed on consent near the end of the trial.

[3] The plaintiff has a degree in chiropractory and is licensed to practice in Ontario. While he was a student, and after, he did extensive research into pillows and cushions. He also

became active in Medline computer system with respect to information on pillows and cushions in Europe, South East Asia and other countries. His main interest was in designing and rebuilding things. He eventually went into business as a sole proprietorship, Aquarius Products.

[4] The defendants Vitacare Medical Products Inc. and Vitafoam Corporation are effectively under the same ownership, with Vitacare Medical and another branch, Engineer Foam Inc., fabricating foam for industrial enterprises.

[5] The parties came into initial contact sometime in the mid 1980s. One of the main difficulties in this case is that neither party, for apparently different reasons, were great believers in formal arrangements. The determination of the issues will therefore be based on the credibility of the witnesses primarily when seen in context of their testimony, the related documentary evidence where it exists, and the evidence as a whole.

[6] For the most part the plaintiff dealt with therapeutic products. Around 1987 he became more involved with mass-merchandising concepts, starting with K-Mart. His approach was to design the component and order from suppliers. He designed the pillow which is the major product in question in this case. He then designed a way of inserting it into a cloth cover which in turn was covered by a plastic bag with printed cardboard insert. He approached K-Mart with a view to testing the possibility of sales to major retailers. Their representative (Mr. Keba) expressed interest but indicated that the packaging needed more attention.

[7] To the best of the plaintiff's knowledge there was no therapeutic pillow marketed by mass merchandising up to that time. He went to Concepts Inc. who produced an original drawing, a picture, script etc. He used the insert with the first order from K-Mart and, except for the addition of a bar code and address later on, there have been no changes in either the English or French versions which have been used since that time.

[8] The plaintiff first dealt with the defendants regarding foam for tables. Around 1981 or 1982 he requested that they cut foam for his pillows. A couple of years later he went to Woodbridge Foam Corporation because Vita could not mould his low back cushion. In other words the defendants Vita cut the foam but Woodbridge Foam moulded it. This arrangement went on for approximately one year.

[9] In 1985 Woodbridge Foam took a sample of the plaintiff's mould of the low-back cushion to their customer and proceeded to get it produced themselves. After seeking legal advice, which he accepted, the plaintiff dropped the possibility of legal action because of the anticipated expenses.

[10] After the experience with Woodbridge he determined that anyone with whom he dealt from then on would have to give him full assurances that they would not use his ideas and compete with him as Woodbridge had.

[11] He then went to Vita and gave them a sample of the foam pillow which had previously been moulded by Woodbridge Foam. The plaintiff says that in his very first personal contact with Vita he gave specific instructions that they were not to compete with him on the same item. He received assurances to the effect that "We are in the business of manufacturing foam for our customers. We are not in the business of competing with them." He says that he specifically requested that the defendants' representatives were not to approach his customers. The defendants indicated that their market was limited to home care and health stores.

[12] The plaintiff's main contact initially and throughout approximately five years was Mr. Rowlands. The latter reaffirmed the promise that "We will not compete with you." Through Rowlands, at the plaintiff's request, arrangements were made to meet the senior owners and partners, Irving and Mel Himell. The plaintiff described the meeting as being cordial and he left with a feeling or reassurance that they would not step on his toes. Rowlands knew the plaintiff was selling to various stores including Hy & Zel, K-Mart, Woolco and Consumers Distributing. Sales were very brisk. Rowlands was also aware of the volume of the plaintiff's sales through his personal and regular contact with the plaintiff and the delivery orders. The relationship between the two men was described as cordial, close and warm. The plaintiff says that he told Rowlands about K-Mart and the insert with pride and enthusiasm. There were no secrets, no problems with deliveries, and Rowlands was privy to the plaintiff's pricing and general approach.

[13] Things went according to plans and agreement until early 1990 when the plaintiff became aware that the defendants had not only approached his customers but had produced a pillow, insert and packaging that were virtually identical to his. Indeed when he first saw it, by accident at the Canadian Chiropractic School graduation night, he thought it was his own.

On closer view, he was shocked to discover that it was not. However, the layout, colours, picture, language, etc. were virtually the same.

[14] In addition to this discovery the plaintiff also was informed by Mr. Keba at K-Mart that a sales representative of the defendants had approached them. The plaintiff felt betrayed by Rowlands, a friend and confidant for over five years. He was angry and requested an immediate meeting with the principals of Vita.

[15] On February 27, 1990, the plaintiff attended a meeting at the defendants' head office. He was alone but the defendants' contingent included the two Himells, Rowlands, and their lawyer, Caplan. Despite the potential problems raised by the incidents at the College and K-Mart, the plaintiff perceived the meeting to be positive. Mel Himell appeared to be genuinely upset and indignant that his representative had called upon K-Mart. Rowlands defended the move because if they had not their own competitor would have. The plaintiff perceived Mel Himell to be admonishing Rowlands. The plaintiff reaffirmed and underlined the fact that Vita had no business being at K-mart pursuant to their agreement. The two pillows were then displayed (Exhibit 1, the plaintiff's; Exhibit 28 the defendants'). Mel Himell seemed shocked at the demonstration. He gave the impression that he was truly unaware of the situation.

[16] Discussion ensued regarding K-Mark, Woolco, Consumers, and the fact that the defendants were not to be there according to the initial and long-standing agreement.

[17] Unfortunately, no one, including the lawyer, took any notes, although the plaintiff prepared his record and impressions after returning to his office. The result of the meeting was that the defendants agreed to cease and desist their contacts with the plaintiff's identified customers and that this would be confirmed in writing.

[18] The plaintiff left the meeting feeling good because of the defendants' promise to clear up the situation. However, his positive feelings lasted only until the lawyer finally produced a document that not only did not reflect the essential points of the meeting but included new conditions precedent to their undertaking not to pursue their contacts with the plaintiff's customers. These conditions, the plaintiff says, were simply never raised at the meeting.

[19] The plaintiff says that other issues that *were* raised were initiated by Irving Himell. The latter discussed the possibility of the plaintiff endorsing some of the defendants' products with a royalties aspect. The defendants also expressed interest in the plaintiff's designs and new

products. These matters were for future discussions and unrelated to the issue of honouring their previous commitment and rectifying the present problem. It was clear that they had agreed not to compete with him, to stay away from his customers and not to use the offensive insert. It is the plaintiff's recollection that not only did no one take notes for the defendants but that the lawyer merely stood through the meeting and at times absented himself.

[20] Further attempts were made to clear up the difficulties, including a meeting between Mel Himell and the plaintiff on May 29, 1990. By that time the written material from the defendants bore little resemblance, if any, to the earlier agreement at the meeting. The plaintiff says that the lawyer clearly attempted to distort and minimize the effect of the original verbal agreement. Mel Himell, in the course of the May meeting, allegedly told the plaintiff, "You have to give me permission to sell to Woolco." The February and March meetings and the agreements discussed at that time were essentially not denied in May, nor was the fact that the original understanding had been breached, but the defendant said, "Yes, but you have to give me permission to sell to them because the buyer, Mr. James, has said that he is not going to buy our other products unless we sell him the pillows as well." The plaintiff says that he would require some form of compensation before he could consider such permission. The resulting impasse was never resolved and this litigation ensued.

[21] Needless to say the defendants deny the existence of any non-competition agreement at any time. Their position is that such an agreement is unheard of in such a highly competitive dog-eat-dog industry. They also say that there was nothing really unique or special about the plaintiff's pillow. They go so far as to say that the coincidental similarity of the insert is basically as a result of their use of "company colours"! As will be seen when dealing with the main issues of this case, I found the plaintiff and his witnesses to be more credible than those of the defendants. The latter impressed me as generally demonstrating a condescending, evasive and manipulative mind-set. That mind-set seems to have prevailed particularly when the plaintiff was not only becoming increasingly successful but had the temerity to assert his rights under their prior agreement. This was so even though they knew from the very beginning of the plaintiff's negative experience with Woodbridge and the resulting elevated importance of honesty and good faith.

Issues

[22] There are four major issues to be resolved in this case:

1. Was there a non-competition agreement or contract between the parties? If so, what was the extent of it and was it breached?

2. Was there a duty of confidence owed by the defendant to the plaintiff? If so, to what information did it relate and was it breached?

3. Was there a fiduciary duty owed by the defendant to the plaintiff? If so, how did it arise and was it breached?

4. What is an appropriate remedy in the circumstances, and what is the quantum of damages, if any?

1. Non-Competition Agreement

[23] There was no written non-competition agreement, but as there was no written contract between the parties at all this cannot be determinative. There can be no doubt that there was a contract, for the defendants to produce foam pillows for the plaintiff, and the question is whether non-competition was a term of that contract. The plaintiff asserts that there was a non-competition agreement, made orally at the outset of their dealings, and reconfirmed periodically.

[24] I believe the testimony of the plaintiff in this regard. He appears credible, logical and cautious. Despite his characteristic tendency to verbosity and repetition, his description of the course of events rings truer than that of the defendants. Given his previous negative experience with Woodbridge, it is natural and reasonable that he would have made non-competition a term of an agreement with any new supplier of foam for his products. Although there is a marked lack of correspondence, notes or other documentation in this case, I find that the circumstances as a whole, and certain pieces of evidence, strongly support the plaintiff's position, to a large extent because the plaintiff at least followed up the major meetings, with responses that pointed out perceived inaccurate representations of what transpired at those meetings. In addition, at the later key meetings, the plaintiff was always outnumbered anywhere from two to three to one including the defendants' lawyer. I accept the plaintiff's evidence that the latter took no notes, that no one took notes and that all persons were not constantly in the room. This *modus operandi* on the part of the defendants impressed me as a pattern that started with the two major defendant brothers and accelerated to having others, including their lawyer, when the plaintiff later became more demanding of clarification. Thus, the initial meeting with the defendants, in my view, reflects what the

plaintiff was to unfortunately discover as time went on. The defendants were not afraid to take advantage of this entrepreneur.

[25] I accept the plaintiff's evidence that the defendants said that they were selling to a supplier, not to chiropractors, when the plaintiff first found a Vitacare pillow for sale at a chiropractors' conference and confronted them about it. There is also the apology by the defendant, through Rowlands, to the plaintiff for approaching Hy & Zel's, which was done through their recently-acquired subsidiary Baymar, and an admission that such an approach would be wrong had it been done directly. Finally, there is the letter from Vitacare to the plaintiff after the February 27th, 1990 meeting, in which they expressly agreed not to approach the plaintiff's three largest clients, subject to conditions which the plaintiff asserts were not discussed at the meeting. All of this supports the plaintiff's contention that the defendants had agreed not to sell to chiropractors, not to sell to mass merchandisers generally, and not to sell to his specific clients.

[26] I therefore believe the plaintiff and find that there was indeed a non-competition agreement between Aquarius and Vitacare, regarding the double contoured pillow. It remains to be determined, however, when this agreement arose, and whether this agreement was intended to cover all sales of posture pillows by the defendant, any sales other than those to the defendants' current customers, if any, or only sales to customers identified by the plaintiff as his, namely chiropractors and mass distributors.

[27] There is little room for doubt that the matter was discussed early on in the parties' business relationship, given the plaintiff's negative experience with his previous supplier, and his desire to prevent a similar occurrence. I believe that the plaintiff was given assurances by everyone with whom he dealt at Vitacare, including his initial contact and Rowlands, and the two brothers Himell. I further believe and find that he was entitled to rely on these assurances, as they formed a fundamental condition for him to deal with a supplier, and he made that quite clear, using the account of what happened with his previous supplier to underscore the importance of this condition. Any reasonable person, upon hearing his demand for non-competition, would realize that he considered this to be a fundamental term of their business arrangement. I find and believe that the rather colourful language used by the Himells, reassuring that they would not "screw" him, can only reaffirm the trust that he placed in them and their acceptance of his offer to deal on his terms.

[28] I believe that this non-competition agreement commenced when Aquarius first began dealing with Vitacare for the manufacture of the double contoured foam pillow in 1985. The latest that this agreement could have come into effect was at the meeting in late 1985 or early 1986, when the defendant's principals, Irving and Mel Himell, confirmed the agreement with the plaintiff. At that meeting the Himells reassured him to the effect that they manufactured foam for their customers, and did not compete with them. Vitacare had at that time a bigger pillow, and said that their market was limited to home care and health stores.

[29] There was therefore an agreement not to compete with the plaintiff's pillow, nor to approach the plaintiff's customers. I am satisfied that this agreement was breached. Both the agreement and the breach have been proven on the balance of probabilities. The defendants modified their pillow to be indistinguishable from the plaintiff's after they began manufacturing for him, using an insert that was the same colour scheme and used virtually the same illustrations and information, and directly approached the exact customers that he had periodically requested that they not approach, namely the chiropractic field and the mass-retailers Hy & Zel's, K-mart, Woolco and Consumers Distributing. The stark similarity of Exhibits 1 and 28, the plaintiff's and the defendants' subsequent pillow, is so striking that even the plaintiff perceived the defendants' pillow as his own when he first saw it on public display. The defendants' attempts at explanations, such as company colours, etc., rang extremely hollow. I found the defendant witnesses generally and, particularly Rowlands and Mel Himell, to be evasive, contradictory, condescending to the plaintiff and basically not credible. Their demeanour and evidence confirmed the plaintiff's description of persons who had effectively taken advantage of a sole business proprietor and were prepared to use their superior corporate clout to keep him under control. This attitude is relevant to the other issues. The reality of this case is that the plaintiff has established the agreement in issue which I have determined after careful and reasoned consideration of the evidence as a whole.

[30] In the absence of a precise date, I conclude that since the agreement arose as early as mid-1985, and no later than mid-1986, fixing the date at January 1, 1986 is appropriate for the purpose of calculating any damages.

2. Duty of Confidence

[31] Canadian intellectual property legislation has developed to protect the proprietary interests of those who create or develop information. The *Patent Act,* R.S.C. 1985, c. P-4, and

the *Copyright Act,* R.S.C. 1985, c. C-42, are two examples of statutes designed to protect the creative process and to regulate who will benefit from the use and disclosure of original and confidential information. Since the plaintiff did not seek to register any of his products neither of these statutes apply, and he is therefore relying on the equitable concept of duty of confidence.

[32] In *Pharand Ski Corp. v. Alberta* (1991), 37 C.P.R. (3d) 288 at p. 333 (Alta. Q.B.), Mason J. conducts a comprehensive survey and analysis of the origin, content and application of the duty of confidence. I need not repeat it here, but I am left with no doubt that Vitacare owed the plaintiff a duty of confidence, and that the defendant breached that duty.

[33] La Forest J., writing for the majority of the Supreme Court of Canada, in *Lac Minerals Ltd. v. International Corona Resources Ltd.,* [1989] 2 S.C.R. 574, 26 C.P.R. (3d) 97, said the following [at p. 635] on this issue:

> The test for whether there has been a breach of confidence... consists in establishing three elements: that the information conveyed was confidential, that it was communicated in confidence, and that it was misused by the party to whom it was communicated.

[34] The information in question in the present case is the design of the pillow and the insert, as well as the customer list, quantities and pricing of the plaintiff's pillow. The plaintiff stated that all of these pieces of information were confidential, and that they were communicated in confidence. I believe the plaintiff when he says that, although there were similar pillows available prior to his, he did considerable research, including clinical research, in order to design a pillow superior to those then on the market. He made changes in size, shape, contouring, foam density and covering. He also hired a design firm to redesign the external packaging, in order to make the product more saleable. I also believe him when he says that the Himells, in his first meeting with them, assured him that they would not disclose his information to his competitors or anybody else and that they had a different market.

