Court File No. CV-12-9667-00-CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SINO-FOREST CORPORATION

Applicant

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

BOOK OF AUTHORITIES OF THE RESPONDENT

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ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.

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 AND ARRANGEMENT INVOLVING METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS II CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS III CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS V CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS XI CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS XII CORP., 4446372 CANADA INC. AND 6932819 CANADA INC., TRUSTEES OF THE CONDUITS LISTED IN SCHEDULE "A" HERETO

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Ontario Court of Appeal

J.I. Laskin, E.A. Cronk, R.A. Blair JJ.A.

Heard: June 25-26, 2008
Judgment: August 18, 2008[FN*]
Docket: CA C48969

Proceedings: affirming *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 2008 CarswellOnt 3523, 43 C.B.R. (5th) 269 (Ont. S.C.J. [Commercial List])

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s. 182 — referred to

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s. 192 — referred to

Code civil du Québec, L.Q. 1991, c. 64

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

Generally — referred to

s. 4 — considered

s. 5.1 [en. 1997, c. 12, s. 122] — considered

s. 6 — considered

Constitution Act, 1867, (U.K.), 30 & 31 Vict., c. 3, reprinted R.S.C. 1985, App. II, No. 5

s. 91 ¶ 21 — referred to

s. 92 — referred to

s. 92 ¶ 13 — referred to

Words and phrases considered:

arrangement

"Arrangement" is broader than "compromise" and would appear to include any scheme for reorganizing the affairs of the debtor.

APPEAL by opponents of creditor-initiated plan from judgment reported at *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 2008 CarswellOnt 3523, 43 C.B.R. (5th) 269, 47 B.L.R. (4th) 74 (Ont. S.C.J. [Commercial List]), granting application for approval of plan.

***R.A. Blair J.A.*:**

A. Introduction

1 In August 2007 a liquidity crisis suddenly threatened the Canadian market in Asset Backed Commercial Paper ("ABCP"). The crisis was triggered by a loss of confidence amongst investors stemming from the news of widespread defaults on U.S. sub-prime mortgages. The loss of confidence placed the Canadian financial market at risk generally and was reflective of an economic volatility worldwide.

2 By agreement amongst the major Canadian participants, the $32 billion Canadian market in third-party ABCP was frozen on August 13, 2007 pending an attempt to resolve the crisis through a restructuring of that market. The Pan-Canadian Investors Committee, chaired by Purdy Crawford, C.C., Q.C., was formed and ultimately put forward the creditor-initiated Plan of Compromise and Arrangement that forms the subject-matter of these proceedings. The Plan was sanctioned by Colin L. Campbell J. on June 5, 2008.

3 Certain creditors who opposed the Plan seek leave to appeal and, if leave is granted, appeal from that decision. They raise an important point regarding the permissible scope of a restructuring under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 as amended ("CCAA"): can the court sanction a Plan that calls for creditors to provide releases to third parties who are themselves solvent and not creditors of the debtor company? They also argue that, if the answer to this question is yes, the application judge erred in holding that this Plan, with its particular releases (which bar some claims even in fraud), was fair and reasonable and therefore in sanctioning it under the CCAA.

Leave to Appeal

4 Because of the particular circumstances and urgency of these proceedings, the court agreed to collapse an oral hearing for leave to appeal with the hearing of the appeal itself. At the outset of argument we encouraged counsel to combine their submissions on both matters.

5 The proposed appeal raises issues of considerable importance to restructuring proceedings under the CCAA Canada-wide. There are serious and arguable grounds of appeal and — given the expedited time-table — the appeal will not unduly delay the progress of the proceedings. I am satisfied that the criteria for granting leave to appeal in CCAA proceedings, set out in such cases as *Cineplex Odeon Corp., Re* (2001), 24 C.B.R. (4th) 201 (Ont. C.A.), and *Country Style Food Services Inc., Re* (2002), 158 O.A.C. 30 (Ont. C.A. [In Chambers]), are met. I would grant leave to appeal.

Appeal

6 For the reasons that follow, however, I would dismiss the appeal.

B. Facts

The Parties

7 The appellants are holders of ABCP Notes who oppose the Plan. They do so principally on the basis that it requires them to grant releases to third party financial institutions against whom they say they have claims for relief arising out of their purchase of ABCP Notes. Amongst them are an airline, a tour operator, a mining company, a wireless provider, a pharmaceuticals retailer, and several holding companies and energy companies.

8 Each of the appellants has large sums invested in ABCP — in some cases, hundreds of millions of dollars. Nonetheless, the collective holdings of the appellants — slightly over $1 billion — represent only a small fraction of the more than $32 billion of ABCP involved in the restructuring.

9 The lead respondent is the Pan-Canadian Investors Committee which was responsible for the creation and negotiation of the Plan on behalf of the creditors. Other respondents include various major international financial institutions, the five largest Canadian banks, several trust companies, and some smaller holders of ABCP product. They participated in the market in a number of different ways.

The ABCP Market

10 Asset Backed Commercial Paper is a sophisticated and hitherto well-accepted financial instrument. It is primarily a form of short-term investment — usually 30 to 90 days — typically with a low interest yield only slightly better than that available through other short-term paper from a government or bank. It is said to be "asset backed" because the cash that is used to purchase an ABCP Note is converted into a portfolio of financial assets or other asset interests that in turn provide security for the repayment of the notes.

11 ABCP was often presented by those selling it as a safe investment, somewhat like a guaranteed investment certificate.

12 The Canadian market for ABCP is significant and administratively complex. As of August 2007, investors had placed over $116 billion in Canadian ABCP. Investors range from individual pensioners to large institutional bodies. On the selling and distribution end, numerous players are involved, including chartered banks, investment houses and other financial institutions. Some of these players participated in multiple ways. The Plan in this proceeding relates to approximately $32 billion of non-bank sponsored ABCP the restructuring of which is considered essential to the preservation of the Canadian ABCP market.

13 As I understand it, prior to August 2007 when it was frozen, the ABCP market worked as follows.

14 Various corporations (the "Sponsors") would arrange for entities they control ("Conduits") to make ABCP Notes available to be sold to investors through "Dealers" (banks and other investment dealers). Typically, ABCP was issued by series and sometimes by classes within a series.

15 The cash from the purchase of the ABCP Notes was used to purchase assets which were held by trustees of the Conduits ("Issuer Trustees") and which stood as security for repayment of the notes. Financial institutions that sold or provided the Conduits with the assets that secured the ABCP are known as "Asset Providers". To help ensure that investors would be able to redeem their notes, "Liquidity Providers" agreed to provide funds that could be drawn upon to meet the demands of maturing ABCP Notes in certain circumstances. Most Asset Providers were also Liquidity Providers. Many of these banks and financial institutions were also holders of ABCP Notes ("Noteholders"). The Asset and Liquidity Providers held first charges on the assets.

16 When the market was working well, cash from the purchase of new ABCP Notes was also used to pay off maturing ABCP Notes; alternatively, Noteholders simply rolled their maturing notes over into new ones. As I will explain, however, there was a potential underlying predicament with this scheme.

The Liquidity Crisis

17 The types of assets and asset interests acquired to "back" the ABCP Notes are varied and complex. They were generally long-term assets such as residential mortgages, credit card receivables, auto loans, cash collateralized debt obligations and derivative investments such as credit default swaps. Their particular characteristics do not matter for the purpose of this appeal, but they shared a common feature that proved to be the Achilles heel of the ABCP market: because of their long-term nature there was an inherent timing mismatch between the cash they generated and the cash needed to repay maturing ABCP Notes.

18 When uncertainty began to spread through the ABCP marketplace in the summer of 2007, investors stopped buying the ABCP product and existing Noteholders ceased to roll over their maturing notes. There was no cash to redeem those notes. Although calls were made on the Liquidity Providers for payment, most of the Liquidity Providers declined to fund the redemption of the notes, arguing that the conditions for liquidity funding had not been met in the circumstances. Hence the "liquidity crisis" in the ABCP market.

19 The crisis was fuelled largely by a lack of transparency in the ABCP scheme. Investors could not tell what assets were backing their notes — partly because the ABCP Notes were often sold before or at the same time as the assets backing them were acquired; partly because of the sheer complexity of certain of the underlying assets; and partly because of assertions of confidentiality by those involved with the assets. As fears arising from the spreading U.S. sub-prime mortgage crisis mushroomed, investors became increasingly concerned that their ABCP Notes may be supported by those crumbling assets. For the reasons outlined above, however, they were unable to redeem their maturing ABCP Notes.

The Montreal Protocol

20 The liquidity crisis could have triggered a wholesale liquidation of the assets, at depressed prices. But it did not. During the week of August 13, 2007, the ABCP market in Canada froze — the result of a standstill arrangement orchestrated on the heels of the crisis by numerous market participants, including Asset Providers, Liquidity Providers, Noteholders and other financial industry representatives. Under the standstill agreement — known as the Montréal Protocol — the parties committed to restructuring the ABCP market with a view, as much as possible, to preserving the value of the assets and of the notes.

21 The work of implementing the restructuring fell to the Pan-Canadian Investors Committee, an applicant in the proceeding and respondent in the appeal. The Committee is composed of 17 financial and investment institutions, including chartered banks, credit unions, a pension board, a Crown corporation, and a university board of governors. All 17 members are themselves Noteholders; three of them also participated in the ABCP market in other capacities as well. Between them, they hold about two thirds of the $32 billion of ABCP sought to be restructured in these proceedings.

22 Mr. Crawford was named the Committee's chair. He thus had a unique vantage point on the work of the Committee and the restructuring process as a whole. His lengthy affidavit strongly informed the application judge's understanding of the factual context, and our own. He was not cross-examined and his evidence is unchallenged.

23 Beginning in September 2007, the Committee worked to craft a plan that would preserve the value of the notes and assets, satisfy the various stakeholders to the extent possible, and restore confidence in an important segment of the Canadian financial marketplace. In March 2008, it and the other applicants sought CCAA protection for the ABCP debtors and the approval of a Plan that had been pre-negotiated with some, but not all, of those affected by the misfortunes in the Canadian ABCP market.

The Plan

a) Plan Overview

24 Although the ABCP market involves many different players and kinds of assets, each with their own challenges, the committee opted for a single plan. In Mr. Crawford's words, "all of the ABCP suffers from common problems that are best addressed by a common solution." The Plan the Committee developed is highly complex and involves many parties. In its essence, the Plan would convert the Noteholders' paper — which has been frozen and therefore effectively worthless for many months — into new, long-term notes that would trade freely, but with a discounted face value. The hope is that a strong secondary market for the notes will emerge in the long run.

25 The Plan aims to improve transparency by providing investors with detailed information about the assets supporting their ABCP Notes. It also addresses the timing mismatch between the notes and the assets by adjusting the maturity provisions and interest rates on the new notes. Further, the Plan adjusts some of the underlying credit default swap contracts by increasing the thresholds for default triggering events; in this way, the likelihood of a forced liquidation flowing from the credit default swap holder's prior security is reduced and, in turn, the risk for ABCP investors is decreased.

26 Under the Plan, the vast majority of the assets underlying ABCP would be pooled into two master asset vehicles (MAV1 and MAV2). The pooling is designed to increase the collateral available and thus make the notes more secure.

27 The Plan does not apply to investors holding less than $1 million of notes. However, certain Dealers have agreed to buy the ABCP of those of their customers holding less than the $1-million threshold, and to extend financial assistance to these customers. Principal among these Dealers are National Bank and Canaccord, two of the respondent financial institutions the appellants most object to releasing. The application judge found that these developments appeared to be designed to secure votes in favour of the Plan by various Noteholders, and were apparently successful in doing so. If the Plan is approved, they also provide considerable relief to the many small investors who find themselves unwittingly caught in the ABDP collapse.

b) The Releases

28 This appeal focuses on one specific aspect of the Plan: the comprehensive series of releases of third parties provided for in Article 10.

29 The Plan calls for the release of Canadian banks, Dealers, Noteholders, Asset Providers, Issuer Trustees, Liquidity Providers, and other market participants — in Mr. Crawford's words, "virtually all participants in the Canadian ABCP market" — from any liability associated with ABCP, with the exception of certain narrow claims relating to fraud. For instance, under the Plan as approved, creditors will have to give up their claims against the Dealers who sold them their ABCP Notes, including challenges to the way the Dealers characterized

the ABCP and provided (or did not provide) information about the ABCP. The claims against the proposed defendants are mainly in tort: negligence, misrepresentation, negligent misrepresentation, failure to act prudently as a dealer/advisor, acting in conflict of interest, and in a few cases fraud or potential fraud. There are also allegations of breach of fiduciary duty and claims for other equitable relief.

30 The application judge found that, in general, the claims for damages include the face value of the Notes, plus interest and additional penalties and damages.

31 The releases, in effect, are part of a *quid pro quo*. Generally speaking, they are designed to compensate various participants in the market for the contributions they would make to the restructuring. Those contributions under the Plan include the requirements that:

> a) Asset Providers assume an increased risk in their credit default swap contracts, disclose certain proprietary information in relation to the assets, and provide below-cost financing for margin funding facilities that are designed to make the notes more secure;
>
> b) Sponsors — who in addition have cooperated with the Investors' Committee throughout the process, including by sharing certain proprietary information — give up their existing contracts;
>
> c) The Canadian banks provide below-cost financing for the margin funding facility and,
>
> d) Other parties make other contributions under the Plan.

32 According to Mr. Crawford's affidavit, the releases are part of the Plan "because certain key participants, whose participation is vital to the restructuring, have made comprehensive releases a condition for their participation."

The CCAA Proceedings to Date

33 On March 17, 2008 the applicants sought and obtained an Initial Order under the CCAA staying any proceedings relating to the ABCP crisis and providing for a meeting of the Noteholders to vote on the proposed Plan. The meeting was held on April 25th. The vote was overwhelmingly in support of the Plan — 96% of the Noteholders voted in favour. At the instance of certain Noteholders, and as requested by the application judge (who has supervised the proceedings from the outset), the Monitor broke down the voting results according to those Noteholders who had worked on or with the Investors' Committee to develop the Plan and those Noteholders who had not. Re-calculated on this basis the results remained firmly in favour of the proposed Plan — 99% of those connected with the development of the Plan voted positively, as did 80% of those Noteholders who had not been involved in its formulation.

34 The vote thus provided the Plan with the "double majority" approval — a majority of creditors representing two-thirds in value of the claims — required under s. 6 of the CCAA.

35 Following the successful vote, the applicants sought court approval of the Plan under s. 6. Hearings were held on May 12 and 13. On May 16, the application judge issued a brief endorsement in which he concluded that he did not have sufficient facts to decide whether all the releases proposed in the Plan were authorized by the CCAA. While the application judge was prepared to approve the releases of negligence claims, he was not prepared at that point to sanction the release of fraud claims. Noting the urgency of the situation and the serious

consequences that would result from the Plan's failure, the application judge nevertheless directed the parties back to the bargaining table to try to work out a claims process for addressing legitimate claims of fraud.

36 The result of this renegotiation was a "fraud carve-out" — an amendment to the Plan excluding certain fraud claims from the Plan's releases. The carve-out did not encompass all possible claims of fraud, however. It was limited in three key respects. First, it applied only to claims against ABCP Dealers. Secondly, it applied only to cases involving an express fraudulent misrepresentation made with the intention to induce purchase and in circumstances where the person making the representation knew it to be false. Thirdly, the carve-out limited available damages to the value of the notes, minus any funds distributed as part of the Plan. The appellants argue vigorously that such a limited release respecting fraud claims is unacceptable and should not have been sanctioned by the application judge.

37 A second sanction hearing — this time involving the amended Plan (with the fraud carve-out) — was held on June 3, 2008. Two days later, Campbell J. released his reasons for decision, approving and sanctioning the Plan on the basis both that he had jurisdiction to sanction a Plan calling for third-party releases and that the Plan including the third-party releases in question here was fair and reasonable.

38 The appellants attack both of these determinations.

C. Law and Analysis

39 There are two principal questions for determination on this appeal:

1) As a matter of law, may a CCAA plan contain a release of claims against anyone other than the debtor company or its directors?

2) If the answer to that question is yes, did the application judge err in the exercise of his discretion to sanction the Plan as fair and reasonable given the nature of the releases called for under it?

(1) Legal Authority for the Releases

40 The standard of review on this first issue — whether, as a matter of law, a CCAA plan may contain third-party releases — is correctness.

41 The appellants submit that a court has no jurisdiction or legal authority under the CCAA to sanction a plan that imposes an obligation on creditors to give releases to third parties other than the directors of the debtor company.[FN1] The requirement that objecting creditors release claims against third parties is illegal, they contend, because:

a) on a proper interpretation, the CCAA does not permit such releases;

b) the court is not entitled to "fill in the gaps" in the CCAA or rely upon its inherent jurisdiction to create such authority because to do so would be contrary to the principle that Parliament did not intend to interfere with private property rights or rights of action in the absence of clear statutory language to that effect;

c) the releases constitute an unconstitutional confiscation of private property that is within the exclusive

plication judge did.

47 The Supreme Court of Canada has affirmed generally — and in the insolvency context particularly — that remedial statutes are to be interpreted liberally and in accordance with Professor Driedger's modern principle of statutory interpretation. Driedger advocated that "the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament": *Rizzo & Rizzo Shoes Ltd., Re*, [1998] 1 S.C.R. 27 (S.C.C.) at para. 21, quoting E.A. Driedger, *Construction of Statutes*, 2nd ed. (Toronto: Butterworths, 1983); *Bell ExpressVu Ltd. Partnership v. Rex*, [2002] 2 S.C.R. 559 (S.C.C.) at para. 26.