[35] The defendants argue that the plaintiff never conveyed any confidential information to them, as all of the information was previously in the public domain. However, the case of *Saltman Engineering Co. v. Campbell Engineering Co.,* [1963] 3 All E.R. 413*n*, 65 R.P.C. 203 (C.A.), which is often quoted as the modern source of the statement of the duty of confidence,

makes a notable qualification to the restriction of the duty to information which is not public knowledge. In that case, the defendant company, who was contracted by the plaintiffs to manufacture certain leather punches from drawings of tools provided solely for that purpose, used those drawings to construct tools so that they could manufacture identical punches and sell them as their own. Lord Greene M.R. stated that:

> The information, to be confidential, must, I apprehend, apart from contract, have the necessary quality of confidence about it, namely, it must not be something which is public property and public knowledge. On the other hand, it is perfectly possible to have a confidential document, be it a formula, a plan, a sketch, or something of that kind, which is the result of work done by the maker on materials which may be available for the use of anybody; but what makes it confidential is the fact that the maker of the document has used his brain and thus produced a result which can only be produced by somebody who goes through the same process.
>
> What the defendants did in this case was to dispense in certain material respects with the necessity of going through the process which had been gone through in compiling these drawings, and thereby to save themselves a great deal of labour and calculation and careful draughtsmanship... That, in my opinion, was a breach of confidence.

[36] The circumstances in the present case are very similar—the plaintiff used information that was public knowledge, and made something new of it. He invested his time, effort, ingenuity and money to produce a marketable product, and while it was open to the defendants to do this work, it was the plaintiff who actually did so, and the defendants, noting the plaintiff's success, decided to take advantage of their newly-gained knowledge.

[37] Also relevant is Megarry J.'s oft-quoted comment in *Coco v. A.N. Clark (Engineers) Ltd.,* [1969] R.P.C. 41:

> In particular, where information of commercial or industrial value is given on a business-like basis and with some avowed common object in mind, such as a joint venture *or the manufacture of articles by one party for the other,* I would regard the recipient as carrying a heavy burden if he seeks to repel a contention that he was bound by an obligation of confidence [Emphasis added.] [Page 48.]

[38] Far from proving that no obligation of confidence existed, the Himells had actually agreed to keep the plaintiff's information confidential. Obviously they meant that they would not disclose anything about the plaintiff's business to others, but this agreement shows that whether they regarded the information as confidential or not, they knew that the plaintiff regarded and had imparted it as such.

[39] Finally, in the same line of cases, a "springboard test" was articulated by Roxburgh J. in *Terrapin Ltd. v. Builders' Supply Co. (Hayes) Ltd.,* [1969] R.P.C. 128 (C.A.), as follows:

> ...a person who has obtained information in confidence is not allowed to use it as a springboard for activities detrimental to the person who made the confidential communication, and springboard it remains even when all the features have been published or can be ascertained by actual inspection by any member of the public... The possessor of the confidential information still has a long start over any member of the public... It is, in my view, inherent in the principle upon which the *Saltman* case rests that the possessor of such information must be placed under a special disability in the field of competition to ensure that he does not get an unfair start.

[40] The receipt of confidential information in circumstances of confidence establishes a duty not to use that information for any purpose other than that for which it was conveyed, and not to use it to the detriment of the confider. The relevant question to be asked is what the receiver of the information is entitled to do with it, not what they are prohibited from doing with it, and the onus falls on the confidee to show that the use of the confidential information was not prohibited. This onus was not met in this case, especially in light of the fact that the defendants had been expressly forbidden from competing with the plaintiff in this market. The only use to which the defendants were entitled to put the plaintiff's information was the manufacture of the pillow for the plaintiff. In this role, the defendants were under a "special disability" with regard to the use of that information, in order to prevent them from doing exactly what they did—get an unfair start in the market, and use the information to the detriment of the plaintiff who supplied the information.

[41] The defendants in this case did receive confidential information, imparted in circumstances of confidence, and used it as a springboard to produce and sell their own product. They used the plaintiff's pillow and the information and layout of his insert, both of which had taken time, effort, research and money to develop. They also knew who his

customers were, and that he had opened up the mass-merchandiser market for therapeutic pillows. They had a good idea of the quantity the plaintiff was selling, to whom, and at what price, because of orders placed with them, some for direct delivery to the retailer, and through discussions between the plaintiff and Rowlands. This information was used to the detriment of the plaintiff, as Vitacare's pillow was sold to the plaintiff's customers, and efforts were made to sell to more of the plaintiff's customers, at prices known to Vitacare to be lower than the plaintiff's, thus reducing his share of the market, reducing his profits and jeopardizing his business. It bears repetition that the defendants' pillow, without reasonable explanation, was virtually identical in colour scheme, printed material, design and packaging.

3. Fiduciary Duty

[42] A fiduciary duty imposes the highest duty in law on the party holding the duty—the fiduciary—to act altruistically for the sole benefit of the beneficiary, to the fiduciary's own detriment if necessary. The traditional categories of relationship in which a fiduciary duty exists are agent to principal, lawyer to client, trustee to beneficiary, business partner to partner, and director to corporation. In all of these situations, a fiduciary duty exists because the fiduciary has assumed a position, and taken on a responsibility, in which the beneficiary's interest is dependent upon the fiduciary's actions. There are, however, other situations in which the duty arises, based on the particular situation and relationship of the parties. In *Frame v. Smith,* [1987] 2 S.C.R. 99, quoted with approval in *Lac Minerals, supra,* Wilson J. stated [at p. 136] that:

> Relationships in which a fiduciary obligation have been imposed seem to possess three general characteristics:
>
> (1) The fiduciary has scope for the exercise of some discretion or power.
>
> (2) The fiduciary can unilaterally exercise that power or discretion so as to affect the beneficiary's legal or practical interests.
>
> (3) The beneficiary is peculiarly vulnerable to or at the mercy of the fiduciary holding the discretion or power.

[43] Courts have been extremely reluctant to impose or recognize a fiduciary duty in the context of an arm's length commercial relationship, given that the essence of such relationships is the profit motive and competition. The Supreme Court of Canada has yet to

be unanimous in finding a fiduciary duty in such circumstances, even when the defendant is in such a professional position that the plaintiff has relied heavily on their advice, such as in the case of financial advisors. There must exist very compelling reasons to impose this high duty, such as the absolute reliance of the one party on the other, and the inability, for whatever reason, of choosing not to rely on their actions or advice. There is special reluctance to impose this duty when, as in this case, a contract or duty of confidence has been breached, and the remedy available is at least equivalent.

[44] In *Hodgkinson v. Simms,* [1994] 3 S.C.R. 377, 57 C.P.R. (3d) 1, in which the majority of the Supreme Court of Canada found a fiduciary duty to exist in the particular circumstances of reliance on an accountant's investment advice, La Forest J. first quoted with approval Dickson J. (as he then was) in *Guerin v. The Queen* (1984), 13 D.L.R. (4th) 321 (S.C.C.) at 341:

> ...where by statute, agreement, or perhaps by unilateral undertaking, one party has an obligation to act for the benefit of another, and that obligation carries with it a discretionary power, the party thus empowered becomes a fiduciary.
>
> La Forest J. then goes on to explain that:
>
> ...outside the established categories, what is required is evidence of a mutual understanding that one party has relinquished its own self-interest and agreed to act solely on behalf of the other party. [Pages 409-410.]

[45] He also says later:

> Commercial interactions between parties at arm's length normally derive their social utility from the pursuit of self-interest, and the courts are rightly circumspect when asked to enforce a duty... that vindicates the very antithesis of self-interest... [Page 414.]

[46] Looking at the relationship between Aquarius and Vitacare, I can see no reason to impose a fiduciary duty. It was, in effect, an arm's length commercial relationship. There was no agreement or undertaking that Vitacare would act *on behalf of* the plaintiff, and the defendant certainly never agreed to relinquish its own self-interest. The agreement I found to exist was simply that the defendant would not act *against* the plaintiff's interests. As in most commercial cases, the breaches that occurred here were those of contract and confidence.

Both of these areas of law provide adequate remedies without trying to stretch the concept of fiduciary duty to include standard commercial transactions.

4. Remedy

[47] The plaintiff has elected to claim for damages alone, as opposed to an injunction against the defendants, or an accounting of their profits. He stated that he is not seeking an injunction because it would unreasonably interfere with the clients, and he feels that adequate compensation for his losses can be achieved with an award of damages. The testimony of the defendants was that they did not make a profit on their sales of posture pillows. This strongly suggests that they were using the pillow as a "loss leader". In light of this, an accounting of profits would not be a suitable remedy, as it would not restore the plaintiff to the position in which he would have been had the breaches not occurred. I agree that damages is the most appropriate remedy in this case.

[48] There is some debate over a court's jurisdiction to award certain remedies, depending on the equitable or legal origin of the claim. Under the common law, damages may be awarded for breach of contract, but only equitable remedies, such as injunctions, specific performance or a constructive trust, may be awarded for breach of an equitable duty. Since this case involves both a legal breach, of contract, and an equitable breach, of confidence, it does not seem necessary to differentiate whether the remedy is to come from law or equity or both, and the fusion of law and equity is making these distinctions less relevant in any event. However, section 99 of the *Courts of Justice Act,* R.S.O. 1990, c. C.43, expands the range of possible remedies, such that regardless of the jurisdictional origin of the action, in law or in equity, damages are available:

> 99. A court that has jurisdiction to grant an injunction or order specific performance may award damages in addition to, or in substitution for, the injunction or specific performance.

[49] Thus, regardless of whether the breach is one of contract, duty of confidence or fiduciary duty, the appropriate and available remedy in this case is damages. The plaintiff should be restored to the position he would have been in had the breach not occurred.

[50] Plaintiffs have a duty to mitigate their damages. I am satisfied that this plaintiff made every effort to do so in this case. He repeatedly contacted the defendants to voice his

concerns about their actions, lowered his price to K-Mart in order not to lose them as customers entirely, and made efforts to renegotiate with Consumers Distributing, Woolco and Hy & Zel's, unfortunately to no avail. He cannot be held at fault for continuing to deal with the defendants for as long as he did. The defendants have alleged that this was acquiescence on his part. The plaintiff testified that he thought that they had a good relationship, that he could still trust them, and that they could work things out. He further explains his final purchase from Vitacare, in 1990, as necessary to fill an existing order from a customer. All of this, in my view, has a ring of reasonable commercial sense in the circumstances in which the plaintiff found himself.

Contract

[51] As pointed out by the defendants, damages for breach of contract are limited to those that are referable to the ordinary consequences of the breach and would flow in the usual course from the breach. Damages must be reasonably within the contemplation of both parties at the time the contract was made. Since the plaintiff's damages are from loss of profits attributable to the defendants entering the market with a virtually identical product and targeting that product at the very customers who were already purchasing the plaintiff's product, and since the contract that was breached was one of non-competition, it was reasonably foreseeable, and indeed unavoidable, that the exact consequences that did follow from the breach would so follow. These consequences are loss of profit to the plaintiff for an indefinite period of time, from loss of certain large customers—Hy & Zel's, Consumers Distributing, Woolco—from extra competition in the market to chiropractors, and from having to lower his price to K-Mart specifically and to possible future customers generally.

[52] A decline in sales does not necessarily mean that it has been caused by the actions of the defendant. The defendants argue that they were not the only ones in competition with the plaintiff in this market, and they testify that the demand for this type of pillow levelled off or declined in the 1990s. While I believe both of these statements to be true, it is also a fact that the actions of the defendants in specifically approaching the very retailers and distributors that they knew to be customers of the plaintiff had a direct negative effect on his sales and pricing and therefore on his profits over the short and long terms. The lost sales and profits can be directly causally linked to the actions of the defendants.

[53] Damages are to be compensatory, in that they are intended to provide compensation to the plaintiff for losses suffered due to the actions of the defendant. Once a breach has been found, there is no requirement that the damages be calculated with absolute precision, as this would be impossible to do in a loss of profits case, where so many variables can affect future sales. Professor Waddams quotes Lord Watson in *United Horse-Shoe & Nail Co. v. Stewart* (1888), 13 App. Cas. 401 (H.L.), still the authority on this point: "That must always be more or less matter of estimate, because it is impossible to ascertain, with arithmetical precision, what in the ordinary course of business would have been the amount of the [plaintiffs'] sales and profits" (in Waddams, S.M., *The Law of Damages,* looseleaf edition (Aurora, Ont.: Canada Law Book Inc., December, 1996), p. 5-41).

[54] The plaintiff has claimed for both compensatory damages and punitive damages. In a breach of contract case, punitive damages will only be awarded in very exceptional circumstances. Pitch, H.D., and Snyder, in *Damages for Breach of Contract,* 2nd ed. (looseleaf edition) (Toronto, Carswell, 1989), pp. 4-29-4-31, sum up the state of the law before 1989:

> Punitive damages are awarded by the court to punish a defendant whose conduct has been particularly high-handed, reprehensible or outrageous. Canadian courts have traditionally been reluctant to award punitive damages in contract actions since the usual objective in an action for breach of contract is to compensate the plaintiff rather than punish the defendant. However, in recent years the courts had indicated a greater willingness to award punitive damages as an additional remedy in breach of contract situations as a means of censuring a defendant whose conduct had been particularly outrageous.

[55] In 1989 the Supreme Court of Canada released their decision in *Vorvis v. Insurance Corp. of British Columbia,* [1989] 1 S.C.R. 1085, a wrongful dismissal case, which, in the words of Pitch and Snyder, "virtually emasculated" the right to claim and recover punitive damages in breach of contract cases. The majority of the court said, at 1107:

> In an action based on breach of contract, the only link between the parties for the purpose of defining their rights and obligations is the contract. Where the defendant had breached the contract, the remedies open to the plaintiff must arise from that contractual relationship, that "private law", which the parties agreed to accept. The injured plaintiff

then is not entitled to be made whole; he is entitled to have that which the contract provided for him or compensation for its loss.

[56] They go on to say, however, that punitive damages may still be available where the conduct complained of 1) constitutes an independent actionable wrong (which has been pleaded), 2) was the cause of damage, and 3) was "malicious", "harsh", "vindictive" or "reprehensible". Punitive or exemplary damages are therefore still available in exceptional cases. Applying this test in *Foxcroft v. Pilot Insurance Co.* (1992), 8 O.R. (3d) 600, the Ontario Divisional Court held that breach of an equitable duty, in that case a fiduciary duty, could constitute such an independent actionable wrong. In *Independent Order of Foresters v. Prime Air Freight Inc.* (1991), 4 B.L.R. (2d) 60 (Ont. Ct. (Gen. Div.)), the defendant freight company agreed to deliver the plaintiff's goods, but destroyed them with the intent to defraud the plaintiff instead. Haley J. assessed damages against the three defendants for conspiracy to defraud. Conspiracy was an actionable wrong independent from the breach of contract, and the damages claimed arose from the wrong. Punitive damages of $5,000 were awarded against the defendant company, and solicitor-client costs were granted.