48 More broadly, I believe that the proper approach to the judicial interpretation and application of statutes — particularly those like the CCAA that are skeletal in nature — is succinctly and accurately summarized by Jackson and Sarra in their recent article, *supra*, at p. 56:

> The exercise of a statutory authority requires the statute to be construed. The plain meaning or textualist approach has given way to a search for the object and goals of the statute and the intentionalist approach. This latter approach makes use of the purposive approach and the mischief rule, including its codification under interpretation statutes that every enactment is deemed remedial, and is to be given such fair, large and liberal construction and interpretation as best ensures the attainment of its objects. This latter approach advocates reading the statute as a whole and being mindful of Driedger's "one principle", that the words of the Act are to be read in their entire context, in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament. It is important that courts first interpret the statute before them and exercise their authority pursuant to the statute, before reaching for other tools in the judicial toolbox. Statutory interpretation using the principles articulated above leaves room for gap-filling in the common law provinces and a consideration of purpose in *Québec* as a manifestation of the judge's overall task of statutory interpretation. Finally, the jurisprudence in relation to statutory interpretation demonstrates the fluidity inherent in the judge's task in seeking the objects of the statute and the intention of the legislature.

49 I adopt these principles.

50 The remedial purpose of the CCAA — as its title affirms — is to facilitate compromises or arrangements between an insolvent debtor company and its creditors. In *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311 (B.C. C.A.) at 318, Gibbs J.A. summarized very concisely the purpose, object and scheme of the Act:

> Almost inevitably, liquidation destroyed the shareholders' investment, yielded little by way of recovery to the creditors, and exacerbated the social evil of devastating levels of unemployment. The government of the day sought, through the C.C.A.A., to create a regime whereby the principals of the company and the creditors could be brought together under the supervision of the court to attempt a reorganization or compromise or arrangement under which the company could continue in business.

51 The CCAA was enacted in 1933 and was necessary — as the then Secretary of State noted in introducing the Bill on First Reading — "because of the prevailing commercial and industrial depression" and the need to alleviate the effects of business bankruptcies in that context: see the statement of the Hon. C.H. Cahan, Secretary of State, *House of Commons Debates (Hansard)* (April 20, 1933) at 4091. One of the greatest effects of that Depression was what Gibbs J.A. described as "the social evil of devastating levels of unemployment". Since then,

domain of the provinces under s. 92 of the *Constitution Act*, 1867;

d) the releases are invalid under Quebec rules of public order; and because

e) the prevailing jurisprudence supports these conclusions.

42 I would not give effect to any of these submissions.

Interpretation, "Gap Filling" and Inherent Jurisdiction

43 On a proper interpretation, in my view, the CCAA permits the inclusion of third party releases in a plan of compromise or arrangement to be sanctioned by the court where those releases are reasonably connected to the proposed restructuring. I am led to this conclusion by a combination of (a) the open-ended, flexible character of the CCAA itself, (b) the broad nature of the term "compromise or arrangement" as used in the Act, and (c) the express statutory effect of the "double-majority" vote and court sanction which render the plan binding on *all* creditors, including those unwilling to accept certain portions of it. The first of these signals a flexible approach to the application of the Act in new and evolving situations, an active judicial role in its application and interpretation, and a liberal approach to that interpretation. The second provides the entrée to negotiations between the parties affected in the restructuring and furnishes them with the ability to apply the broad scope of their ingenuity in fashioning the proposal. The latter afford necessary protection to unwilling creditors who may be deprived of certain of their civil and property rights as a result of the process.

44 The CCAA is skeletal in nature. It does not contain a comprehensive code that lays out all that is permitted or barred. Judges must therefore play a role in fleshing out the details of the statutory scheme. The scope of the Act and the powers of the court under it are not limitless. It is beyond controversy, however, that the CCAA is remedial legislation to be liberally construed in accordance with the modern purposive approach to statutory interpretation. It is designed to be a flexible instrument and it is that very flexibility which gives the Act its efficacy: *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]). As Farley J. noted in *Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Gen. Div. [Commercial List]), at 111, "[t]he history of CCAA law has been an evolution of judicial interpretation."

45 Much has been said, however, about the "evolution of judicial interpretation" and there is some controversy over both the source and scope of that authority. Is the source of the court's authority statutory, discerned solely through application of the principles of statutory interpretation, for example? Or does it rest in the court's ability to "fill in the gaps" in legislation? Or in the court's inherent jurisdiction?

46 These issues have recently been canvassed by the Honourable Georgina R. Jackson and Dr. Janis Sarra in their publication "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters,"[FN2] and there was considerable argument on these issues before the application judge and before us. While I generally agree with the authors' suggestion that the courts should adopt a hierarchical approach in their resort to these interpretive tools — statutory interpretation, gap-filling, discretion and inherent jurisdiction — it is not necessary in my view to go beyond the general principles of statutory interpretation to resolve the issues on this appeal. Because I am satisfied that it is implicit in the language of the CCAA itself that the court has authority to sanction plans incorporating third-party releases that are reasonably related to the proposed restructuring, there is no "gap-filling" to be done and no need to fall back on inherent jurisdiction. In this respect, I take a somewhat different approach than the ap-

courts have recognized that the Act has a broader dimension than simply the direct relations between the debtor company and its creditors and that this broader public dimension must be weighed in the balance together with the interests of those most directly affected: see, for example, *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 O.R. (3d) 289 (Ont. C.A.), *per* Doherty J.A. in dissent; *Skydome Corp., Re* (1998), 16 C.B.R. (4th) 125 (Ont. Gen. Div. [Commercial List]); *Anvil Range Mining Corp., Re* (1998), 7 C.B.R. (4th) 51 (Ont. Gen. Div. [Commercial List]).

52 In this respect, I agree with the following statement of Doherty J.A. in *Elan*, *supra*, at pp. 306-307:

> . . . [T]he Act was designed to serve a "broad constituency of investors, creditors and employees".[FN3] Because of that "broad constituency" the court must, when considering applications brought under the Act, *have regard not only to the individuals and organizations directly affected by the application, but also to the wider public interest*. [Emphasis added.]

Application of the Principles of Interpretation

53 An interpretation of the CCAA that recognizes its broader socio-economic purposes and objects is apt in this case. As the application judge pointed out, the restructuring underpins the financial viability of the Canadian ABCP market itself.

54 The appellants argue that the application judge erred in taking this approach and in treating the Plan and the proceedings as an attempt to restructure a financial market (the ABCP market) rather than simply the affairs between the debtor corporations who caused the ABCP Notes to be issued and their creditors. The Act is designed, they say, only to effect reorganizations between a corporate debtor and its creditors and not to attempt to restructure entire marketplaces.

55 This perspective is flawed in at least two respects, however, in my opinion. First, it reflects a view of the purpose and objects of the CCAA that is too narrow. Secondly, it overlooks the reality of the ABCP marketplace and the context of the restructuring in question here. It may be true that, in their capacity as ABCP *Dealers*, the releasee financial institutions are "third-parties" to the restructuring in the sense that they are not creditors of the debtor corporations. However, in their capacities as *Asset Providers* and *Liquidity Providers*, they are not only creditors but they are prior secured creditors to the Noteholders. Furthermore — as the application judge found — in these latter capacities they are making significant contributions to the restructuring by "foregoing immediate rights to assets and ... providing real and tangible input for the preservation and enhancement of the Notes" (para. 76). In this context, therefore, the application judge's remark at para. 50 that the restructuring "involves the commitment and participation of all parties" in the ABCP market makes sense, as do his earlier comments at paras. 48-49:

> Given the nature of the ABCP market and all of its participants, it is more appropriate to consider all Noteholders as claimants and the object of the Plan to restore liquidity to the assets being the Notes themselves. The restoration of the liquidity of the market necessitates the participation (including more tangible contribution by many) of all Noteholders.
>
> In these circumstances, *it is unduly technical to classify the Issuer Trustees as debtors and the claims of the Noteholders as between themselves and others as being those of third party creditors*, although I recognize that the restructuring structure of the CCAA requires the corporations as the vehicles for restructuring. [Emphasis added.]

56 The application judge did observe that "[t]he insolvency is of the ABCP market itself, the restructuring is that of the market for such paper ..." (para. 50). He did so, however, to point out the uniqueness of the Plan before him and its industry-wide significance and not to suggest that he need have no regard to the provisions of the CCAA permitting a restructuring as between debtor and creditors. His focus was on *the effect* of the restructuring, a perfectly permissible perspective, given the broad purpose and objects of the Act. This is apparent from his later references. For example, in balancing the arguments against approving releases that might include aspects of fraud, he responded that "what is at issue is a liquidity crisis that affects the ABCP market in Canada" (para. 125). In addition, in his reasoning on the fair-and-reasonable issue, he stated at para. 142: "Apart from the Plan itself, there is a need to restore confidence in the financial system in Canada and this Plan is a legitimate use of the CCAA to accomplish that goal."