Breach of Confidence

[57] In *Pharand Ski Corp. v. Alberta, supra,* Mason J. states [at p. 309] that:

> There has been, at law, a long-recognized obligation of confidence, the breach of which gives rise to a number of remedies including damages, compensatory or nominal, an accounting for profits earned from the breach, the issuance of an injunction to protect privacy, even an *in rem* remedy, the constructive trust. The nature of the remedy is dependent upon the jurisdictional basis applicable to the nature of the confidence and the breach. The obligation of confidence can arise both in private as well as public law: see *United Kingdom (Attorney-General) v. Observer Ltd.* (1988), 99 N.R. 241, particularly at pp. 244-5, and *LAC Minerals Ltd. v. International Corona Resources Ltd...*

[58] As in a breach of contract case, the objective of awarding damages is to monetarily restore the plaintiff to the position in which they would have been had the breach not occurred. Although it may not be strictly necessary to prove detrimental use of the confidential information in a breach of confidence case, the detriment to the confider will affect the nature and quantum of remedy available. I am satisfied that, in this case, the confidential information was used to the detriment of the plaintiff, and that he should therefore be fairly compensated

for it. In *ICAM Technologies Corp. v. EBCO Industries Ltd.* (1991), 6 B.L.R. (2d) 98, 36 C.P.R. (3d) 504 (B.C.S.C.), which followed *Pharand,* Maczko J. addresses the assessment of damages for breach of confidence (at para. 70):

> Depending on the position of a particular plaintiff, the damages may be calculated in a number of ways. For example, the appropriate measure may be any one of or a combination of the following considerations:
>
> (a) the confider's loss of profit;
>
> (b) the value of a consultant's fee;
>
> (c) the depreciation and value of information in consequence of a breach of confidence;
>
> (d) the development costs incurred in acquiring the information;
>
> (e) capitalization of an appropriate royalty;
>
> (f) the market value on information as between a willing buyer and a willing seller.

[59] The most applicable of these to the current case are (a), (b) and (d). The loss of profit issue involves the same considerations as for breach of contract. A consultant's fee is applicable for the time and energy the plaintiff put into the design of the pillow and the development of the mass-merchandiser market. The costs incurred by the plaintiff in hiring a design company to produce the insert should be reimbursed by the defendant, since they have admitted that they did no work of their own, but only "looked at existing material", and the result was an insert remarkably similar, indeed vitually identical, to that of the plaintiff.

Breach of Fiduciary Duty

[60] Having decided that there was no fiduciary duty owed in this case, and therefore no breach, it is unnecessary to address the question of remedy. I will note, however, that the Supreme Court of Canada recently stated in the case of *Hodgkinson v. Simms, supra,* that:

> It is well established that the proper approach to damages for breach of a fiduciary duty is restitutionary. On this approach, the appellant is entitled to be put in as good a position as he would have been in had the breach not occurred.

[61] As such, had a fiduciary duty been found to have been breached, the principles applied to the calculation of damages would have been essentially the same as that for the breaches of contract and duty of confidence as set out above.

Assessment of Damages

[62] The plaintiff has submitted that he lost sales of 7,500 pillows annually to his previous customers, starting in 1990, due to the actions of the defendants. This figure was not challenged. At an average profit rate of $7.50 per pillow, that amounts to an annual loss of $56,250. This is much more reasonable than the $63,750 per year put forward by the plaintiff, as he probably would have had to lower his price somewhat due to increasing competition from other companies in any event. While the damages to the plaintiff will probably go on indefinitely, they cannot be quantified beyond the first few years after the breach, and I believe that the allowable time period for him to recover the annual loss of $56,250 is limited to the years of 1990, 1991 and 1992, for a total of $168,750.

[63] The plaintiff also states that due to the defendants' efforts to undercut him by their approach to K-Mart, he was forced to lower his price to that customer, on the 2,500 pillows per year that he sells to them, by approximately $3.00 per pillow, all of which was taken out of his profits. This results in a loss of $7,500 annually. Again, he would probably have been forced to lower his prices by external market forces not attributable to the defendants; he should recover this amount for the years of 1990 and 1991 only, for a total of $15,000. Although exact figures were not available for all customers for all relevant time periods, enough was provided to satisfy me that these numbers are fair in the particular circumstances of this case. Any doubts are to be exercised in favour of the plaintiff.

[64] It is difficult to put a dollar value on the time and effort that the plaintiff put into developing his pillow, the cotton cover, and the mass-merchandiser market, given that these efforts took place over a number of years. However, between $50,000 and $100,000 would not be an unreasonable consulting fee, had the defendants hired someone to do this work for them. The plaintiff should therefore recover the sum of $75,000. He also paid $5,060 to the design company that created the insert for him, and should be reimbursed this amount by the defendants as well.

[65] While I find that the defendants' conduct in this case was irresponsible and basically unfairly manipulative and condescending, I am not prepared to find that it was particularly high-handed, reprehensible or outrageous, such as to invite punitive damages. The independent actionable wrong in this case is the breach of confidence, which was pleaded and proved, and which was a direct cause of the damage suffered. The defendants breached the non-competition agreement with the plaintiff, they lulled him into trusting them by repeatedly reassuring him that they would not compete, and, most unacceptable of all, they used his own confidential information to compete with his product. However, the courts should interfere as little as possible with commercial relations. The defendants' conduct and treatment of the plaintiff, which were still evident in the defendant witnesses' demeanour, cannot be condoned. However, I decline to make a specific award for punitive damages.

Conclusion

[66] I find in favour of the plaintiff. A breach of contract and a breach of the duty of confidence did occur, regarding the defendant's competition with the plaintiff's therapeutic foam pillow, and their use of the plaintiff's confidential information. Damages are awarded in the amount of $263,810, with prejudgment interest on that amount calculated pursuant to s. 128 of the *Courts of Justice Act.*

[67] The plaintiff will have his costs after assessment or as agreed upon by the parties. It is my understanding that the senior master in Toronto can now entertain requests for assessments to be brought on without undue delay and that this matter could be expedited. In the circumstances, I would urge the parties to avail themselves of this opportunity.

Judgment for plaintiff.

C.E.B. & P.G.R. 8179, **51 C.C.P.B. 297**

2005 CarswellOnt 7306

General Chemical Canada Ltd., Re

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF GENERAL CHEMICAL CANADA LTD.

AND IN THE MATTER OF THE APPLICATION OF GENERAL CHEMICAL CANADA LTD.

HARBERT DISTRESSED INVESTMENT FUND, L.P. and HARBERT DISTRESSED INVESTMENT MASTER FUND, LTD. (Applicants) and GENERAL CHEMICAL CANADA LTD. (Respondent)

Ontario Superior Court of Justice

C. Campbell J.

Heard: November 18, 2005
Judgment: December 14, 2005
Docket: 05-CL-5712, 05-CL-6160

Counsel: Steven Weisz, Karen Park for General Chemical Canada Ltd.

Robert Staley, Lisa Knorst, Mark Laugesen for Harbert Distressed Investment Fund, L.P.

Deborah Grieve, Domenico Magisano for Ministry of the Environment

Mark Bailey for Superintendent of Financial Services

Clifton Prophet, Massimo C. Starnino for General Chemical Canada Holding Inc.

Ashley Taylor, Jessica Bookman for PricewaterhouseCoopers Inc. -- Monitor

Lewis Gottheil for CAW-Canada

Ian Wallace for Sherway Consulting (Windsor) Ltd.

John Leslie for Pollard Highway Products

Subject: Insolvency; Corporate and Commercial

Bankruptcy and insolvency --- Bankruptcy petitions for receiving orders -- Stay of petition -- Pending outcome of other proceedings

Restructuring of debtor company under Companies' Creditors Arrangement Act failed because prospective purchaser of assets on going concern basis would not assume environmental liabilities -- Debtor applied for receiving order under Bankruptcy and Insolvency Act -- Superintendent of Financial Services brought motion for stay pending determination of its priority and order for immediate payment of past pension plan contributions -- Minister of Environment brought motion to appoint interim receiver to oversee compliance with its orders prior to sale of assets or assignment in bankruptcy -- Motions dismissed -- It would be unfair to secured creditor to grant either motion -- Moving parties agreed to forgo claims in order to pursue plan of arrangement -- Moving parties knew that pressing claims then would likely prevent sale of assets -- Arrangement was pursued in good faith and considered reasonable by all parties -- Refusing relief sought did not bring bankruptcy process into disrepute.

Cases considered by C. Campbell J.:

> Graphicshoppe Ltd., Re (2005), 2005 CarswellOnt 7008 (Ont. C.A.) -- referred to
>
> Ivaco Inc., Re (2005), 2005 CarswellOnt 3445, 47 C.C.P.B. 62, 12 C.B.R. (5th) 213 (Ont. S.C.J. [Commercial List]) -- followed
>
> King (Township) v. Rolex Equipment Co. (1992), 23 R.P.R. (2d) 313, 8 O.R. (3d) 457, 90 D.L.R. (4th) 442, 9 C.E.L.R. (N.S.) 1, 1992 CarswellOnt 216 (Ont. Gen. Div.) -- referred to
>
> Panamericana de Bienes y Servicios S.A. v. Northern Badger Oil & Gas Ltd. (1991), 8 C.B.R. (3d) 31, 81 Alta. L.R. (2d) 45, [1991] 5 W.W.R. 577, 81 D.L.R. (4th) 280, 7 C.E.L.R. (N.S.) 66, 117 A.R. 44, 2 W.A.C. 44, 1991 CarswellAlta 315 (Alta. C.A.) -- referred to
>
> Royal Oak Mines Inc., Re (1999), 1999 CarswellOnt 1068, 11 C.B.R. (4th) 122 (Ont. Gen. Div. [Commercial List]) -- followed
>
> Strathcona (County) v. PriceWaterhouseCoopers Inc. (2005), 2005 ABQB 559, 2005 CarswellAlta 1018, 13 C.B.R. (5th) 145, 256 D.L.R. (4th) 536, 12 M.P.L.R. (4th) 167, 47 Alta. L.R. (4th) 138 (Alta. Q.B.) -- referred to
>
> Toronto Dominion Bank v. Usarco Ltd. (1991), 42 E.T.R. 235, 1991 CarswellOnt 540 (Ont. Gen. Div.) -- distinguished

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3

s. 47(1) -- referred to

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

Generally -- referred to

Courts of Justice Act, R.S.O. 1990, c. C.43

s. 101 -- referred to

Pension Benefits Act, R.S.O. 1990, c. P.8

Generally -- referred to

s. 22 -- referred to

s. 58(3) -- referred to

s. 58(4) -- referred to

MOTIONS by Superintendent of Financial Services and Minister of Environment for stay of application by company for receiving order under Bankruptcy and Insolvency Act and for appointment of receiver.

***C. Campbell J.*:**

1 Several motions were heard together, all in connection with a failed restructuring pursuant to the *Companies Creditor Arrangement Act* ("CCAA.")

2 Since the extension order under the CCAA was to expire on November 18, 2005 at midnight and any extension thereof was opposed by General Chemical Canada Ltd. ("the Company"), its major secured creditor and the prospective purchaser of assets, all motions were heard in a compacted time frame.

3 The anticipated sale of all of the assets on a going concern basis failed, since the prospective purchaser was not prepared to assume liability for environmental liabilities associated with a soda ash settling basin facility.

4 Harbert Distressed Investment Fund, L.P. and related entities ("Harbert" or "the Secured Creditor") sought a receiving order pursuant to s. 47(1) of the *Bankruptcy and Insolvency Act.*, R.S.C. 1985 c. B-3 ("BIA") to appoint PricewaterhouseCoopers Inc. ("PWC") as interim receiver of the undertakings and property of the Company.

5 The Secured Creditor and the Company also sought an order vesting the assets in the interim receiver for the purpose of sale to it, approval for which was sought on expiration of CCAA extension on November 18, 2005.

6 The Company sought a declaration in respect of its bankruptcy to be effective November 18, 2005 on its filing on November 22, 2005.

7 The Superintendent of Financial Services ("the Superintendent") sought to impose restraint on the Company

making an assignment in bankruptcy until determination of the trust status of unpaid pension plan contributions. The relief sought by the Superintendent was supported by the Canadian Auto Workers Union ("CAW-Canada") and opposed by the Company and the Secured Creditor.

8 The Ministry of the Environment ("MOE") sought the appointment of a receiver, the purpose of which was to enable the Company to comply with environmental orders prior to any sale of assets or assignment under the BIA. The position taken by both the Superintendent and the MOE is supported by CAW-Canada.

9 The Superintendent and the MOE oppose the appointment of the Interim Receiver proposed by the Company, its parent General Chemical Canada Holding Inc. ("Holding"), and the Secured Creditor, being the purchaser of certain assets supported by PricewaterhouseCoopers Inc. ("PWC" or "the Monitor.")

10 The basis of the opposition is that both the Superintendent and the MOE urge determination of the respective rights of those Ministries while the Company is in CCAA and before what is expected to be an assignment in bankruptcy. In particular, the MOE seeks extension of the CCAA proceeding on the appointment of an interim receiver over all the lands and undertaking of the Company, not just those lands that are sought to be covered in the Company's application.

11 In a companion motion to its opposition, the Superintendent sought payment of unremitted employer pension contributions to the Company's pensions plans.

12 At its essence, the position of the Superintendent is that notwithstanding the initial CCAA order, the Company is required to perform the duties of a pension plan administrator set out in the *Pension Benefits Act* ("PBA") and is a fiduciary in respect of plan members pursuant to s. 22 of the PBA.

13 The Initial CCAA Order granted by Farley J. on January 19, 2005 provided for a stay of proceedings but in doing so, specifically permitted the Company to make pension plan payments.

14 The Company responded to a request for information from the Office of the Superintendent that in accordance with its financial projections, the Company simply did not "have the financial resources to make special payments under the plan."

15 The Company took the position that "the Initial Order provides for current service costs of continuing employees to be paid, thus responding to the concern that accruing benefits of active employees do not prejudice the financial plans for inactive employees."

16 The following paragraphs from the Superintendent's factum set out its state of knowledge:

> 18. Based on this exchange of correspondence, FSCO [Superintendent] staff understood that the Applicant's assessment of its financial position in January 2005 indicated that there were insufficient assets available to make special payments to the pension plans. FSCO [Superintendent] staff also understood that current service contributions for the employees who continued employment after January 14, 2005 (the "retained employees") were being made to the funds for the pension plans.
>
> 19. FSCO [Superintendent] staff were advised by representatives of the Applicant at various points during the *CCAA* restructuring process that efforts were being made to market the assets of the Applicant with a view to completing a sale of all or part of the Applicant's assets on a going concern basis. The Superintendent was

> also advised that no decisions in respect of the pension plans would be made until the bids submitted by prospective purchasers were assessed and there were discussions with the CAW. In fact, the Applicant entered into a conditional Asset Purchase Agreement on July 7, 2005.

17 The Superintendent had understood that current service (as opposed to past unpaid) contributions would be made. While funds had been set aside, they were not paid. The Court understands they have now been made as part of this proceeding.

18 As a result of the Superintendent's understanding that the Company did not have the financial resources to make the required pension plan contribution at the time the Initial Order was granted, it did not actively pursue the remedies now sought.

19 It would now appear that the issue of current service contributions is resolved and the issue raised by the Superintendent relates only to past contributions not made. The main reason that current contributions are no longer an issue, is that unknown to the Superintendent, cash reserves increased during the time from the Initial Order.

20 The motion request on behalf of the Superintendent supports the appointment of a Receiver to enable pension contribution payments to be made prior to the assignment in bankruptcy proposed by the Company.

21 The Superintendent urges that there is no pressing requirement to have a bankruptcy prior to the payment of pension claims. More importantly, the Superintendent submits it would be unfair and inequitable to permit secured creditors to utilize the bankruptcy procedures to compound what is alleged to be the Company's breach of statutory and fiduciary duties.

22 The following paragraphs from the factum of the Superintendent set out the position of his office. Footnotes are omitted:

> [34] The amounts owing to the Pension Plans on account of the unpaid contributions are subject to a deemed trust in favour of the pension beneficiaries. Under subsection 57(3) of the *PBA*, the Applicant is deemed to hold in trust, for the benefit of the members and former members of the pension plans, an amount of money equal to the contributions due but not paid into the Pension Plans.
>
> [35] "Contributions" owing by an employer include those amounts owing on account of both current service contributions and in respect of special payments. Contributions owing by an employer accrue on a daily basis.
>
> [36] The deemed trusts provided for by subsections 57(3) and (4) give the pension claims priority over secured claims and all unsecured claims against the Applicant. Monies held in trust are not the property of the trustee and are not subject to attachment by creditors. Subsection 30(7) of the *Personal Property Security Act* ("PPSA") reinforces this by providing, that pension beneficiaries have priority over any other security interests in accounts and inventory.
>
> [37] Section 57(5) of the *PBA* provides that the Applicant in its capacity as administrator of the Pension Plans has a lien and charge on the Applicant's assets in the amount equal to the deemed trusts under subsections 57(3) and (4).

23 The Superintendent relies on the decision of Farley J. in *Toronto Dominion Bank v. Usarco Ltd.*, [1991] O.J. No.

1314 (Ont. Gen. Div.) for the proposition that the deemed trust provisions of ss. 58(3) and 58(4) of the PBA applied in that case with pension plan contributions which were to have been made were not. In that case the security interest of the bank in the situation of a failed but not proceeded with bankruptcy petition was held to be subordinate to the interest of the beneficiaries of the deemed trust, which extended to the amount owing but unpaid on pension contributions.

24 That case can be distinguished. In *Usarco*, the motion by the plan administrator was made in objection to the secured creditors' appointment of a receiver to sell and dispose of assets. The issue before this Court involves a CCAA proceeding that has been ongoing for some months. The motion before the Court is not to avoid the payment of pension obligations. In any event, the payments that have become due during the CCAA proceedings have now been paid.

25 The second decision the Superintendent seeks to distinguish is *Ivaco Inc., Re*, [2005] O.J. No. 3337 (Ont. S.C.J. [Commercial List]), where the Court considered whether or not to grant an order (requested also by the Superintendent) requiring the payment of contributions to pension plans that were maintained by debtor. Certain of the secured creditors had filed motions seeking certain relief with a view to moving the debtor towards bankruptcy. The Court in *Ivaco Inc.* refused to order the immediate payment of pension plan contributions.

26 The basis on which the Superintendent in counsel's factum seeks to factually distinguish *Ivaco Inc.* has largely disappeared with the failed CCAA process and now the request to make an assignment in bankruptcy.

27 I accept that genuine issues in law continue to exist with respect to the priority to be accorded unpaid pension issues in the course of CCAA proceedings in the face of impending bankruptcy or after an assignment in bankruptcy. The fact that leave to appeal has been granted by the Court of Appeal for Ontario in *Ivaco Inc.* attests to this problem. The recent decision of the Court of Appeal in *Graphicshoppe Ltd., Re* [2005 CarswellOnt 7008 (Ont. C.A.)] (unreported, December 5, 2005, docket C42864 and M32603) attested to the difficulties of tracing.

28 In the circumstances of this case, I have concluded that the reasoning of Farley J. in *Ivaco Inc.* is directly applicable to these facts.

29 The following factual findings support the conclusion I have reached.

> [1] There is no suggestion that the CCAA proceedings initiated at the beginning of 2005 were anything but proper and appropriate. There is no suggestion by any party, including the Superintendent, that they were initiated for an improper purpose.
>
> [2] During the course of the year, all parties, including the Superintendent, believed that it was reasonable to pursue a "going concern" realization of assets.
>
> [3] The improvement in cash flow of the Applicant was thought by it to be kept by it to support a "going concern" transaction.
>
> [4] While the Superintendent did not have details of the improvement in cash flow, it did not seek to monitor that situation and did not seek to burden any potential "going concern" transaction by imposing a term such as that now sought.
>
> [5] The proximate cause of the failure of the "going concern" sale and of the CCAA proceedings was the position of the MOE in respect of environmental liabilities. [This finding should not be taken as any

criticism of the MOE.]

[6] The motion to appoint a receiver, the sale of assets to a willing purchaser and the assignment into bankruptcy by the Company were a reasonable and appropriate response by those entities following the position taken by the MOE and not for any improper purpose.

30 While I do accept the submission on behalf of the Superintendent that the Court does have discretion as to the content and terms of a receiving order, I do not conclude that the Court's discretion should be exercised in the manner sought by the Superintendent.

31 The Superintendent did have the opportunity to seek the kind of relief it now seeks, but did not, expecting as did other parties that a "going concern" sale would succeed. The Superintendent must be taken to have been aware that an insistence on the relief it now seeks and a determination in its favour might well be fatal to a "going concern" sale.

32 I do not accept, as submitted, that the result that deprives the Superintendent of a determination with respect to priority prior to a voluntary assignment in bankruptcy brings the bankruptcy process into disrepute.

33 One can understand and accept the belief of all involved that a "going concern" sale would eliminate the issue of the need to deal with priorities. There remains the genuine issue within the bankruptcy of the Company that enables the Superintendent to pursue the same remedy and does operate to preserve fairness of process.

34 I agree with the conclusions reached by Farley J. in *Ivaco Inc.*, particularly those at paragraphs 16 to 19, which read as follows:

[16] Given the limited role of the Monitor as indicated above I do not see that the Monitor in fact, law and fairness can be considered a fiduciary to the pension beneficiaries in the nature of an administrator of the Salaried Plans.

[17] Pursuant to s. 57(3) and (4) of the *Pension Benefits Act*, what is the responsibility? It is that the employer (the Ivaco Companies) be deemed to hold the pension funding monies in trust for the pension beneficiaries. However there is no provision in that legislation that the monies be paid out to the pension plan at any particular time. As discussed above, those deemed trusts may be defeated, in the sense of being inoperative to give a priority, in the event of a bankruptcy. The BIA does not contain any provision that the priority position is maintained in a bankruptcy; rather the case law is to the contrary: see *Henfrey* at p. 741; *Bassano* at pp. 201-202; *IBL* at pp. 143-4.

[18] In the end result I do not see that the Superintendent has made a compelling case to the effect that the petitions in bankruptcy should not be allowed to proceed in the ordinary course. I have reached that conclusion by weighing the factors pro and con as discussed above, including the relative benefits to all stakeholders (including workers and pensioners) to maintaining the CCAA proceedings (with the benefit of the suspension of past contributions as per the unopposed (and un-reconsidered) order of November 28, 2003, the fact that no reorganization is now possible as all Ivaco Companies (except Docap) have ceased operations and are without operational assets and that the Ivaco Companies are now essentially in a distribution of proceeds mode.

[19] However, to allow sufficient time for consideration of appeal, no action or step is to be taken with respect to dealing with the bankruptcy for at least 60 days from the release of these reasons. Of course it will be within the context of those bankruptcy proceedings that priorities will be determined if there is a bankruptcy,

keeping in mind that s. 43(7) of the BIA may be raised at the hearing of the petition.

35 To conclude otherwise (absent improper motive on the part of the Company or a major creditor) would be to negate both CCAA proceedings and bankruptcy proceedings by preventing creditors from pursuing a process of equitable distribution of the debtor's property as they believe it to be when making their decisions. The Superintendent is not for either CCAA or bankruptcy a secured creditor of which other creditors are aware.

36 On the above basis, the motion of the Superintendent to in effect restrain a voluntary assignment by limiting the authority of the Receiver and preserving the status quo is dismissed. An order setting aside current services contributions to be paid for the purposes of the Pension Plans is granted as agreed to by the Company.

Position of the MOE

37 The effect of the relief sought by the MOE is similar to that sought by the Superintendent. The MOE seeks to appoint its own receiver pursuant to s. 101 of the *Courts of Justice Act* to take effect immediately on the expiration of the CCAA proceedings.

38 The purpose of the Receivership sought by the MOE is to avoid the soda ash settling basin ("SASB") facility of the Company being "abandoned as an orphan site to be cared for remediation at the expense of the taxpayers of Ontario," a result suggested that may be inevitable if the Company is permitted to file in bankruptcy.

39 I accept the submissions on behalf of the MOE that environmental legislation comprises important public welfare statutes designed to protect the air, land and water of the Province for all members of the public. I accept that the MOE has standing to assist the Court with whom and under what circumstances a Receiver should be appointed. As I understand the position of the MOE, it is not the entity that is proposed by the Applicant that is objected to as Receiver, but rather what will be the mandate of any Receiver appointed.

40 I also accept that the state of the law at present raises (as it does in the issues raised by the Superintendent) genuine issues that involve the constitutional interplay between the provincial environmental legislation and federal bankruptcy and insolvency law.

41 Cases referred to by counsel for the MOE illustrate the unsettled state of the law. See *Panamericana de Bienes y Servicios S.A. v. Northern Badger Oil & Gas Ltd.*, [1991] 5 W.W.R. 577 (Alta. C.A.); *Strathcona (County) v. PriceWaterhouseCoopers Inc.*, 2005 CarswellAlta 1018 (Alta. Q.B.); *King (Township) v. Rolex Equipment Co.*, [1992] O.J. No. 810 (Ont. Gen. Div.)

42 I have concluded in the case before me for much the same reason given above, that the relief sought by the MOE should not be granted in this case. Like the Superintendent, the MOE did not intervene at an earlier time in the CCAA proceeding to insist that the Company or any prospective purchaser be obligated to comply. Presumably, the MOE knew that to do so while a "going concern" transaction was beign sought might impair it. This did turn out to be the case.

43 To now impair a sale of assets transaction that would maximize the benefit to creditors by postponing bankruptcy until environmental issues are addressed would in my view at this stage be unfair. I accept that the rights of the MOE within bankruptcy may be less than if they had been actively pursued and enforced while the Company was in CCAA. The creditor process of the CCAA was allowed to proceed on the expectation of all, including the MOE, that a workable deal could be achieved. That has not turned out to be the case.

44 I have concluded that there is no improper conduct or motive on the part of any of the parties to the CCAA process, including the MOE. To now permit in effect a pre-emptive position to the MOE by postponing bankruptcy would do a disservice to the creditors of the Company, including the principal secured creditor that participated for a legitimate purpose in a permitted restructuring process.

45 Any claim for in effect priority on the part of the MOE should in my view be dealt with in the bankruptcy rather than extraordinary relief that pre-empts the legitimate position of creditors who have proceeded in a totally legitimate fashion albeit in their own interests but with no impropriety.

46 The MOE did have during the course of the CCAA the opportunity to put forward its position, which in this situation brought about its failure. As noted above, I voice no criticism of the MOE for its position, but if it could not have successfully imposed a remedial situation during the course of CCAA it should not now be enabled to prevent an entirely legitimate result for creditors from taking place.

47 Since the concern raised by the MOE is to what the Receiver may do (which actions I have accepted), their objection to PricewaterhouseCoopers Inc. as receiver does not prevail. Like Farley J. in *Royal Oak Mines Inc., Re* , [1999] O.J. No. 1369 (Ont. Gen. Div. [Commercial List]), I find no fault with the Receiver proposed by the MOE but have concluded simply that given the history and what is to be done, PWC is to be preferred.

48 The relief sought by the MOE is therefore dismissed.

49 As a result of the decision reflected in these reasons, orders issued all dated November 18, 2005:

> 1. Pursuant to s. 47(1)a of the BIA appointing PricewaterhouseCoopers as interim receiver of certain assets of the Company pursuant to the terms of the Order signed in Court File No. 05-CL-6160.
>
> 2. Vesting certain assets in the Receiver for the purpose of sale to Harbert Distressed Investment Fun on the terms and conditions as more particularly set out in the Order signed and dated November 18, 2005 in Court File No. 05-CL-6160.
>
> 3. Declaring that the Company General Chemical Canada Ltd. has made an effective assignment in bankruptcy as of November 18, 2005 by filing at the office of the Office of the Official Receiver in London, Ontario on November 22, 2005 in accordance with the Order signed on November 18, 2005 in Court File No. 05-CL-5712.

50 It would not appear that costs in respect of these motions are appropriate. If, however, any party is of the view that costs should be awarded, they may make written submissions within two weeks and the response of any party opposing should be received within one week following.

Motions dismissed.

END OF DOCUMENT

12 P.P.S.A.C. (3d) 46, **37 C.B.R. (5th) 107**

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Textron Financial Canada Ltd. v. Beta Ltée/Beta Brands Ltd.

TEXTRON FINANCIAL CANADA LIMITED (Applicant) and BETA LIMITEE/BETA BRANDS LIMITED (Respondent) and BAKERY, CONFECTIONERY, TOBACCO WORKERS AND GRAIN MILLERS INTERNATIONAL UNION, LOCAL 242G and MINTZ & PARTNERS LIMITED

Ontario Superior Court of Justice

L.C. Leitch R.S.J.

Heard: July 19, 2007
Judgment: October 18, 2007[FN*]
Docket: 06-CL-6820

Counsel: E. Patrick Shea for Textron Financial Canada Limited

Steven Weisz for Sun Beta LLC

Duncan Grace for Moving Party, Bakery, Confectionery, Tobacco Workers and Grain Millers International Union, Local 242

Subject: Insolvency; Corporate and Commercial; Civil Practice and Procedure

Bankruptcy and insolvency --- Priorities of claims -- Preferred claims -- Wages and salaries of employees -- Priority over other creditors

Creditor had registered security interest over inventory and accounts of debtor -- At time of appointment of receiver, debtor owed vacation pay to its employees -- Creditor petitioned for bankruptcy and application was outstanding -- Interim distribution order directed receiver to hold reserve for vacation pay -- Union brought motion for declaration that employees' claim had priority over creditor's -- Motion dismissed -- Vacation pay was deemed to be held in trust by s. 40(1) of Employment Standards Act, 2000 -- Priority given by s. 30(7) of Personal Property Security Act probably did not apply as creditor had perfected purchase-money security interest in inventory and its proceeds -- In any event, priorities established by provincial legislation were superseded by those created by s. 136 of Bankruptcy and Insolvency Act ("BIA") -- Vacation pay reserve was not excluded property under BIA -- Debtor did not in fact hold those funds in trust and receiver had no obligation to do so -- Priorities were not crystallized on date receiver was

appointed -- Court was bound to apply priorities under BIA unless application was abandoned.