57 I agree. I see no error on the part of the application judge in approaching the fairness assessment or the interpretation issue with these considerations in mind. They provide the context in which the purpose, objects and scheme of the CCAA are to be considered.

The Statutory Wording

58 Keeping in mind the interpretive principles outlined above, I turn now to a consideration of the provisions of the CCAA. Where in the words of the statute is the court clothed with authority to approve a plan incorporating a requirement for third-party releases? As summarized earlier, the answer to that question, in my view, is to be found in:

> a) the skeletal nature of the CCAA;
>
> b) Parliament's reliance upon the broad notions of "compromise" and "arrangement" to establish the framework within which the parties may work to put forward a restructuring plan; and in
>
> c) the creation of the statutory mechanism binding all creditors in classes to the compromise or arrangement once it has surpassed the high "double majority" voting threshold and obtained court sanction as "fair and reasonable".

Therein lies the expression of Parliament's intention to permit the parties to negotiate and vote on, and the court to sanction, third-party releases relating to a restructuring.

59 Sections 4 and 6 of the CCAA state:

> 4. Where a compromise or an arrangement is proposed between a debtor company and its unsecured creditors or any class of them, the court may, on the application in a summary way of the company, of any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors, and, if the court so determines, of the shareholders of the company, to be summoned in such manner as the court directs.
>
> 6. Where a majority in number representing two-thirds in value of the creditors, or class of creditors, as the case may be, present and voting either in person or by proxy at the meeting or meetings thereof respectively held pursuant to sections 4 and 5, or either of those sections, agree to any compromise or arrangement either as proposed or as altered or modified at the meeting or meetings, the compromise or arrangement may be sanctioned by the court, and if so sanctioned is binding

(a) on all the creditors or the class of creditors, as the case may be, and on any trustee for any such class of creditors, whether secured or unsecured, as the case may be, and on the company; and

(b) in the case of a company that has made an authorized assignment or against which a bankruptcy order has been made under the *Bankruptcy and Insolvency Act* or is in the course of being wound up under the *Winding-up and Restructuring Act*, on the trustee in bankruptcy or liquidator and contributories of the company.

Compromise or Arrangement

60 While there may be little practical distinction between "compromise" and "arrangement" in many respects, the two are not necessarily the same. "Arrangement" is broader than "compromise" and would appear to include any scheme for reorganizing the affairs of the debtor: Houlden & Morawetz, *Bankruptcy and Insolvency Law of Canada*, loose-leaf, 3rd ed., vol. 4 (Toronto: Thomson Carswell) at 10A-12.2, N§10. It has been said to be "a very wide and indefinite [word]": *Reference re Refund of Dues Paid under s.47 (f) of Timber Regulations in the Western Provinces*, [1935] A.C. 184 (Canada P.C.) at 197, affirming S.C.C. [1933] S.C.R. 616 (S.C.C.). See also, *Guardian Assurance Co., Re*, [1917] 1 Ch. 431 (Eng. C.A.) at 448, 450; *T&N Ltd., Re* (2006), [2007] 1 All E.R. 851 (Eng. Ch. Div.).

61 The CCAA is a sketch, an outline, a supporting framework for the resolution of corporate insolvencies in the public interest. Parliament wisely avoided attempting to anticipate the myriad of business deals that could evolve from the fertile and creative minds of negotiators restructuring their financial affairs. It left the shape and details of those deals to be worked out within the framework of the comprehensive and flexible concepts of a "compromise" and "arrangement." I see no reason why a release in favour of a third party, negotiated as part of a package between a debtor and creditor and reasonably relating to the proposed restructuring cannot fall within that framework.

62 A proposal under the *Bankruptcy and Insolvency Act*, R.S., 1985, c. B-3 (the "BIA") is a contract: *Employers' Liability Assurance Corp. v. Ideal Petroleum (1959) Ltd.*, [1978] 1 S.C.R. 230 (S.C.C.) at 239; *Society of Composers, Authors & Music Publishers of Canada v. Armitage* (2000), 50 O.R. (3d) 688 (Ont. C.A.) at para. 11. In my view, a compromise or arrangement under the CCAA is directly analogous to a proposal for these purposes, and therefore is to be treated as a contract between the debtor and its creditors. Consequently, parties are entitled to put anything into such a plan that could lawfully be incorporated into any contract. See *Air Canada, Re* (2004), 2 C.B.R. (5th) 4 (Ont. S.C.J. [Commercial List]) at para. 6; *Olympia & York Developments Ltd. v. Royal Trust Co.* (1993), 12 O.R. (3d) 500 (Ont. Gen. Div.) at 518.

63 There is nothing to prevent a debtor and a creditor from including in a contract between them a term providing that the creditor release a third party. The term is binding as between the debtor and creditor. In the CCAA context, therefore, a plan of compromise or arrangement may propose that creditors agree to compromise claims against the debtor and to release third parties, just as any debtor and creditor might agree to such a term in a contract between them. Once the statutory mechanism regarding voter approval and court sanctioning has been complied with, the plan — including the provision for releases — becomes binding on all creditors (including the dissenting minority).

64 *T&N Ltd., Re*, *supra*, is instructive in this regard. It is a rare example of a court focussing on and examining the meaning and breadth of the term "arrangement". T&N and its associated companies were engaged in the

manufacture, distribution and sale of asbestos-containing products. They became the subject of many claims by former employees, who had been exposed to asbestos dust in the course of their employment, and their dependents. The T&N companies applied for protection under s. 425 of the U.K. *Companies Act 1985*, a provision virtually identical to the scheme of the CCAA — including the concepts of compromise or arrangement.[FN4]

65 T&N carried employers' liability insurance. However, the employers' liability insurers (the "EL insurers") denied coverage. This issue was litigated and ultimately resolved through the establishment of a multi-million pound fund against which the employees and their dependants (the "EL claimants") would assert their claims. In return, T&N's former employees and dependants (the "EL claimants") agreed to forego any further claims against the EL insurers. This settlement was incorporated into the plan of compromise and arrangement between the T&N companies and the EL claimants that was voted on and put forward for court sanction.

66 Certain creditors argued that the court could not sanction the plan because it did not constitute a "compromise or arrangement" between T&N and the EL claimants since it did not purport to affect rights as between them but only the EL claimants' rights against the EL insurers. The Court rejected this argument. Richards J. adopted previous jurisprudence — cited earlier in these reasons — to the effect that the word "arrangement" has a very broad meaning and that, while both a compromise and an arrangement involve some "give and take", an arrangement need not involve a compromise or be confined to a case of dispute or difficulty (paras. 46-51). He referred to what would be the equivalent of a solvent arrangement under Canadian corporate legislation as an example.[FN5] Finally, he pointed out that the compromised rights of the EL claimants against the EL insurers were not unconnected with the EL claimants' rights against the T&N companies; the scheme of arrangement involving the EL insurers was "an integral part of a single proposal affecting all the parties" (para. 52). He concluded his reasoning with these observations (para. 53):

> In my judgment it is not a necessary element of an arrangement for the purposes of s 425 of the 1985 Act that it should alter the rights existing between the company and the creditors or members with whom it is made. No doubt in most cases it will alter those rights. But, provided that the context and content of the scheme are such as properly to constitute an arrangement between the company and the members or creditors concerned, it will fall within s 425. It is ... neither necessary nor desirable to attempt a definition of arrangement. The legislature has not done so. To insist on an alteration of rights, or a termination of rights as in the case of schemes to effect takeovers or mergers, is to impose a restriction which is neither warranted by the statutory language nor justified by the courts' approach over many years to give the term its widest meaning. *Nor is an arrangement necessarily outside the section, because its effect is to alter the rights of creditors against another party or because such alteration could be achieved by a scheme of arrangement with that party.* [Emphasis added.]

67 I find Richard J.'s analysis helpful and persuasive. In effect, the claimants in *T&N* were being asked to release their claims against the EL insurers in exchange for a call on the fund. Here, the appellants are being required to release their claims against certain financial third parties in exchange for what is anticipated to be an improved position for all ABCP Noteholders, stemming from the contributions the financial third parties are making to the ABCP restructuring. The situations are quite comparable.

The Binding Mechanism

68 Parliament's reliance on the expansive terms "compromise" or "arrangement" does not stand alone, however. Effective insolvency restructurings would not be possible without a statutory mechanism to bind an

unwilling minority of creditors. Unanimity is frequently impossible in such situations. But the minority must be protected too. Parliament's solution to this quandary was to permit a wide range of proposals to be negotiated and put forward (the compromise or arrangement) and to bind *all* creditors by class to the terms of the plan, but to do so only where the proposal can gain the support of the requisite "double majority" of votes[FN6] *and* obtain the sanction of the court on the basis that it is fair and reasonable. In this way, the scheme of the CCAA supports the intention of Parliament to encourage a wide variety of solutions to corporate insolvencies without unjustifiably overriding the rights of dissenting creditors.