Cases considered by L.C. Leitch R.S.J.:

British Columbia v. Henfrey Samson Belair Ltd. (1989), 1989 CarswellBC 711, [1989] 1 T.S.T. 2164, 75 C.B.R. (N.S.) 1, [1989] 2 S.C.R. 24, 34 E.T.R. 1, [1989] 5 W.W.R. 577, 59 D.L.R. (4th) 726, 97 N.R. 61, 38 B.C.L.R. (2d) 145, 2 T.C.T. 4263, 1989 CarswellBC 351 (S.C.C.) -- referred to

Canadian Imperial Bank of Commerce v. Melnitzer (Trustee of) (1993), 23 C.B.R. (3d) 161, 1 E.T.R. (2d) 1, 6 P.P.S.A.C. (2d) 5, 1993 CarswellOnt 251 (Ont. Bktcy.) -- considered

Canadian Imperial Bank of Commerce v. Melnitzer (Trustee of) (1997), 1997 CarswellOnt 4609, 50 C.B.R. (3d) 79 (Ont. C.A.) -- referred to

GMAC Commercial Credit Corp. - Canada v. TCT Logistics Inc. (2005), (sub nom. TCT Logistics Inc. (Bankrupt), Re) 194 O.A.C. 360, 2005 CarswellOnt 636, 7 C.B.R. (5th) 202, 74 O.R. (3d) 382 (Ont. C.A.) -- considered

Husky Oil Operations Ltd. v. Minister of National Revenue (1995), 1995 CarswellSask 739, 1995 CarswellSask 740, 188 N.R. 1, 24 C.L.R. (2d) 131, 35 C.B.R. (3d) 1, 128 D.L.R. (4th) 1, 137 Sask. R. 81, 107 W.A.C. 81, [1995] 3 S.C.R. 453, [1995] 10 W.W.R. 161 (S.C.C.) -- referred to

Irving A. Burton Ltd. v. Canadian Imperial Bank of Commerce (1982), 17 B.L.R. 170, 2 P.P.S.A.C. 22, 134 D.L.R. (3d) 369, 1982 CarswellOnt 165, (sub nom. Huxley Catering Ltd., Re) 41 C.B.R. (N.S.) 217, 36 O.R. (2d) 703 (Ont. C.A.) -- considered

Ivaco Inc., Re (2006), 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 2006 CarswellOnt 6292, 56 C.C.P.B. 1, 26 B.L.R. (4th) 43 (Ont. C.A.) -- followed

Ontario Dairy Cow Leasing Ltd. v. Ontario (Milk Marketing Board) (1993), 4 P.P.S.A.C. (2d) 269, 1993 CarswellOnt 655 (Ont. C.A.) -- considered

Sperry Inc. v. Canadian Imperial Bank of Commerce (1985), 50 O.R. (2d) 267, 17 D.L.R. (4th) 236, 8 O.A.C. 79, 55 C.B.R. (N.S.) 68, 4 P.P.S.A.C. 314, 1985 CarswellOnt 167 (Ont. C.A.) -- considered

Textron Financial Canada Ltd. v. Beta Ltee/Beta Brands Ltd. (2007), 2007 CarswellOnt 89, 27 C.B.R. (5th) 1 (Ont. S.C.J.) -- referred to

Toronto Dominion Bank v. Usarco Ltd. (1991), 42 E.T.R. 235, 1991 CarswellOnt 540 (Ont. Gen. Div.) -- distinguished

Statutes considered:

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3

Generally -- referred to

s. 67(1) -- referred to

s. 136 -- referred to

s. 244 -- referred to

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

Generally -- referred to

Employment Standards Act, 2000, S.O. 2000, c. 41

Generally -- referred to

s. 40(1) -- considered

s. 40(2) -- considered

Pension Benefits Act, 1987, S.O. 1987, c. 35

Generally -- referred to

Pension Benefits Act, R.S.O. 1990, c. P.8

Generally -- referred to

Personal Property Security Act, R.S.O. 1980, c. 375

s. 35(1)(c) -- referred to

Personal Property Security Act, R.S.O. 1990, c. P.10

Generally -- referred to

s. 1(1) "purchase-money security interest" -- referred to

s. 30(7) -- considered

s. 30(8) -- referred to

s. 33 -- referred to

s. 33(1)(a) -- referred to

s. 33(1)(b) -- referred to

Wage Earner Protection Program Act, S.C. 2005, c. 47

Generally -- referred to

MOTION by union for declaration that claim for employees' vacation pay had priority over claim of secured creditor.

L.C. Leitch R.S.J.:

1 The Bakery, Confectionary, Tobacco Workers and Grain Millers International Union, Local 242G ("Local 242G") brings a motion for a declaration that its claim on account of vacation pay ranks in priority to the claims of the secured creditors of Beta Limitee/Beta Brands Limited ("Beta Brands") in and to Beta Brands accounts and inventory and any and all proceeds derived or to be derived therefrom. The motion is opposed by the applicant, a secured creditor of Beta Brands and Sun Beta LLC, an unsecured creditor of Beta Brands and a participant in the applicant's secured loan to Beta Brands.

Background Facts

2 The applicant holds a security interest over all of the present and future personal property of Beta Brands including, without limitation, Beta Brands' inventory and accounts pursuant to a security agreement dated December 17, 2004, which was amended August 29, 2005, and June 20, 2006. Notice of this security interest was registered under the *Personal Property Security Act*, R.S.O. 1990, c. P.1 (the "PPSA") on November 18, 2004. All secured creditors of Beta Brands that had registered financing statements against Beta Brands prior in time to the applicant's registration subordinated their interests to the applicant.

3 A default letter and a statutory notice under section 244 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B.3 (the "BIA") were sent by the applicant's counsel to Beta Brands' counsel on November 24, 2006. Beta Brands was then in negotiations with Bremner Food Group Inc. ("Bremner") respecting a sale of its assets. The applicant entered into a forbearance agreement with Beta Brands dated December 13, 2006, to facilitate the sale to Bremner. The applicant agreed to forbear enforcement of its security on certain terms and conditions and to provide financing to Beta Brands to manufacture inventory required to complete the sale to Bremner.

4 On January 3, 2007, pursuant to the order of Lax J., Mintz & Partners Limited (the "Receiver") was appointed the interim Receiver and Receiver of Beta Brands' property, which included accounts receivable and inventory. Lax J. found that the applicant has valid, perfected security over the property of Beta Brands.

5 As of January 3, 2007, the members of Local 242G were owed substantial amounts including an amount on account of vacation pay estimated at $559,000. Local 242G had opposed the appointment of the Receiver. As noted by Lax J., Local 242G submitted that the "true purpose" of the receivership "was to avoid or eliminate the contractual and/or legislative obligations for severance and termination pay, which are substantial" (*Textron Financial Canada Ltd. v. Beta Ltee/Beta Brands Ltd.*, [2007] O.J. No. 84 (Ont. S.C.J.) at para. 10).

6 By order dated January 5, 2007, the Receiver was authorized to sell Beta Brands' bakery division and certain finished goods inventory to Bremner. Local 242G also participated at the hearing that led to that order. The employment of all members of Local 242G was terminated shortly thereafter.

7 The Receiver was authorized to sell other assets by a further order dated April 12, 2007. The Receiver successfully collected some accounts receivables of Beta Brands.

8 A bankruptcy application in respect of Beta Brands and an affidavit of verification were executed by the applicant on February 20, 2007. It is clear from the Sixth Report of the Receiver that there were communications relating to a bankruptcy proceeding in February 2007 in which Local 242G participated; however, no bankruptcy application was issued.

9 An interim distribution order was granted on consent on March 1, 2007. Pursuant to that order, the Receiver established a vacation pay reserve of $550,000.00. As set out in the interim distribution order, the creation of this reserve "shall not constitute an admission or otherwise evidence that funds necessary to satisfy any liability of Beta Brands for Outstanding Vacation Pay were or are held separate and apart in trust or otherwise" (at para. 2). The order also provided that the reserve was deemed to have been drawn from the proceeds of distribution of Beta Brands' inventory and the collection of receivables.

10 At the hearing of this motion, the applicant's counsel advised that a second bankruptcy petition was issued July 17, 2007, dated July 12, 2007, and an affidavit of verification was sworn July 12, 2007.

11 It is clear that Local 242G has diligently pursued relief on behalf of its members and that there has been an ongoing "dispute" regarding their vacation pay from the outset of the receivership which predates any bankruptcy application.

Statement of Issues

12 This motion raises the following issues:

> 1. Are the former employees of Beta Brands entitled to a statutory lien in respect of vacation pay that ranks in priority to the applicant's security interest in Beta Brands inventory and accounts?
>
> 2. Are the former employees of Beta Brands entitled to a deemed trust in respect of vacation pay that ranks in priority to the applicant's security interest in Beta Brands inventory and accounts?
>
> 3. Will the bankruptcy of Beta Brands have the effect of reversing or nullifying the priority that such statutory lien or deemed trust has in respect of vacation pay?
>
> 4. If the bankruptcy of Beta Brands will reverse or nullify the priority of any lien or deemed trust in respect of vacation pay, is it appropriate for the court to order a distribution to Local 242G's members prior to the bankruptcy application in respect of Beta Brands being determined?
>
> 5. If a distribution is ordered, what procedure should be put in place to determine the quantum of the vacation pay owing to Beta Brands' former employees?

The Statutory Lien Issue

13 Section 40(2) of the *Employment Standards Act, 2000*, S.O. 2000, c.41 (the "*ESA*") establishes a statutory lien with respect to vacation pay. Section 40(2) of the *ESA* provides as follows:

> (2) An amount equal to vacation pay becomes a lien and charge upon the assets of the employer that in the ordinary course of business would be entered in books of account, even if it is not entered in the books of account.

14 Although s. 40(2) of the *ESA* provides the employees with a statutory lien in respect of their vacation pay, there is nothing in the *ESA* which establishes priority of that lien in respect of the other relevant security interests. As such, priority will be determined based on the chronological order in which the respective interest arose with the first in time having priority. The applicant was granted security over the assets and property of Beta Brands in 2004. There is no evidence that the vacation pay claimed by Local 242G on behalf of Beta Brands' former employees was accrued prior to 2004. Thus, it appears that the statutory lien does not have priority over the security interest of the applicant.

15 As a result, although Local 242G can establish a statutory lien in accordance with s. 40(2) of the *ESA*, that lien does not have priority over the applicant's security interest granted in 2004.

The Deemed Trust Issue

16 Section 40(1) the *ESA* "deems" Beta Brands to have held vacation pay in "trust" for the employees of Beta Brands. That section provides as follows:

> Every employer shall be deemed to hold vacation pay accruing due to an employee in trust for the employee whether or not the employer has kept the amount for it separate and apart.

17 The section "deems" the vacation pay owing to Beta Brands' former employees to be held "separate and apart." Thus, there is no question that the employees have a deemed trust in respect of their vacation pay held by Beta Brands. It is important to note that such a trust has been described as "a legal fiction" (see *Ivaco Inc., Re*, *infra* at para. 46).

18 The critical question is whether this deemed trust ranks in priority to the applicant's security interest in Beta Brands' inventory and accounts.

19 There is nothing in s. 40(1) of the *ESA* that establishes priority of the deemed trust. Guidance on this point comes from the *PPSA*.

20 Section 30(7) of the *PPSA* provides the following:

> A security interest in an account or inventory and its proceeds is subordinate to the interest of a person who is the beneficiary of a deemed trust arising under the *Employment Standards Act* or under the *Pension Benefits Act*.

21 Section 30(8) of the *PPSA* provides that subsection (7) does not apply to a perfected purchase-money security interest in inventory or its proceeds.

22 A contentious issue on this motion is whether the applicant has a perfected purchase-money security interest in Beta Brands' inventory or its proceeds. There is no dispute that the applicant's security interest was perfected. If the applicant's interest in Beta Brands' inventory is a purchase-money security interest then the deemed trust in favour of Beta Brands employees will be subordinate to the applicant's security interest.

23 A purchase-money security interest (a "PMSI") is defined in s. 1(1) of the *PPSA* as follows:

"purchase-money security interest" means,

> (a) a security interest taken or reserved in collateral, other than investment property, to secure payment of all or part of its price,
>
> (b) a security interest taken in collateral, other than investment property, by a person who gives value for the purpose of enabling the debtor to acquire rights in or to the collateral, to the extent that the value is applied to acquire the rights, or
>
> (c) the interest of a lessor of goods under a lease for a term of more than one year;

24 Local 242G takes the position that there is no evidence which suggests that the applicant's security interest is a PMSI in inventory or its proceeds. Local 242G points out that portions of the applicant's advances were operating loans, while acknowledging that the forbearance agreement contemplated funding for purposes of an inventory build. The applicant is of the view that they do, in fact, have such a security interest on the basis that it advanced all funds to produce the inventory, there were no other operating lenders, and the proceeds from the sale of that inventory are traceable.

25 Local 242G also advances the proposition that when the agreement of purchase and sale with Bremner was signed, all of the assets of Beta Brands were converted to an account and thus, the applicant would lose the benefit of a PMSI. As Local 242G points out, the Ontario Court of Appeal in *Irving A. Burton Ltd. v. Canadian Imperial Bank of Commerce* (1982), 2 P.P.S.A.C. 22 (Ont. C.A.) concluded that at p. 23:

> Accordingly, from the moment the contract for sale was made by Huxley Catering Limited the right to the purchase money was a chose in action that was capable of being assigned.

This contract for sale was made before Huxley Catering Ltd. made an assignment in bankruptcy. As a result, the bank was entitled to the purchase money pursuant to its assignment of book debts and the proceeds were not available to the Trustee in Bankruptcy for distribution to all creditors.

26 Section 33 of the *PPSA* sets out the requirements that must be complied with in order for a PMSI in inventory or its proceeds to have priority over any other security interest in the same collateral. There is no dispute that the applicant's security interest was perfected at the time Beta Brands obtained possession of the inventory as required by subsection 33(1)(a). Although the applicant did not give notice in writing to every other secured party who has registered a financing statement in which the collateral is classified as inventory before the date of registration by the applicant as required by subsection 33(1)(b), I agree with the applicant's counsel that notice to such creditors was not required to obtain priority because the applicant had the benefit of subordination agreements from such creditors.

27 It seems to me that the applicant has a PMSI in Beta Brands' inventory and its proceeds based upon its position set out above. Therefore, s. 30(7) would not be applicable and the deemed trust would not rank in priority to the applicant's PMSI in inventory and its proceeds. I appreciate the perspective of Local 242G that the evidentiary foundation for the PMSI is limited and indeed, the applicant took the position that it was unnecessary to determine whether it had a PMSI in inventory and its proceeds because the applicant was prepared to ground its opposition to the motion on the applicability of the priority rules in bankruptcy. As a result, the main issue on this motion was whether the priority of the deemed trust can prevail in these circumstances where a bankruptcy application was signed and an affidavit of verification sworn, after the Receiver was appointed but remained outstanding. I will now turn to consideration of the impact of bankruptcy on the deemed trust.

The Impact of Bankruptcy on the Deemed Trust

28 The law is well established that the change in priorities that is created by the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "*BIA*") supersedes the priorities established by the relevant provincial legislation. Section 136 of the *BIA* establishes the priority of claims on a bankruptcy. Application of this provision creates a result in which the vacation pay claims of Beta Brands' former employees characterized as either a lien or a trust ranks subordinate to the claims of Beta Brands' secured creditors, but would have priority over the claims of Beta Brands' unsecured creditors. The *ESA* as provincial legislation cannot alter priorities established by the *BIA*. Thus, the priority in respect of the deemed trust established by s. 30(7) of the *PPSA* (assuming the applicant did not have a PMSI in inventory and its proceeds) would not be effective in a bankruptcy (see *British Columbia v. Henfrey Samson Belair Ltd.* (1989), 75 C.B.R. (N.S.) 1 (S.C.C.) and *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453 (S.C.C.)). Local 242G quite properly acknowledged that if the priority rules in bankruptcy are relevant, then s. 30(7) of the *PPSA* is inoperative.

Will the Trust relating to the Vacation Pay be Excluded Property on Bankruptcy?

29 As discussed more fully below, the position of Local 242G is that the priority rules in bankruptcy have no relevance on this motion. The alternative position is that even if those priority rules apply, Local 242G's claim to vacation pay would be effective against a trustee in bankruptcy because the Receiver was obliged to create a reserve for vacation pay as part of its fiduciary obligations.

30 I will deal first with the alternative position of Local 242G. Local 242G relies on the provisions of s. 67(1) of the *BIA*, which defines property to exclude property that the bankrupt holds in trust. Thus, Local 242G submits that even if the priority rules under the *BIA* apply, the deemed trust would still have priority by virtue of the definition of property in s. 67(1) of the *BIA*. To fit within this exception, the trust must satisfy the requirements of the general law of trusts (described in *Ivaco Inc., Re*, *infra* at para. 39 as "the three certainties of a common law trust: certainty of intent; certainty of subject matter; and certainty of object") and the trust property must be kept separate and apart, and be traceable (see *British Columbia v. Henfrey Samson Belair Ltd.*, *supra*).