The Required Nexus

69 In keeping with this scheme and purpose, I do not suggest that any and all releases between creditors of the debtor company seeking to restructure and third parties may be made the subject of a compromise or arrangement between the debtor and its creditors. Nor do I think the fact that the releases may be "necessary" in the sense that the third parties or the debtor may refuse to proceed without them, of itself, advances the argument in favour of finding jurisdiction (although it may well be relevant in terms of the fairness and reasonableness analysis).

70 The release of the claim in question must be justified as part of the compromise or arrangement between the debtor and its creditors. In short, there must be a reasonable connection between the third party claim being compromised in the plan and the restructuring achieved by the plan to warrant inclusion of the third party release in the plan. This nexus exists here, in my view.

71 In the course of his reasons, the application judge made the following findings, all of which are amply supported on the record:

a) The parties to be released are necessary and essential to the restructuring of the debtor;

b) *The claims to be released are rationally related to the purpose of the Plan and necessary for it*;

c) The Plan cannot succeed without the releases;

d) *The parties who are to have claims against them released are contributing in a tangible and realistic way to the Plan*; and

e) The Plan will benefit not only the debtor companies but creditor Noteholders generally.

72 Here, then — as was the case in *T&N* — there is a close connection between the claims being released and the restructuring proposal. The tort claims arise out of the sale and distribution of the ABCP Notes and their collapse in value, just as do the contractual claims of the creditors against the debtor companies. The purpose of the restructuring is to stabilize and shore up the value of those notes in the long run. The third parties being released are making separate contributions to enable those results to materialize. Those contributions are identified earlier, at para. 31 of these reasons. The application judge found that the claims being released are not independent of or unrelated to the claims that the Noteholders have against the debtor companies; they are closely connected to the value of the ABCP Notes and are required for the Plan to succeed. At paras. 76-77 he said:

> [76] I do not consider that the Plan in this case involves a change in relationship among creditors "that does not directly involve the Company." Those who support the Plan and are to be released are "directly involved in the Company" in the sense that many are foregoing immediate rights to assets and are providing real and

> tangible input for the preservation and enhancement of the Notes. It would be unduly restrictive to suggest that the moving parties' claims against released parties do not involve the Company, since the claims are directly related to the value of the Notes. The value of the Notes is in this case the value of the Company.
>
> [77] This Plan, as it deals with releases, doesn't change the relationship of the creditors apart from involving the Company and its Notes.

73 I am satisfied that the wording of the CCAA — construed in light of the purpose, objects and scheme of the Act and in accordance with the modern principles of statutory interpretation — supports the court's jurisdiction and authority to sanction the Plan proposed here, including the contested third-party releases contained in it.

The Jurisprudence

74 Third party releases have become a frequent feature in Canadian restructurings since the decision of the Alberta Court of Queen's Bench in *Canadian Airlines Corp., Re* (2000), 265 A.R. 201 (Alta. Q.B.), leave to appeal refused by (2000), 266 A.R. 131 (Alta. C.A. [In Chambers]), and (2001), 293 A.R. 351 (note) (S.C.C.). In *Muscletech Research & Development Inc., Re* (2006), 25 C.B.R. (5th) 231 (Ont. S.C.J.) Justice Ground remarked (para. 8):

> [It] is not uncommon in CCAA proceedings, in the context of a plan of compromise and arrangement, to compromise claims against the Applicants and other parties against whom such claims or related claims are made.

75 We were referred to at least a dozen court-approved CCAA plans from across the country that included broad third-party releases. With the exception of *Canadian Airlines Corp., Re*, however, the releases in those restructurings — including *Muscletech Research & Development Inc., Re* — were not opposed. The appellants argue that those cases are wrongly decided, because the court simply does not have the authority to approve such releases.

76 In *Canadian Airlines Corp., Re* the releases in question were opposed, however. Paperny J. (as she then was) concluded the court had jurisdiction to approve them and her decision is said to be the well-spring of the trend towards third-party releases referred to above. Based on the foregoing analysis, I agree with her conclusion although for reasons that differ from those cited by her.

77 Justice Paperny began her analysis of the release issue with the observation at para. 87 that "[p]rior to 1997, the CCAA did not provide for compromises of claims against anyone other than the petitioning company." It will be apparent from the analysis in these reasons that I do not accept that premise, notwithstanding the decision of the Quebec Court of Appeal in *Steinberg Inc. c. Michaud*,[FN7] of which her comment may have been reflective. Paperny J.'s reference to 1997 was a reference to the amendments of that year adding s. 5.1 to the CCAA, which provides for limited releases in favour of directors. Given the limited scope of s. 5.1, Justice Paperny was thus faced with the argument — dealt with later in these reasons — that Parliament must not have intended to extend the authority to approve third-party releases beyond the scope of this section. She chose to address this contention by concluding that, although the amendments "[did] not authorize a release of claims against third parties other than directors, [they did] not prohibit such releases either" (para. 92).

78 Respectfully, I would not adopt the interpretive principle that the CCAA permits releases because it does not expressly prohibit them. Rather, as I explain in these reasons, I believe the open-ended CCAA permits third-

party releases that are reasonably related to the restructuring at issue because they are encompassed in the comprehensive terms "compromise" and "arrangement" and because of the double-voting majority and court sanctioning statutory mechanism that makes them binding on unwilling creditors.

79 The appellants rely on a number of authorities, which they submit support the proposition that the CCAA may not be used to compromise claims as between anyone other than the debtor company and its creditors. Principal amongst these are *Steinberg Inc. c. Michaud*, *supra*; *NBD Bank, Canada v. Dofasco Inc.* (1999), 46 O.R. (3d) 514 (Ont. C.A.); *Pacific Coastal Airlines Ltd. v. Air Canada* (2001), 19 B.L.R. (3d) 286 (B.C. S.C.); and *Stelco Inc., Re* (2005), 78 O.R. (3d) 241 (Ont. C.A.) ("*Stelco I*"). I do not think these cases assist the appellants, however. With the exception of *Steinberg Inc.*, they do not involve third party claims that were reasonably connected to the restructuring. As I shall explain, it is my opinion that *Steinberg Inc.* does not express a correct view of the law, and I decline to follow it.

80 In *Pacific Coastal Airlines Ltd.*, Tysoe J. made the following comment at para. 24:

> [The purpose of the CCAA proceeding] is not to deal with disputes between a creditor of a company and a third party, even if the company was also involved in the subject matter of the dispute. While issues between the debtor company and non-creditors are sometimes dealt with in CCAA proceedings, it is not a proper use of a CCAA proceeding to determine disputes between parties other than the debtor company.

81 This statement must be understood in its context, however. Pacific Coastal Airlines had been a regional carrier for Canadian Airlines prior to the CCAA reorganization of the latter in 2000. In the action in question it was seeking to assert separate tort claims against Air Canada for contractual interference and inducing breach of contract in relation to certain rights it had to the use of Canadian's flight designator code prior to the CCAA proceeding. Air Canada sought to have the action dismissed on grounds of *res judicata* or issue estoppel because of the CCAA proceeding. Tysoe J. rejected the argument.

82 The facts in *Pacific Coastal Airlines Ltd.* are not analogous to the circumstances of this case, however. There is no suggestion that a resolution of Pacific Coastal's separate tort claim against Air Canada was in any way connected to the Canadian Airlines restructuring, even though Canadian — at a contractual level — may have had some involvement with the particular dispute. Here, however, the disputes that are the subject-matter of the impugned releases are not simply "disputes between parties other than the debtor company". They are closely connected to the disputes being resolved between the debtor companies and their creditors and to the restructuring itself.

83 Nor is the decision of this Court in the *NBD Bank, Canada* case dispositive. It arose out of the financial collapse of Algoma Steel, a wholly-owned subsidiary of Dofasco. The Bank had advanced funds to Algoma allegedly on the strength of misrepresentations by Algoma's Vice-President, James Melville. The plan of compromise and arrangement that was sanctioned by Farley J. in the Algoma CCAA restructuring contained a clause releasing Algoma from all claims creditors "may have had against Algoma or its directors, officers, employees and advisors." Mr. Melville was found liable for negligent misrepresentation in a subsequent action by the Bank. On appeal, he argued that since the Bank was barred from suing Algoma for misrepresentation by its officers, permitting it to pursue the same cause of action against him personally would subvert the CCAA process — in short, he was personally protected by the CCAA release.