31 The position of Local 242G is that the Receiver knew vacation pay was owed when it was appointed and when it terminated the employment Local 242G's members. Although Local 242G does not suggest on this motion that the Receiver is personally liable for vacation pay, it asserts that the Receiver knowing there was a priority dispute had the obligation to set aside moneys to answer the employees' claims to vacation pay in the event that their claims were found to have priority. To put it more simply, Local 242G says that the Receiver should have established a separate fund to which the deemed trust could attach and thus be excluded from Beta Brands' property upon bankruptcy. According to Local 242G, the interim distribution order in regard to vacation pay merely confirmed what the Receiver was already obliged to do -- identify and segregate property or proceeds to satisfy the vacation pay liability thereby creating a trust that is not excluded property in the event of a bankruptcy.

32 The applicant's position, supported by Sun Beta, is that Beta Brands held no property in trust that can be excluded from the impact of bankruptcy -- in other words, there is no actual trust that can survive the bankruptcy of Beta Brands. They note that Beta Brands did not actually segregate any assets separate and apart in respect of vacation pay and that the terms of the interim distribution order limited the significance of the creation of the reserve for vacation pay. They also take the position that it is important that the Receiver maintain the status quo. Thus, in their view, Local 242G's proposition is inconsistent with the Receiver's obligations and is unworkable because a Receiver ought not to determine priorities of competing complainants absent a specific statutory requirement such as was before the court in *TCT Logistics Inc.*, *infra* discussed in more detail below.

33 Despite the able argument of counsel for Local 242G, I cannot accept the propositions he advanced. Beta Brands did not hold any funds separate and apart for vacation pay and was not obliged to do so. Therefore, there can be no actual trust in favour of the former employees that survives a bankruptcy. The interim distribution order required the Receiver to establish a reserve for the vacation pay pending a determination of the employees' entitlement in priority to the rights of Beta Brands' secured creditors. The order specifically provided that the reserve was not an admission or other evidence that the vacation pay was being held separate and apart from Beta Brands' assets and property. I disagree with Local 242G that the Receiver, knowing there was a priority dispute, was obliged to create a segregated fund for vacation pay. The Receiver's obligation cannot exceed what the debtor was obliged to do. The Receiver "stands in the shoes of the debtor, and is furthermore acting as an officer of the court" as the Court of Appeal noted in *GMAC Commercial Credit Corp. - Canada v. TCT Logistics Inc.* (2005), 7 C.B.R. (5th) 202 (Ont. C.A.), at 216. In that case, the legislation in issue required the debtor to maintain a segregated fund to satisfy the trust obligation in issue and the Receiver was similarly obliged to do so. Here Beta Brands was under no such obligation in relation to vacation pay. It was not required to, and did not, maintain a separate fund on account of vacation pay. Thus there is no segregated fund for the Receiver to maintain and preserve and the Receiver is under no obligation to create such a fund.

Are the Priority Rules in Bankruptcy Relevant?

34 I will turn next to the issue of whether the priority rules in bankruptcy are relevant on this motion. Local 242G asserts that the court has an obligation to determine priority issues based on the facts as they exist at the time the rights of the competing complainants came into conflict. I am urged to focus on when the priority issue crystallized and determine the priority dispute as at that date.

35 Local 242G emphasizes that its dispute regarding the vacation pay has been clear from "day one," and it made every possible effort to collect vacation pay from that day. Local 242G's position on this motion is grounded on the fact that when the dispute regarding the vacation pay arose a bankruptcy proceeding was not pending, nor had a bankruptcy occurred. The position of Local 242G is that the employees ought not to be deprived of their vacation pay because there might be a bankruptcy.

36 The applicant's position, again supported by Sun Beta LLC, is that the appointment of the Receiver does not crystallize the date on which priorities are determined and until a bankruptcy proceeding is effectively abandoned or denied, the court should not order a distribution to creditors whose claims would be subordinated by the bankruptcy.

37 Local 242G relies on *Sperry Inc. v. Canadian Imperial Bank of Commerce* (1985), 50 O.R. (2d) 267 (Ont. C.A.) for its position that the priority issues should be determined when the priority dispute crystallized (which Local 242G asserts is the date the Receiver was appointed, and thus a date when there was no application in bankruptcy). The issue in *Sperry Inc.* was the priority of the security interests of Sperry Rand Inc. and the Canadian Imperial Bank of Commerce in the unpaid inventory of W.J. Allinson Farm Equipment & Supplies Limited. The Court of Appeal found that neither Sperry nor the bank had registered or perfected their security interests, with the result that Sperry's security interest had priority under s. 35(1)(c) of the *Personal Property Security Act*, R.S.O. 1980, c. 375 (now see R.S.O. 1990, c. P.10, s. 30(1)(4)) as the first security interest attached. After making that determination, the Court of Appeal went on to express its views "on different bases for coming to the same conclusion" (*Sperry Inc.*, *supra*, at 278). The Court said, in *obiter*, "that it would be reasonable to conclude that the priority issue between the parties should be resolved as of the time when their respective security interest came into conflict" (*Sperry Inc.*, *ibid*).

38 This principle was adopted by the Ontario Court of Appeal in *Ontario Dairy Cow Leasing Ltd. v. Ontario (Milk Marketing Board)*, [1993] O.J. No. 464 (Ont. C.A.) where it concluded, "The priority issue between the parties must be resolved as of the time when their respective security interests came into conflict" (at para. 4).

39 The principle in *Sperry Inc.* that a priority dispute is addressed as at the date the conflict arose was also adopted by Mr. Justice Killeen in *Canadian Imperial Bank of Commerce v. Melnitzer (Trustee of)*, [1993] O.J. No. 3021 (Ont. Bktcy.), aff'd [1997] O.J. No. 4634 (Ont. C.A.) [*Melnitzer*]. At para. 194 of his reasons, Killeen J. concluded that once "808756 Ontario rights came into 'conflict' with those of other creditors on August 3 when the Receiver, Coopers & Lybrand, took over control of the assets [...] under the rule laid down in *Sperry Inc. v. CIBC* 808756 Ontario's then unperfected interest [was] prevented from acquiring a higher status by later acts such as the August 29 registration."

40 Local 242G also relies on the decision in *Toronto Dominion Bank v. Usarco Ltd.*, 1991 CarswellOnt 540 (Ont. Gen. Div.). The decision in *Usarco Ltd.* dealt with deemed trust provisions in the *Pension Benefits Act*, S.O. 1987, c. 35. In that case, a bankruptcy petition was filed, dated January 5, 1990. As a term of an adjournment, the Receiver undertook to "hold $500,000 collected since November 7, 1991 (sic) from the proceeds of accounts receivable and inventories of Usarco until the return of the motion [...]" (*Usarco Ltd.*, *supra*, at para. 8).

41 By the date of judgment on August 2, 1991, no further action had been taken on the petition in bankruptcy. The bank indicated that no such move would be made until certain real property was sold, but without providing any likely timetable. The pension administrator argued that the deemed trust had been converted to a true trust by virtue of the Receiver having separated the funds pursuant to the undertaking, or by virtue of notice. Mr. Justice Farley found that "it would be inappropriate for the Bank to put all proceedings involving Usarco (including this motion by the Administrator) into suspended animation while the Bank determined if, as and when it wished to take action" (*Usarco Ltd.*, *supra*, at para. 9). He ordered the Receiver to pay out the amounts covered by the deemed trust provisions in the *Pension Benefits Act*, *supra*.

42 Local 242G submits that while *Usarco Ltd.* was distinguished in *Ivaco Inc., Re*, 2006 CarswellOnt 6292 (Ont. C.A.), a case relied on by the applicant, the principles underlying the reasoning in *Usarco Ltd.* were not commented on and should be applied here where the circumstances are even more compelling because the priority dispute arose before the bankruptcy application began.

43 The applicant submits that the decision in *Usarco Ltd.* is also distinguishable on its facts on this motion, and relies on the principles established in *Ivaco Inc., Re* in support of its position. In *Ivaco Inc., Re* deemed trust provisions in the *Pension Benefits Act*, R.S.O. 1990, c. P.8 were again considered. Proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 [*CCAA*], had run their course, and an application under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 [*BIA*] was pending. The court found that there was no requirement to segregate the amounts of the deemed trust under the *CCAA*, and that there was no gap between the *CCAA* and the *BIA* that would allow an order to pay out the deemed trust amounts. The Court of Appeal noted that provinces cannot directly alter priorities under the *BIA*, and in *Ivaco Inc., Re* refused to allow them to do so indirectly.

44 While I agree with Local 242G that, according to *Sperry Inc.*, priorities as between competing security interests are determined when they come into conflict, I do not agree that priorities are "crystallized" or frozen on the date a Receiver is appointed such that the subsequent occurrence of a bankruptcy is not relevant to the court's analysis. It seems to me that it was key to the conclusion of Killeen J. in *Melnitzer (Trustee of)* that the receivership order, by its terms, "effectively prevented 808756, or any other creditor, from improving its priority position thereafter" (*supra*, at para. 189). The receivership order made by Lax J. January 3, 2007 does not contain terms and provisions of a similar nature. Indeed, paragraph 5 of the order, as the applicants' counsel points out, permits the filing by creditors of any registration to preserve or protect a security interest and the registration of a claim for lien and the order specifically contemplates that any party may apply to amend or vary it.

45 I agree with the applicant and Sun Beta that the facts on this motion are distinct from those considered by the

court in *Usarco Ltd.* In *Usarco Ltd.* the bankruptcy application had been effectively abandoned, and it was arguable that the funds were actually segregated and held in trust by the Receiver. As the court in *Ivaco Inc., Re* observed in distinguishing the case, "in *Usarco Ltd.* the petitioning creditor was not proceeding with its bankruptcy petition because its principal had died, and no other creditor took steps to advance the petition. Thus, unlike in this case, in *Usarco Ltd.* it was unclear whether bankruptcy proceedings would ever take place" (*Ivaco Inc., Re*, *supra*, at para. 67). For similar reasons, I find the facts on this motion different from those considered in *Usarco*. A bankruptcy application in respect of Beta Brands was signed by the applicant on February 20, 2007, and a further petition was issued just prior to the hearing of this motion. Although the first application was not proceeded with it cannot be said that it has been "effectively abandoned" and, indeed, a further petition was issued.

46 The *Ivaco Inc., Re* case established that the court should not exercise its discretion to order distribution of pension amounts where a bankruptcy application is pending and the effect of bankruptcy will be to subordinate the claim for pension amounts to claims of the secured creditors. In *Ivaco Inc., Re*, the court noted at paragraph 64 that "where a creditor seeks to petition a debtor company into bankruptcy at the end of CCAA proceedings, any claim under a provincial deemed trust must be dealt with in bankruptcy proceedings [...]. Were it otherwise, creditors might be tempted to forgo efforts to restructure a debtor company and instead put the company immediately into bankruptcy. That would not be a desirable result."

47 The facts on this motion are in line with those before the court in *Ivaco Inc., Re* where the creditors were actively seeking to petition the debtor company into bankruptcy. The principles established in *Ivaco Inc., Re* support a determination that this court should not exercise its discretion to order distribution of vacation pay where a bankruptcy application is to be heard and the effect of the bankruptcy will be to subordinate the claim for vacation pay. As a result this motion by Local 242G must be dismissed.

48 The following words of the Court of Appeal at para. 69 of *Ivaco Inc., Re* with respect to pension claimants are equally applicable to the claims of Local 242G's members in relation to their vacation pay:

> Because the federal legislative regime under the CCAA and the BIA determines the claims of creditors of an insolvent company, if the rights of pension claimants are to be given priority, Parliament, not the courts, must do so.

Indeed as noted in *Ivaco Inc., Re* at para. 69, "Parliament has at least signalled its intentions to do so" by passage of the *Wage Earner Protection Program Act*, S.C. 2005, c.47, which, as the court noted, had not then been proclaimed in force. As of this date, this legislation still has not been proclaimed. This legislation, which defines "wages" to include vacation pay, would establish a program to enable individuals to collect "wages" from employers who are bankrupt or subject to a receivership. Regrettably for the members of Local 242G, without such legislation that would give their claim priority, the declaration they seek cannot be granted.

Motion dismissed.

FN*. A corrigendum issued by the court on November 13, 2007 has been incorporated herein.

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2009 BCCA 205, [2009] B.C.W.L.D. 3450, [2009] B.C.W.L.D. 3452

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Ted Leroy Trucking Ltd., Re

In the Matter of the Companies' Creditors Arrangement Act, R.S.B.C. 1985, c. C-36

And In the Matter of the Business Corporations Act, R.S.B.C. 2002, c. 57

And In the Matter of Ted LeRoy Trucking Ltd. and 383838 B.C. Ltd.

The Attorney General of Canada on behalf of Her Majesty the Queen in right of Canada (Appellant) and Ted LeRoy Trucking Ltd., 383838 B.C. Ltd., Century Services Inc. and PricewaterhouseCoopers Inc. in its capacity as Monitor (Respondents)

British Columbia Court of Appeal

D. Smith J.A., Newbury J.A., and Tysoe J.A.

Heard: March 30, 2009
Judgment: May 7, 2009
Docket: Vancvouer CA036474

Proceedings: reversing *Ted Leroy Trucking Ltd., Re* (2008), 2008 CarswellBC 2895, 2008 BCSC 1805, [2008] G.S.T.C. 221 (B.C. S.C. [In Chambers])

Counsel: D.W. Jacyk, K.K. Khalsa for Appellant

M.I.A. Buttery, M.J.G. Curtis for Respondent, Century Services Inc.

Subject: Estates and Trusts; Goods and Services Tax (GST); Tax -- Miscellaneous; Insolvency

Tax --- Goods and Services Tax -- Collection and remittance -- GST held in trust

Debtor commenced proceedings under Companies' Creditors Arrangement Act ("CCAA") -- Debtor obtained order staying all proceedings while it attempted to restructure its financial affairs -- Debtor company owed Crown pursuant

to Excise Tax Act ("ETA") in respect of GST collected -- Debtor company brought application for court approval of distribution of sale proceeds and for leave to assign itself into bankruptcy -- Crown brought application for order that monies be held in trust by monitor to be paid to Receiver General of Canada -- Debtor's application was granted and Crown's application was dismissed -- Crown appealed -- Appeal allowed -- Funds paid into trust account of monitor were to be paid to Receiver General -- There was actual or express trust that should have been recognized by chambers judge -- While chambers judge had authority to stay Crown's right to enforce **deemed trust** during period in which debtor attempted to reorganize its financial affairs, after restructuring efforts came to end, chambers judge did not have discretion to ignore **deemed trust** under s. 222 of ETA or express trust that was created in favour of Crown when debtor paid funds into trust account of monitor -- Crown was entitled to rely on **deemed trust** and express trust -- Chambers judge did not have discretion to decide whether pre-bankruptcy or post-bankruptcy scheme of distribution should be preferred -- He was bound to apply scheme of distribution in effect at time he was asked to deal with funds -- Express trust was created once chambers judge made his order and amount was paid into trust account of monitor -- Common law requirements for trust were all met -- Monies were intended to be held in trust and that investment of funds in term deposit kept them identifiable -- Chambers judge did have authority to order funds to be paid out of monitor's trust account because they were paid into trust account pending further order of court -- It was clearly contemplated that there would be order in CCAA proceedings directing payment of funds out of trust account.

Tax --- General principles -- Priority of tax claims in bankruptcy proceedings

Debtor commenced proceedings under Companies' Creditors Arrangement Act ("CCAA") -- Debtor obtained order staying all proceedings while it attempted to restructure its financial affairs -- Debtor company owed Crown pursuant to Excise Tax Act ("ETA") in respect of GST collected -- Debtor company brought application for court approval of distribution of sale proceeds and for leave to assign itself into bankruptcy -- Crown brought application for order that monies be held in trust by monitor to be paid to Receiver General of Canada -- Debtor's application was granted and Crown's application was dismissed -- Crown appealed -- Appeal allowed -- Funds paid into trust account of monitor were to be paid to Receiver General -- There was actual or express trust that should have been recognized by chambers judge -- It was clearly contemplated that there would be order in CCAA proceedings directing payment of funds out of trust account -- There were valid policy reasons for encouraging insolvent companies to attempt to restructure their affairs so that their businesses could continue with little disruption to employees and other stakeholders -- It was appropriate for courts to take such policy considerations into account, but only if it was in connection with matter that was not considered by Parliament -- Parliament would have specifically identified **Bankruptcy** and **Insolvency Act** as exception when enacting current version of s. 222(3) of ETA without considering CCAA as possible second exception.

Cases considered by *Tysoe J.A.*:

> *Alnav Platinum Group Inc. v. APM Delstar Inc.* (2001), 2002 G.T.C. 1178, 2001 ABQB 930, 2001 CarswellAlta 1777, 306 A.R. 233, 32 C.B.R. (4th) 1, [2002] G.S.T.C. 21 (Alta. Q.B.) -- considered
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> *Fine's Flowers Ltd. v. Fine's Flowers Ltd. (Creditors of)* (1993), (sub nom. *Fine's Flowers Ltd. v. Creditors of Fine's Flowers Ltd.)* 16 O.R. (3d) 315, 14 B.L.R. (2d) 178, 1993 CarswellOnt 236, 22 C.B.R. (3d) 1, 108 D.L.R. (4th) 765, (sub nom. *Ontario v. Fine's Flowers Ltd.)* 65 O.A.C. 316 (Ont. C.A.) -- considered
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> *First Vancouver Finance v. Minister of National Revenue* (2002), [2002] 3 C.T.C. 285, (sub nom. *Minister of National Revenue v. First Vancouver Finance)* 2002 D.T.C. 6998 (Eng.), (sub nom. *Minister of National Revenue v. First Vancouver Finance)* 2002 D.T.C. 7007 (Fr.), 288 N.R. 347, 212 D.L.R. (4th) 615, [2002] G.S.T.C. 23, [2003] 1 W.W.R. 1, 45 C.B.R. (4th) 213, 2002 SCC 49, 2002 CarswellSask 317, 2002 CarswellSask 318, [2002] 2 S.C.R. 720 (S.C.C.) -- considered

Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 51 B.C.L.R. (2d) 84, 1990 CarswellBC 394, 4 C.B.R. (3d) 311, *(*sub nom. *Chef Ready Foods Ltd. v. Hongkong Bank of Canada)* [1991] 2 W.W.R. 136 (B.C. C.A.) -- followed

Ivaco Inc., Re (2006), 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 2006 CarswellOnt 6292, 56 C.C.P.B. 1, 26 B.L.R. (4th) 43 (Ont. C.A.) -- referred to

Minister of National Revenue v. Points North Freight Forwarding Inc. (2000), 2000 SKQB 504, 200 Sask. R. 283, [2001] 3 W.W.R. 304, [2001] G.S.T.C. 87, 24 C.B.R. (4th) 184, 2000 CarswellSask 641 (Sask. Q.B.) -- considered

Ottawa Senators Hockey Club Corp., Re (2005), 2005 G.T.C. 1327 (Eng.), 6 C.B.R. (5th) 293, 2005 D.T.C. 5233 (Eng.), 2005 CarswellOnt 8, [2005] G.S.T.C. 1, 193 O.A.C. 95, 73 O.R. (3d) 737 (Ont. C.A.) -- followed

Royal Bank v. Sparrow Electric Corp. (1997), 193 A.R. 321, 135 W.A.C. 321, [1997] 2 W.W.R. 457, 208 N.R. 161, 12 P.P.S.A.C. (2d) 68, 1997 CarswellAlta 112, 1997 CarswellAlta 113, 46 Alta. L.R. (3d) 87, *(*sub nom. *R. v. Royal Bank)* 97 D.T.C. 5089, 143 D.L.R. (4th) 385, 44 C.B.R. (3d) 1, [1997] 1 S.C.R. 411 (S.C.C.) -- referred to

Royal Oak Mines Inc., Re (1999), 1999 CarswellOnt 625, 6 C.B.R. (4th) 314, 96 O.T.C. 272 (Ont. Gen. Div. [Commercial List]) -- considered

Statutes considered:

Bankruptcy *and* ***Insolvency Act***, R.S.C. 1985, c. B-3

Generally -- referred to

s. 67(2) -- referred to

s. 67(3) -- referred to

Bankruptcy *and* ***Insolvency Act****, the Companies' Creditors Arrangement Act and the Income Tax Act, Act to amend the*, S.C. 1997, c. 12

Generally -- referred to

Canada ***Pension*** *Plan*, R.S.C. 1985, c. C-8

Generally -- referred to

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

Generally -- referred to

s. 11 -- considered

s. 11.4 [en. 1997, c. 12, s. 124] -- referred to

s. 11.8(3)-11.8(9) [en. 1997, c. 12, s. 124] -- referred to

s. 18.2 [en. 1997, c. 12, s. 125] -- referred to

s. 18.3(1) [en. 1997, c. 12, s. 125] -- considered

s. 18.3(2) [en. 1997, c. 12, s. 125] -- considered

s. 18.4 [en. 1997, c. 12, s. 125] -- referred to

s. 18.5 [en. 1997, c. 12, s. 125] -- referred to

s. 21 [en. 1997, c. 12, s. 126] -- referred to

Employment Insurance Act, S.C. 1996, c. 23

Generally -- referred to

Excise Tax Act, R.S.C. 1985, c. E-15

Pt. IX [en. 1990, c. 45, s. 12(1)] -- referred to

s. 222 [en. 1990, c. 45, s. 12(1)] -- considered

s. 222(1) [en. 1990, c. 45, s. 12(1)] -- considered

s. 222(1) [rep. & sub. 2000, c. 30, s. 50(1)] -- referred to

s. 222(3) [en. 1990, c. 45, s. 12(1)] -- considered

s. 222(3) [rep. & sub. 2000, c. 30, s. 50(2)] -- referred to

s. 317 [en. 1990, c. 45, s. 12(1)] -- referred to

s. 317(3) [en. 1990, c. 45, s. 12(1)] -- referred to

Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.)

Generally -- referred to

s. 224(1.2) -- referred to

s. 227(4.1) [en. 1998, c. 19, s. 226(1)] -- referred to

***Pension** Benefits Act*, R.S.O. 1990, c. P.8

s. 57 -- referred to

s. 57(3) -- referred to

APPEAL by Crown from decision reported at *Ted Leroy Trucking Ltd., Re* (2008), 2008 CarswellBC 2895, 2008 BCSC 1805, [2008] G.S.T.C. 221 (B.C. S.C. [In Chambers]), dismissing its application for payment of monies set aside for GST payment by debtor.

***Tysoe J.A.*:**

1 Her Majesty the Queen in right of Canada (the "Crown") appeals from an order dismissing its application on the eve of the bankruptcy of Ted LeRoy Trucking Ltd. (the "Debtor Company") to have funds being held in trust paid to the Receiver General for Canada.

2 The Debtor Company commenced proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "*CCAA*"), on December 14, 2007. As is typical in *CCAA* proceedings, the Debtor Company obtained an order staying all proceedings while it attempted to restructure its financial affairs, and an accounting firm was appointed as Monitor.

3 The Debtor Company owed the Crown, pursuant to the *Excise Tax Act*, R.S.C. 1985, c. E-15 (the "*ETA*"), in respect of goods and services tax ("GST") collected by the Debtor Company from third parties. The aggregate amount collected in reporting periods preceding the *CCAA* filing, but not remitted to the Receiver General, was the sum of $305,202.30.

4 The *ETA* provides the Crown with rights to enforce payment of unremitted GST collections. One example, which is not in issue on this appeal, is the right given to the Minister of Finance under s. 317 to issue a form of garnishment called a requirement to pay.

5 The enforcement right given to the Crown in issue on this appeal is contained in s. 222 of the *ETA*, and is commonly referred to as the "**deemed trust**" provision. Subsection (1) provides that all amounts collected on account of GST are deemed to be held by the person collecting them in trust for the Crown until they are remitted to the Receiver General. Subsection (3) creates a **deemed trust** in respect of the property of the person collecting the GST, as follows:

> (3) Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the ***Bankruptcy** and **Insolvency Act***), any enactment of a province or any other law, if at any time an amount deemed by subsection (1) to be held by a person in trust for Her Majesty is not remitted to the Receiver General or withdrawn in the manner and at the time provided under this Part, property of the person and property held by any secured creditor of the person that, but for a security interest, would be property of the person, equal in value to the amount so deemed to be held in trust, is deemed
>
> (a) to be held, from the time the amount was collected by the person, in trust for Her Majesty,

> separate and apart from the property of the person, whether or not the property is subject to a security interest, and
>
> (b) to form no part of the estate or property of the person from the time the amount was collected, whether or not the property has in fact been kept separate and apart from the estate or property of the person and whether or not the property is subject to a security interest
>
> and is property beneficially owned by Her Majesty in right of Canada despite any security interest in the property or in the proceeds thereof and the proceeds of the property shall be paid to the Receiver General in priority to all security interests.

6 The Debtor Company had been authorized by the court to conduct sales of its redundant equipment, and it applied on April 29, 2008 for court approval of the distribution of the sale proceeds. The Debtor Company proposed that, subject to a holdback of the $305,202.30 owed to the Crown on account of GST, an amount not exceeding $5 million be paid to Century Services, the major secured creditor of the Debtor Company. Over the objection of the Crown, which wanted the monies paid directly to it, the chambers judge agreed with the Debtor Company's proposal and ordered that the Monitor hold the sum of $305,202.30 in its trust account pending further order of the court. No appeal was taken by the Crown from this order.

7 The Debtor Company eventually came to the realization that it could not successfully reorganize its financial affairs. It applied on September 3, 2008 for court approval of the distribution of further sale proceeds and for leave to assign itself into bankruptcy. The Crown applied on the same day for an order that the monies held in trust by the Monitor be paid to the Receiver General. The chambers judge heard the Debtor Company's application first and granted it. He then heard and dismissed the Crown's application.

8 The reasoning of the chambers judge in dismissing the Crown's application was as follows (2008 BCSC 1805 (B.C. S.C. [In Chambers])):

> [5] I recognize that the funds collected by the petitioners pre-filing were the subject [of] the **deemed trust** provisions in the legislation. Monies were collected by the petitioner from third parties on behalf of Canada and they were not paid over to Canada. However, the triggering date was the date of the *CCAA* filing. Under the existing *CCAA* law, the court is required to maintain the status quo amongst the parties as of that date. At the date of the first day order the outstanding GST monies were owed but had not been remitted and remained in the possession of the petitioner.
>
> [6] In my view the amounts that were segregated were done to facilitate an ultimate payment of the GST monies which were owing pre-filing, but only if a viable plan emerged at the conclusion of the *CCAA* process. That has not happened. The reality is there will never be a plan in this case, but merely a sale of assets under the *BIA* as well as under the *CCAA* continued stay. That being so, it seems to me that the Crown has simply lost its preference under the provisions of the *BIA* and that that is simply a consequence of the way in which this restructuring has ended. It is no different than if the petitioner had filed under the *BIA* at the outset. The Crown is simply in the position that it is entitled to be in under the *BIA*. It will have the rights that Parliament has chosen to confer upon it under that legislation.

9 It was agreed between the parties that two additional pieces of information could be admitted on this appeal. The first is that the Debtor Company did make an assignment in bankruptcy on September 4, 2008, and the Monitor was named the trustee in bankruptcy, as well as being appointed receiver under the security held by Century Services. The second is that the Monitor invested the $305,202.30 sum in a term deposit when the monies were received from the

Debtor Company and that, on or after September 4, the term deposit plus interest thereon ($308,245.15) was paid into the general trust account of the trustee/receiver, which contained other funds.

10 Before discussing the decision of the chambers judge, I will provide a backdrop by reviewing general principles of the *CCAA* and outlining the introduction of the provisions of the *CCAA* dealing with Crown claims. I will also briefly make reference to the nature of the **deemed trust** provision in favour of the Crown.

11 Much has been written about the purpose of the *CCAA* and the stay provisions of s. 11 of the Act. One of the most often cited passages is the following paragraph from *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311 (B.C. C.A.), at 315, (1990), 51 B.C.L.R. (2d) 84 (B.C. C.A.):

> [10] The purpose of the C.C.A.A. is to facilitate the making of a compromise or arrangement between an insolvent debtor company and its creditors to the end that the company is able to continue in business. It is available to any company incorporated in Canada with assets or business activities in Canada that is not a bank, a railway company, a telegraph company, an insurance company, a trust company, or a loan company. When a company has recourse to the C.C.A.A., the Court is called upon to play a kind of supervisory role to preserve the status quo and to move the process along to the point where a compromise or arrangement is approved or it is evident that the attempt is doomed to failure. Obviously time is critical. Equally obviously, if the attempt at compromise or arrangement is to have any prospect of success there must be a means of holding the creditors at bay, hence the powers vested in the Court under s. 11.

12 Similar comments were made in *Royal Oak Mines Inc., Re* (1999), 6 C.B.R. (4th) 314 (Ont. Gen. Div. [Commercial List]), at 317, (1999), 96 O.T.C. 272 (Ont. Gen. Div. [Commercial List]):

> [7] Section 11 of the CCAA is the provision of the Act embodying the broad and flexible statutory power invested in the court to "grant its protection" to an applicant by imposing a stay of proceedings against the applicant company, subject to terms, while the company attempts to negotiate a restructuring of its debt with its creditors. It is well established that the provisions of the Act are remedial in nature, and that they should be given a broad and liberal interpretation in order to facilitate compromises and arrangements between companies and their creditors, and to keep companies in business where that end can reasonably be achieved: ..

[citations omitted]

13 When the use of the *CCAA* was resurrected in the late 1980s and early 1990s after a period of dormancy, there was uncertainty as to whether the Crown was bound by orders made in *CCAA* proceedings. There were a number of conflicting decisions, including *Fine's Flowers Ltd. v. Fine's Flowers Ltd. (Creditors of)* (1993), 108 D.L.R. (4th) 765, 22 C.B.R. (3d) 1 (Ont. C.A.), where it was held that the *CCAA* did not bind the Crown. This undermined the utility of the *CCAA* and, as a result, several provisions were added to the *CCAA* in the 1997 round of amendments to the Act (S.C. 1997, c. 12). The most important of these provisions was s. 21, which specifically provides that the *CCAA* is binding on the Crown.

14 Parliament simultaneously enacted several other provisions in the *CCAA* dealing with specific Crown claims and rights of enforcement. Section 11.4 was added to provide that a stay order can stay the garnishment rights of the Crown under s. 224(1.2) of the *Income Tax Act* and similar provisions in the *Canada **Pension** Plan* and the *Employment Insurance Act* (and comparable provisions under provincial legislation), provided that, among other things, the debtor company remains current in respect of amounts due to the Crown after the date of the stay order. Section 18.2 was

added to provide that if an order does stay the provisions referred to in s. 11.4, no compromise or arrangement shall be sanctioned by the court unless it provides for payment in full to the Crown within six months of the amounts outstanding at the date of the stay order that could have been garnished in the absence of the stay order or unless the Crown consents. Other additions dealt specifically with environmental claims (s. 11.8(3) to (9)), workers' compensation (s. 18.4), and registered security held by the Crown (s. 18.5).