84 Rosenberg J.A., writing for this Court, rejected this argument. The appellants here rely particularly upon his following observations at paras. 53-54:

> 53 In my view, the appellant has not demonstrated that allowing the respondent to pursue its claim against him would undermine or subvert the purposes of the Act. As this court noted in *Elan Corp. v. Comiskey* (1990), 1 O.R. (3d) 289 at 297, the *CCAA* is remedial legislation "intended to provide a structured environment for the negotiation of compromises between a debtor company and its creditors for the benefit of both". It is a means of avoiding a liquidation that may yield little for the creditors, especially unsecured creditors like the respondent, and the debtor company shareholders. However, the appellant has not shown that allowing a creditor to continue an action against an officer for negligent misrepresentation would erode the effectiveness of the Act.
>
> 54 In fact, to refuse on policy grounds to impose liability on an officer of the corporation for negligent misrepresentation would contradict the policy of Parliament as demonstrated in recent amendments to the *CCAA* and the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3. Those Acts now contemplate that an arrangement or proposal may include a term for compromise of certain types of claims against directors of the company except claims that "are based on allegations of misrepresentations made by directors". L.W. Houlden and C.H. Morawetz, the editors of *The 2000 Annotated Bankruptcy and Insolvency Act* (Toronto: Carswell, 1999) at p. 192 are of the view that the policy behind the provision is to encourage directors of an insolvent corporation to remain in office so that the affairs of the corporation can be reorganized. I can see no similar policy interest in barring an action against an officer of the company who, prior to the insolvency, has misrepresented the financial affairs of the corporation to its creditors. It may be necessary to permit the compromise of claims against the debtor corporation, otherwise it may not be possible to successfully reorganize the corporation. The same considerations do not apply to individual officers. Rather, it would seem to me that it would be contrary to good policy to immunize officers from the consequences of their negligent statements which might otherwise be made in anticipation of being forgiven under a subsequent corporate proposal or arrangement. [Footnote omitted.]

85 Once again, this statement must be assessed in context. Whether Justice Farley had the authority in the earlier Algoma CCAA proceedings to sanction a plan that included third party releases was not under consideration at all. What the Court was determining in *NBD Bank, Canada* was whether the release extended by its terms to protect a third party. In fact, on its face, it does not appear to do so. Justice Rosenberg concluded only that not allowing Mr. Melville to rely upon the release did not subvert the purpose of the CCAA. As the application judge here observed, "there is little factual similarity in *NBD Bank, Canada* to the facts now before the Court" (para. 71). Contrary to the facts of this case, in *NBD Bank, Canada* the creditors had not agreed to grant a release to officers; they had not voted on such a release and the court had not assessed the fairness and reasonableness of such a release as a term of a complex arrangement involving significant contributions by the beneficiaries of the release — as is the situation here. Thus, *NBD Bank, Canada* is of little assistance in determining whether the court has authority to sanction a plan that calls for third party releases.

86 The appellants also rely upon the decision of this Court in *Stelco I*. There, the Court was dealing with the scope of the CCAA in connection with a dispute over what were called the "Turnover Payments". Under an inter-creditor agreement one group of creditors had subordinated their rights to another group and agreed to hold in trust and "turn over" any proceeds received from Stelco until the senior group was paid in full. On a disputed classification motion, the Subordinated Debt Holders argued that they should be in a separate class from the Senior Debt Holders. Farley J. refused to make such an order in the court below, stating:

> [Sections] 4, 5 and 6 [of the CCAA] talk of compromises or arrangements between a company and its creditors. There is no mention of this extending by statute to encompass a change of relationship among the

> creditors vis-à-vis the creditors themselves *and not directly involving the company*. [Citations omitted; emphasis added.]

See *Re Stelco Inc.* (2005), 15 C.B.R. (5th) 297 (Ont. S.C.J. [Commercial List]) at para. 7.

87 This Court upheld that decision. The legal relationship between each group of creditors and Stelco was the same, albeit there were inter-creditor differences, and creditors were to be classified in accordance with their legal rights. In addition, the need for timely classification and voting decisions in the CCAA process militated against enmeshing the classification process in the vagaries of inter-corporate disputes. In short, the issues before the Court were quite different from those raised on this appeal.

88 Indeed, the Stelco plan, as sanctioned, included third party releases (albeit uncontested ones). This Court subsequently dealt with the same inter-creditor agreement on an appeal where the Subordinated Debt Holders argued that the inter-creditor subordination provisions were beyond the reach of the CCAA and therefore that they were entitled to a separate civil action to determine their rights under the agreement: *Stelco Inc., Re* (2006), 21 C.B.R. (5th) 157 (Ont. C.A.) (*"Stelco II"*). The Court rejected that argument and held that where the creditors' rights amongst themselves were sufficiently related to the debtor and its plan, they were properly brought within the scope of the CCAA plan. The Court said (para. 11):

> In [*Stelco I*] — the classification case — the court observed that it is not a proper use of a CCAA proceeding to determine disputes between parties other than the debtor company ... [*H*]*owever, the present case is not simply an inter-creditor dispute that does not involve the debtor company; it is a dispute that is inextricably connected to the restructuring process*. [Emphasis added.]

89 The approach I would take to the disposition of this appeal is consistent with that view. As I have noted, the third party releases here are very closely connected to the ABCP restructuring process.

90 Some of the appellants — particularly those represented by Mr. Woods — rely heavily upon the decision of the Quebec Court of Appeal in *Steinberg Inc. c. Michaud*, *supra*. They say that it is determinative of the release issue. In *Steinberg*, the Court held that the CCAA, as worded at the time, did not permit the release of directors of the debtor corporation and that third-party releases were not within the purview of the Act. Deschamps J.A. (as she then was) said (paras. 42, 54 and 58 — English translation):

> [42] Even if one can understand the extreme pressure weighing on the creditors and the respondent at the time of the sanctioning, a plan of arrangement is not the appropriate forum to settle disputes other than the claims that are the subject of the arrangement. In other words, one cannot, under the pretext of an absence of formal directives in the Act, transform an arrangement into a potpourri.
>
> . . . . .
>
> [54] The Act offers the respondent a way to arrive at a compromise with is creditors. It does not go so far as to offer an umbrella to all the persons within its orbit by permitting them to shelter themselves from any recourse.
>
> . . . . .
>
> [58] The [CCAA] and the case law clearly do not permit extending the application of an arrangement to persons other than the respondent and its creditors and, consequently, the plan should not have been sanctioned

as is [that is, including the releases of the directors].

91 Justices Vallerand and Delisle, in separate judgments, agreed. Justice Vallerand summarized his view of the consequences of extending the scope of the CCAA to third party releases in this fashion (para. 7):

> In short, the Act will have become the Companies' *and Their Officers and Employees* Creditors Arrangement Act — an awful mess — and likely not attain its purpose, which is to enable the company to survive in the face of *its* creditors and through their will, and not in the face of the creditors of its officers. This is why I feel, just like my colleague, that such a clause is contrary to the Act's mode of operation, contrary to its purposes and, for this reason, is to be banned.

92 Justice Delisle, on the other hand, appears to have rejected the releases because of their broad nature — they released directors from all claims, including those that were altogether unrelated to their corporate duties with the debtor company — rather than because of a lack of authority to sanction under the Act. Indeed, he seems to have recognized the wide range of circumstances that could be included within the term "compromise or arrangement". He is the only one who addressed that term. At para. 90 he said:

> The CCAA is drafted in general terms. It does not specify, among other things, what must be understood by "compromise or arrangement". However, it may be inferred from the purpose of this [A]ct that these terms *encompass all that should enable the person who has recourse to it to fully dispose of his debts*, both those that exist on the date when he has recourse to the statute and *those contingent on the insolvency in which he finds himself* ... [Emphasis added.]

93 The decision of the Court did not reflect a view that the terms of a compromise or arrangement should "encompass all that should enable the person who has recourse to [the Act] to dispose of his debts ... and those contingent on the insolvency in which he finds himself," however. On occasion such an outlook might embrace third parties other than the debtor and its creditors in order to make the arrangement work. Nor would it be surprising that, in such circumstances, the third parties might seek the protection of releases, or that the debtor might do so on their behalf. Thus, the perspective adopted by the majority in *Steinberg Inc.*, in my view, is too narrow, having regard to the language, purpose and objects of the CCAA and the intention of Parliament. They made no attempt to consider and explain why a compromise or arrangement could not include third-party releases. In addition, the decision appears to have been based, at least partly, on a rejection of the use of contract-law concepts in analysing the Act — an approach inconsistent with the jurisprudence referred to above.

94 Finally, the majority in *Steinberg Inc.* seems to have proceeded on the basis that the CCAA cannot interfere with civil or property rights under Quebec law. Mr. Woods advanced this argument before this Court in his factum, but did not press it in oral argument. Indeed, he conceded that if the Act encompasses the authority to sanction a plan containing third-party releases — as I have concluded it does — the provisions of the CCAA, as valid federal insolvency legislation, are paramount over provincial legislation. I shall return to the constitutional issues raised by the appellants later in these reasons.