15 The addition to the Act of particular importance to this matter is s. 18.3(1) dealing with **deemed trusts** in favour of the Crown:

> 18.3(1) Subject to subsection (2), notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be regarded as held in trust for Her Majesty unless it would be so regarded in the absence of that statutory provision.

Subsection (2) of s. 18.3 provides that subsection (1) does not apply to the **deemed trust** provisions in certain sections of the *Income Tax Act*, the *Canada **Pension** Plan* and the *Employment Insurance Act* (as well as similar provincial legislation). Subsection (2) does not mention s. 222 of the *ETA*.

16 Provisions virtually identical to ss. 18.3(1) and (2) are also contained in the ***Bankruptcy** and **Insolvency Act***, R.S.C. 1985, c. B-3 (the "*BIA*"), (namely, ss. 67(2) and (3)). That is why, generally speaking, **deemed trusts** in favour of the Crown are not effective in a bankruptcy situation, with the result that the Crown ranks in priority behind secured creditors in respect of the unremitted amounts giving rise to the **deemed trusts**.

17 The Supreme Court of Canada considered the nature of the **deemed trust** under s. 227(4.1) of the *Income Tax Act* (which is identical in material respects to s. 222(3) of the *ETA*) in *First Vancouver Finance v. Minister of National Revenue*, 2002 SCC 49, [2002] 2 S.C.R. 720 (S.C.C.). The issue in that case was whether the Crown could claim against accounts receivable that were factored by the taxpayer to a third party after the **deemed trust** had come into existence as a result of the failure of the taxpayer to make required remittances. In holding that the Crown could not claim against the factored accounts receivable, Mr. Justice Iacobucci likened the **deemed trust** to a floating charge:

> [40] In my view, the scheme envisioned by Parliament in enacting ss. 227(4) and 227(4.1) is that the **deemed trust** is in principle similar to a floating charge over all the assets of the tax debtor in the amount of the default. As noted above, the trust has priority from the time the source deductions are made, and remains in existence as long as the default continues. However, the trust does not attach specifically to any particular assets of the tax debtor so as to prevent their sale. As such, the debtor is free to alienate its property in the ordinary course, in which case the trust property is replaced by the proceeds of sale of such property.

18 Mr. Justice Iacobucci also commented at para. 27 that the **deemed trust** in s. 227(4.1) of the *Income Tax Act* had been strengthened by amendments in 1998 in response to the court's earlier decision in *Royal Bank v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411, 143 D.L.R. (4th) 385 (S.C.C.). The **deemed trust** provision of the *ETA* was similarly strengthened in 2000 (S.C. 2000, c. 30, s. 50) by the enactment of the present versions of ss. 222(1) and (3). One of the changes from the previous **deemed trust** provision in the *ETA* was the inclusion of the opening phrase of subsection (3): "Despite any other provision of this Act (except subsection (4)), any other enactment of Canada (except the ***Bankruptcy** and **Insolvency Act***), ..."

19 In *Ottawa Senators Hockey Club Corp., Re* (2005), 6 C.B.R. (5th) 293, 73 O.R. (3d) 737 (Ont. C.A.), the Ontario Court of Appeal was called upon to reconcile s. 18.3(1) of the *CCAA* and s. 222(3) of the *ETA* in view of the fact that

they both contained clauses with "notwithstanding" language. In that case, the Ottawa Senators Hockey Club Corporation commenced a *CCAA* proceeding but when negotiations on a restructuring proposal foundered, its assets were sold to a third party. The sale was approved by an order made in the *CCAA* proceeding. At issue was whether the **deemed trust** under s. 222(3) of the *ETA* was to be recognized, enabling the Crown to recover the unremitted GST out of the sale proceeds in priority to the claims of secured creditors.

20 Relying on the principles of statutory interpretation flowing from the facts that s. 18.3(1) of the *CCAA* was enacted earlier and was more specific than s. 222(3) of the *ETA*, the court held that s. 222(3) was to be given preference. The result was that the **deemed trust** for GST survived in a *CCAA* proceeding; the Crown was entitled to be paid the amount of the unremitted GST from the sale proceeds before any of the sale proceeds were distributed to secured creditors.

21 In the present case, the Crown relies heavily on *Ottawa Senators* and says that the chambers judge did not have a discretion to ignore the legislative will expressed in s. 222(3) of the *ETA*. With great respect to the chambers judge, I agree. It is also my view that there was an actual or express trust that should have been recognized by the chambers judge.

22 While the chambers judge had the authority to stay the Crown's right to enforce the s. 222(3) **deemed trust** during the period in which the Debtor Company attempted to reorganize its financial affairs, it is my view that, after the restructuring efforts came to an end, the chambers judge did not have a discretion to ignore the **deemed trust** under s. 222 of the *ETA* or the express trust that was created in favour of the Crown when the Debtor Company paid the funds into the trust account of the Monitor.

23 At the time of the hearing of the application, the chambers judge was acting under the *CCAA*. There was no longer any purpose under the *CCAA* to prevent the Crown from exercising its rights under the **deemed trust** or from receiving the funds being held in trust. The chambers judge was being asked to make a decision on the disposition of the funds being held in trust by the Monitor. Under the statutory regime in existence on that day, the Crown was entitled to rely on the **deemed trust** and the express trust. There was no reason to delay the decision and, as in *Ottawa Senators*, the funds should have been ordered to be paid to the Crown. The effect of the chambers judge's decision was to apply the scheme of distribution under the *BIA* before that Act had become engaged by the bankruptcy of the Debtor Company. In my opinion, the chambers judge did not have the discretion to decide whether the pre-bankruptcy or post-bankruptcy scheme of distribution should be preferred. He was bound to apply the scheme of distribution in effect at the time he was asked to deal with the funds.

24 It is my view that an express trust was created once the chambers judge made his order of April 29, 2008 and the $305,202.30 sum was paid into the trust account of the Monitor. In my opinion, the common law requirements for a trust (being certainty of intent, subject matter and object) were all met. There is no doubt that the monies were intended to be held in trust and that the investment of the funds in a term deposit kept them identifiable.

25 It may be argued that there was not sufficient certainty of object because the April 29 order stipulated that the funds were to be held in trust pending further order of the court, and the court could have ordered the funds to be paid to someone other than the Receiver General. It is my view there was sufficient certainty of object for two reasons. The first is the wording of the order itself:

> 2. the Monitor shall, pending further Order of the Court, hold the sum of $305,202.30 in its trust account in respect of the amount owing by [the Debtor Company] to the Canada Revenue Agency for pre-filing Goods and Services Tax.

The funds were being held in trust for the pre-filing GST, which was owed to the Crown.

26 Secondly, after the payments were made pursuant to the April 29 order, I am of the view that the court did not have the option of ordering the payment of the trust funds to any person other than the Receiver General. The closing words of s. 222(3) of the *ETA* provide that the Crown has a **deemed trust** covering the proceeds of the property of the person who collected the GST and that "the proceeds of the property shall be paid to the Receiver General in priority to all security interests". The court could not have authorized a payment to a secured creditor out of the proceeds from the sale of assets of the Debtor Company without ensuring payment of the GST to the Receiver General. Otherwise, the court would be sanctioning a breach of trust because it would be authorizing payment of proceeds covered by the **deemed trust** to a secured creditor in direct contravention of the closing phrase of s. 222(3). Hence, after the payment of the majority of the sale proceeds was made to Century Services, the court was required to ultimately order that the sum put aside on account of GST be paid to the Receiver General.

27 An express trust was found in the somewhat analogous circumstances of *Alnav Platinum Group Inc. v. APM Delstar Inc.*, 2001 ABQB 930, 32 C.B.R. (4th) 1 (Alta. Q.B.). There, a secured creditor had acted on its security and had collected accounts receivable owing to the debtor company. The amounts collected included GST. The amount collected exceeded the amount owed to the secured creditor and it paid the surplus to a receiver appointed at the instance of another secured creditor. The first secured creditor and the receiver entered into a "Proceeds Agreement" that referred to "Pre-Receivership G.S.T.", and the Alberta Queen's Bench ordered that the sum relating to GST claims be paid by the receiver into a separate account. On a subsequent application after the debtor company had been adjudged bankrupt, the court held that an express trust had been created and that the funds were to be paid to the Crown.

28 In the same fashion that the Crown relies on the decision in *Ottawa Senators*, Century Services relies heavily on two decisions, *Minister of National Revenue v. Points North Freight Forwarding Inc.*, 2000 SKQB 504, 24 C.B.R. (4th) 184 (Sask. Q.B.), and *Ivaco Inc., Re* (2006), 275 D.L.R. (4th) 132, 25 C.B.R. (5th) 176 (Ont. C.A.).

29 In *Points North*, a stay had been granted under the *CCAA* and the Crown applied to amend the stay order to allow it to exercise its garnishment rights under s. 317(3) of the *ETA*. Mr. Justice Barclay held that despite the fact that s. 11 of the *CCAA* does not mention the garnishment provision of the *ETA* (while mentioning similar provisions in other federal statutes), it was nevertheless intended by Parliament that an order under s. 11 of the *CCAA* can stay the enforcement rights of the Crown under s. 317(3) of the *ETA*. Century Services particularly relies on the following paragraph from *Points North*:

> [14] I agree with counsel for the respondents that there is no actual conflict as an order under s. 11 merely suspends the Crown's right under s. 317 of the *Excise Tax Act* as the Court deems necessary in order to allow the debtor to submit a proposal. The Crown's rights are not taken away, they are merely suspended. If the proposal is rejected by the creditors or the stay of proceedings is lifted, the Crown is then in a position to exercise its full rights under s. 317.

30 I do not quarrel with the proposition that an order under s. 11 of the *CCAA* can stay the enforcement rights of the Crown. However, when the restructuring efforts have come to an unsuccessful end, the Crown is then in a position to exercise its rights under the **deemed trust**. In addition, the s. 11 stay powers do not permit the court to authorize a breach of the **deemed trust** for the benefit of another creditor.

31 The facts in *Ivaco* do have some similarity to the case at bar. The debtor company was not able to restructure under the *CCAA* and its assets were sold. Two secured creditors brought motions to have the *CCAA* stay lifted so that they could petition the debtor company into bankruptcy. The Ontario Superintendent of Financial Services made a concurrent motion for an order that part of the sale proceeds be paid to satisfy unpaid **pension** contributions which

were deemed by s. 57 of the ***Pension** Benefits Act*, R.S.O. 1990, c. P.8, to be held in trust for the employees.

32 The Ontario Court of Appeal upheld the decision of the motions judge dismissing the Superintendent's application and allowing the bankruptcy petitions to proceed. The court rejected the Superintendent's arguments that the motions judge was required to order the segregation of the amount of the **deemed trusts** during the *CCAA* proceedings and that the motions judge was required in law to order that the amount of the **deemed trusts** be paid at the end of the *CCAA* proceeding but before bankruptcy.

33 In my opinion, *Ivaco* is distinguishable on a number of bases. In the case at bar, funds had previously been paid into a trust account in respect of GST, but no funds had been earmarked in *Ivaco*. Here, I have found an express trust in favour of the Crown, while the Superintendent in *Ivaco* was relying only on the **deemed trust**. The **deemed trust** under s. 57 of the ***Pension** Benefits Act* is not as strong as the **deemed trust** under s. 222 of the *ETA* in several respects. Section 57 does not specify any property of the debtor company to be held in trust but, rather, s. 57(3) provides that the administrator of the **pension** plan has a lien and charge on the assets of the debtor company. Also, s. 57 does not contain "notwithstanding" language or a requirement similar to the one in s. 222(3) that "proceeds of the property shall be paid to the Receiver General in priority to all security interests".

34 I find of interest one of the comments made by Mr. Justice Laskin in rejecting the Superintendent's second argument, where he said the following:

> [60] The CCAA itself did not require the motions judge to execute the **deemed trusts**. The Superintendent cannot point to any section of the statute where a legal obligation to order payment of the past service contributions can be found. Moreover, in my view, absent an agreement, I doubt that the CCAA even authorized the motions judge to order this payment. Once restructuring was not possible and the CCAA proceedings were spent, as the motions judge found and all parties acknowledged, I question whether the court had any authority to order a distribution of the sale proceeds. See for example *Re United Maritime Fishermen Co-op* (1988), 68 C.B.R. (N.S.) 170 (N.B. Q.B.) at 173.

In the context of the present case, the chambers judge did have authority to order the funds to be paid out of the Monitor's trust account because they were paid into the trust account pending further order of the court. It was clearly contemplated that there would be an order in the *CCAA* proceedings directing the payment of the funds out of the trust account.

35 Mr. Justice Laskin's comments are of interest because he questioned whether the motions judge had any authority to make further orders once restructuring was not possible and the *CCAA* proceedings were spent. In the case at bar, once restructuring possibilities had been exhausted and the *CCAA* proceedings were spent, there was no reason to prevent the Crown from exercising its rights in relation to the funds being held in trust. The distinction in this regard between *Ivaco* and this case is that the motions judge in *Ivaco* was being asked to execute the **deemed trusts**, while the chambers judge in this case was simply being asked to release monies that were being held in a trust account in respect of GST.

36 The final point I wish to address is Century Services' argument that public policy favours its position because insolvent companies should be encouraged to attempt to restructure rather than to file for bankruptcy. Century Services relies on the following two sentences from *Ivaco*:

> [64] ... Were it otherwise, creditors might be tempted to forgo efforts to restructure a debtor company and instead put the company immediately into bankruptcy. That would not be a desirable result.

The chambers judge in this case appears to have agreed with this public policy argument because he stated in para. 6 of his reasons for judgment that the result of dismissing the Crown's application was no different than if the Debtor Company had filed under the *BIA* at the outset.

37 I do not dispute that there are valid policy reasons for encouraging insolvent companies to attempt to restructure their affairs so that their business can continue with as little disruption to employees and other stakeholders as possible. It is appropriate for the courts to take such policy considerations into account, but only if it is in connection with a matter that has not been considered by Parliament. Here, Parliament must be taken to have weighed policy considerations when it enacted the amendments to the *CCAA* and *ETA* described above. As Mr. Justice MacPherson observed at para. 43 of *Ottawa Senators*, it is inconceivable that Parliament would specifically identify the *BIA* as an exception when enacting the current version of s. 222(3) of the *ETA* without considering the *CCAA* as a possible second exception. I also make the observation that the 1992 set of amendments to the *BIA* enabled proposals to be binding on secured creditors and, while there is more flexibility under the *CCAA*, it is possible for an insolvent company to attempt to restructure under the auspices of the *BIA*.

38 For these reasons, I would allow the appeal and order that the funds paid into the trust account of the Monitor, together with interest earned thereon, be paid to the Receiver General.

***Newbury J.A.*:**

I agree.

***D. Smith J.A.*:**

I agree.

Appeal allowed.

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IN THE MATTER OF the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 as amended AND IN THE MATTER of a Plan of Compromise or Arrangement of INDALEX LIMITED, INDALEX HOLDINGS (B.C.) LTD., 6326765 CANADA INC. and NOVAR INC.

Court File No. CV-09-8122-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
Proceeding commenced at TORONTO

RESPONDING FACTUM BOOK OF AUTHORITIES OF THE UNITED STEELWORKERS

(MOTION RETURNABLE AUGUST 28, 2009)

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