95 Accordingly, to the extent *Steinberg Inc.* stands for the proposition that the court does not have authority under the CCAA to sanction a plan that incorporates third-party releases, I do not believe it to be a correct statement of the law and I respectfully decline to follow it. The modern approach to interpretation of the Act in accordance with its nature and purpose militates against a narrow interpretation and towards one that facilitates and encourages compromises and arrangements. Had the majority in *Steinberg Inc.* considered the broad nature of the terms "compromise" and "arrangement" and the jurisprudence I have referred to above, they might well

have come to a different conclusion.

The 1997 Amendments

96 *Steinberg Inc.* led to amendments to the CCAA, however. In 1997, s. 5.1 was added, dealing specifically with releases pertaining to directors of the debtor company. It states:

> 5.1(1) A compromise or arrangement made in respect of a debtor company may include in its terms provision for the compromise of claims against directors of the company that arose before the commencement of proceedings under this Act and that relate to the obligations of the company where the directors are by law liable in their capacity as directors for the payment of such obligations.
>
> **Exception**
>
> (2) A provision for the compromise of claims against directors may not include claims that
>
> (a) relate to contractual rights of one or more creditors; or
>
> (b) are based on allegations of misrepresentations made by directors to creditors or of wrongful or oppressive conduct by directors.
>
> **Powers of court**
>
> (3) The court may declare that a claim against directors shall not be compromised if it is satisfied that the compromise would not be fair and reasonable in the circumstances.
>
> **Resignation or removal of directors**
>
> (4) Where all of the directors have resigned or have been removed by the shareholders without replacement, any person who manages or supervises the management of the business and affairs of the debtor company shall be deemed to be a director for the purposes of this section.
>
> 1997, c. 12, s. 122.

97 Perhaps the appellants' strongest argument is that these amendments confirm a prior lack of authority in the court to sanction a plan including third party releases. If the power existed, why would Parliament feel it necessary to add an amendment specifically permitting such releases (subject to the exceptions indicated) in favour of directors? *Expressio unius est exclusio alterius*, is the Latin maxim sometimes relied on to articulate the principle of interpretation implied in that question: to express or include one thing implies the exclusion of the other.

98 The maxim is not helpful in these circumstances, however. The reality is that there *may* be another explanation why Parliament acted as it did. As one commentator has noted:[FN8]

> Far from being a rule, [the maxim *expressio unius*] is not even lexicographically accurate, because it is simply not true, generally, that the mere express conferral of a right or privilege in one kind of situation implies the denial of the equivalent right or privilege in other kinds. Sometimes it does and sometimes its does not, and whether it does or does not depends on the particular circumstances of context. Without contextual support, therefore there is not even a mild presumption here. Accordingly, the maxim is at best a description, after the fact, of what the court has discovered from context.

99 As I have said, the 1997 amendments to the CCAA providing for releases in favour of directors of debtor companies in limited circumstances were a response to the decision of the Quebec Court of Appeal in *Steinberg Inc.*. A similar amendment was made with respect to proposals in the BIA at the same time. The rationale behind these amendments was to encourage directors of an insolvent company to remain in office during a restructuring, rather than resign. The assumption was that by remaining in office the directors would provide some stability while the affairs of the company were being reorganized: see Houlden & Morawetz, vol.1, *supra*, at 2-144, E§11A; *Royal Penfield Inc., Re*, [2003] R.J.Q. 2157 (Que. S.C.) at paras. 44-46.

100 Parliament thus had a particular focus and a particular purpose in enacting the 1997 amendments to the CCAA and the BIA. While there is some merit in the appellants' argument on this point, at the end of the day I do not accept that Parliament intended to signal by its enactment of s. 5.1 that it was depriving the court of authority to sanction plans of compromise or arrangement in all circumstances where they incorporate third party releases in favour of anyone other than the debtor's directors. For the reasons articulated above, I am satisfied that the court does have the authority to do so. Whether it sanctions the plan is a matter for the fairness hearing.

The Deprivation of Proprietary Rights

101 Mr. Shapray very effectively led the appellants' argument that legislation must not be construed so as to interfere with or prejudice established contractual or proprietary rights — including the right to bring an action — in the absence of a clear indication of legislative intention to that effect: *Halsbury's Laws of England*, 4th ed. reissue, vol. 44 (1) (London: Butterworths, 1995) at paras. 1438, 1464 and 1467; Driedger, 2nd ed., *supra*, at 183; Ruth Sullivan, *Sullivan and Driedger on the Construction of Statutes*, 4th ed., (Markham: Butterworths, 2002) at 399. I accept the importance of this principle. For the reasons I have explained, however, I am satisfied that Parliament's intention to clothe the court with authority to consider and sanction a plan that contains third party releases is expressed with sufficient clarity in the "compromise or arrangement" language of the CCAA coupled with the statutory voting and sanctioning mechanism making the provisions of the plan binding on all creditors. This is not a situation of impermissible "gap-filling" in the case of legislation severely affecting property rights; it is a question of finding meaning in the language of the Act itself. I would therefore not give effect to the appellants' submissions in this regard.

The Division of Powers and Paramountcy

102 Mr. Woods and Mr. Sternberg submit that extending the reach of the CCAA process to the compromise of claims as between solvent creditors of the debtor company and solvent third parties to the proceeding is constitutionally impermissible. They say that under the guise of the federal insolvency power pursuant to s. 91(21) of the *Constitution Act, 1867*, this approach would improperly affect the rights of civil claimants to assert their causes of action, a provincial matter falling within s. 92(13), and contravene the rules of public order pursuant to the *Civil Code of Quebec*.

103 I do not accept these submissions. It has long been established that the CCAA is valid federal legislation under the federal insolvency power: *Reference re Companies' Creditors Arrangement Act (Canada)*, [1934] S.C.R. 659 (S.C.C.). As the Supreme Court confirmed in that case (p. 661), citing Viscount Cave L.C. in *Quebec (Attorney General) v. Bélanger (Trustee of)*, [1928] A.C. 187 (Canada P.C.), "the exclusive legislative authority to deal with all matters within the domain of bankruptcy and insolvency is vested in Parliament." Chief Justice Duff elaborated:

> Matters normally constituting part of a bankruptcy scheme but not in their essence matters of bankruptcy

> and insolvency may, of course, from another point of view and in another aspect be dealt with by a provincial legislature; but, when treated as matters pertaining to bankruptcy and insolvency, they clearly fall within the legislative authority of the Dominion.

104 That is exactly the case here. The power to sanction a plan of compromise or arrangement that contains third-party releases of the type opposed by the appellants is embedded in the wording of the CCAA. The fact that this may interfere with a claimant's right to pursue a civil action — normally a matter of provincial concern — or trump Quebec rules of public order is constitutionally immaterial. The CCAA is a valid exercise of federal power. Provided the matter in question falls within the legislation directly or as necessarily incidental to the exercise of that power, the CCAA governs. To the extent that its provisions are inconsistent with provincial legislation, the federal legislation is paramount. Mr. Woods properly conceded this during argument.

Conclusion With Respect to Legal Authority

105 For all of the foregoing reasons, then, I conclude that the application judge had the jurisdiction and legal authority to sanction the Plan as put forward.

(2) The Plan is "Fair and Reasonable"

106 The second major attack on the application judge's decision is that he erred in finding that the Plan is "fair and reasonable" and in sanctioning it on that basis. This attack is centred on the nature of the third-party releases contemplated and, in particular, on the fact that they will permit the release of some claims based in fraud.

107 Whether a plan of compromise or arrangement is fair and reasonable is a matter of mixed fact and law, and one on which the application judge exercises a large measure of discretion. The standard of review on this issue is therefore one of deference. In the absence of a demonstrable error an appellate court will not interfere: see *Ravelston Corp., Re* (2007), 31 C.B.R. (5th) 233 (Ont. C.A. [In Chambers]).

108 I would not interfere with the application judge's decision in this regard. While the notion of releases in favour of third parties — including leading Canadian financial institutions — that extend to claims of fraud is distasteful, there is no legal impediment to the inclusion of a release for claims based in fraud in a plan of compromise or arrangement. The application judge had been living with and supervising the ABCP restructuring from its outset. He was intimately attuned to its dynamics. In the end he concluded that the benefits of the Plan to the creditors as a whole, and to the debtor companies, outweighed the negative aspects of compelling the unwilling appellants to execute the releases as finally put forward.

109 The application judge was concerned about the inclusion of fraud in the contemplated releases and at the May hearing adjourned the final disposition of the sanctioning hearing in an effort to encourage the parties to negotiate a resolution. The result was the "fraud carve-out" referred to earlier in these reasons.

110 The appellants argue that the fraud carve-out is inadequate because of its narrow scope. It (i) applies only to ABCP Dealers, (ii) limits the type of damages that may be claimed (no punitive damages, for example), (iii) defines "fraud" narrowly, excluding many rights that would be protected by common law, equity and the Quebec concept of public order, and (iv) limits claims to representations made directly to Noteholders. The appellants submit it is contrary to public policy to sanction a plan containing such a limited restriction on the type of fraud claims that may be pursued against the third parties.

111 The law does not condone fraud. It is the most serious kind of civil claim. There is therefore some force to the appellants' submission. On the other hand, as noted, there is no legal impediment to granting the release of an antecedent claim in fraud, provided the claim is in the contemplation of the parties to the release at the time it is given: *Fotinis Restaurant Corp. v. White Spot Ltd* (1998), 38 B.L.R. (2d) 251 (B.C. S.C. [In Chambers]) at paras. 9 and 18. There may be disputes about the scope or extent of what is released, but parties are entitled to settle allegations of fraud in civil proceedings — the claims here all being untested allegations of fraud — and to include releases of such claims as part of that settlement.

112 The application judge was alive to the merits of the appellants' submissions. He was satisfied in the end, however, that the need "to avoid the potential cascade of litigation that ... would result if a broader 'carve out' were to be allowed" (para. 113) outweighed the negative aspects of approving releases with the narrower carve-out provision. Implementation of the Plan, in his view, would work to the overall greater benefit of the Noteholders as a whole. I can find no error in principle in the exercise of his discretion in arriving at this decision. It was his call to make.

113 At para. 71 above I recited a number of factual findings the application judge made in concluding that approval of the Plan was within his jurisdiction under the CCAA and that it was fair and reasonable. For convenience, I reiterate them here — with two additional findings — because they provide an important foundation for his analysis concerning the fairness and reasonableness of the Plan. The application judge found that:

> a) The parties to be released are necessary and essential to the restructuring of the debtor;
>
> b) The claims to be released are rationally related to the purpose of the Plan and necessary for it;
>
> c) The Plan cannot succeed without the releases;
>
> d) The parties who are to have claims against them released are contributing in a tangible and realistic way to the Plan;
>
> e) The Plan will benefit not only the debtor companies but creditor Noteholders generally;
>
> f) The voting creditors who have approved the Plan did so with knowledge of the nature and effect of the releases; and that,
>
> g) The releases are fair and reasonable and not overly broad or offensive to public policy.

114 These findings are all supported on the record. Contrary to the submission of some of the appellants, they do not constitute a new and hitherto untried "test" for the sanctioning of a plan under the CCAA. They simply represent findings of fact and inferences on the part of the application judge that underpin his conclusions on jurisdiction and fairness.

115 The appellants all contend that the obligation to release the third parties from claims in fraud, tort, breach of fiduciary duty, etc. is confiscatory and amounts to a requirement that they — as individual creditors — make the equivalent of a greater financial contribution to the Plan. In his usual lively fashion, Mr. Sternberg asked us the same rhetorical question he posed to the application judge. As he put it, how could the court countenance the compromise of what in the future might turn out to be fraud perpetrated at the highest levels of Canadian and foreign banks? Several appellants complain that the proposed Plan is unfair to them because they will make very little additional recovery if the Plan goes forward, but will be required to forfeit a cause of action

against third-party financial institutions that may yield them significant recovery. Others protest that they are being treated unequally because they are ineligible for relief programs that Liquidity Providers such as Canaccord have made available to other smaller investors.

116 All of these arguments are persuasive to varying degrees when considered in isolation. The application judge did not have that luxury, however. He was required to consider the circumstances of the restructuring as a whole, including the reality that many of the financial institutions were not only acting as Dealers or brokers of the ABCP Notes (with the impugned releases relating to the financial institutions in these capacities, for the most part) but also as Asset and Liquidity Providers (with the financial institutions making significant contributions to the restructuring in these capacities).

117 In insolvency restructuring proceedings almost everyone loses something. To the extent that creditors are required to compromise their claims, it can always be proclaimed that their rights are being unfairly confiscated and that they are being called upon to make the equivalent of a further financial contribution to the compromise or arrangement. Judges have observed on a number of occasions that CCAA proceedings involve "a balancing of prejudices," inasmuch as everyone is adversely affected in some fashion.

118 Here, the debtor corporations being restructured represent the issuers of the more than $32 billion in non-bank sponsored ABCP Notes. The proposed compromise and arrangement affects that entire segment of the ABCP market and the financial markets as a whole. In that respect, the application judge was correct in adverting to the importance of the restructuring to the resolution of the ABCP liquidity crisis and to the need to restore confidence in the financial system in Canada. He was required to consider and balance the interests of *all* Noteholders, not just the interests of the appellants, whose notes represent only about 3% of that total. That is what he did.

119 The application judge noted at para. 126 that the Plan represented "a reasonable balance between benefit to all Noteholders and enhanced recovery for those who can make out specific claims in fraud" within the fraud carve-out provisions of the releases. He also recognized at para. 134 that:

> No Plan of this size and complexity could be expected to satisfy all affected by it. The size of the majority who have approved it is testament to its overall fairness. No plan to address a crisis of this magnitude can work perfect equity among all stakeholders.

120 In my view we ought not to interfere with his decision that the Plan is fair and reasonable in all the circumstances.

D. Disposition

121 For the foregoing reasons, I would grant leave to appeal from the decision of Justice Campbell, but dismiss the appeal.

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

I agree.

***E.A. Cronk J.A.*:**

I agree.

Schedule A — Conduits

Apollo Trust

Apsley Trust

Aria Trust

Aurora Trust

Comet Trust

Encore Trust

Gemini Trust

Ironstone Trust

MMAI-I Trust

Newshore Canadian Trust

Opus Trust

Planet Trust

Rocket Trust

Selkirk Funding Trust

Silverstone Trust

Slate Trust

Structured Asset Trust

Structured Investment Trust III

Symphony Trust

Whitehall Trust

Schedule B — Applicants

ATB Financial

Caisse de dépôt et placement du Québec

Canaccord Capital Corporation

Canada Mortgage and Housing Corporation

Canada Post Corporation

Credit Union Central Alberta Limited

Credit Union Central of BC

Credit Union Central of Canada

Credit Union Central of Ontario

Credit Union Central of Saskatchewan

Desjardins Group

Magna International Inc.

National Bank of Canada/National Bank Financial Inc.

NAV Canada

Northwater Capital Management Inc.

Public Sector Pension Investment Board

The Governors of the University of Alberta

Schedule A — Counsel

1) Benjamin Zarnett and Frederick L. Myers for the Pan-Canadian Investors Committee

2) Aubrey E. Kauffman and Stuart Brotman for 4446372 Canada Inc. and 6932819 Canada Inc.

3) Peter F.C. Howard and Samaneh Hosseini for Bank of America N.A.; Citibank N.A.; Citibank Canada, in its capacity as Credit Derivative Swap Counterparty and not in any other capacity; Deutsche Bank AG; HSBC Bank Canada; HSBC Bank USA, National Association; Merrill Lynch International; Merill Lynch Capital Services, Inc.; Swiss Re Financial Products Corporation; and UBS AG

4) Kenneth T. Rosenberg, Lily Harmer and Max Starnino for Jura Energy Corporation and Redcorp Ventures Ltd.

5) Craig J. Hill and Sam P. Rappos for the Monitors (ABCP Appeals)

6) Jeffrey C. Carhart and Joseph Marin for Ad Hoc Committee and Pricewaterhouse Coopers Inc., in its capacity as Financial Advisor

7) Mario J. Forte for Caisse de Dépôt et Placement du Québec

8) John B. Laskin for National Bank Financial Inc. and National Bank of Canada

9) Thomas McRae and Arthur O. Jacques for Ad Hoc Retail Creditors Committee (Brian Hunter, et al)

10) Howard Shapray, Q.C. and Stephen Fitterman for Ivanhoe Mines Ltd.

11) Kevin P. McElcheran and Heather L. Meredith for Canadian Banks, BMO, CIBC RBC, Bank of Nova Scotia and T.D. Bank

12) Jeffrey S. Leon for CIBC Mellon Trust Company, Computershare Trust Company of Canada and BNY Trust Company of Canada, as Indenture Trustees

13) Usman Sheikh for Coventree Capital Inc.

14) Allan Sternberg and Sam R. Sasso for Brookfield Asset Management and Partners Ltd. and Hy Bloom Inc. and Cardacian Mortgage Services Inc.

15) Neil C. Saxe for Dominion Bond Rating Service

16) James A. Woods, Sebastien Richemont and Marie-Anne Paquette for Air Transat A.T. Inc., Transat Tours Canada Inc., The Jean Coutu Group (PJC) Inc., Aéroports de Montréal, Aéroports de Montréal Capital Inc., Pomerleau Ontario Inc., Pomerleau Inc., Labopharm Inc., Agence Métropolitaine de Transport (AMT), Giro Inc., Vêtements de sports RGR Inc., 131519 Canada Inc., Tecsys Inc., New Gold Inc. and Jazz Air LP

17) Scott A. Turner for Webtech Wireless Inc., Wynn Capital Corporation Inc., West Energy Ltd., Sabre Energy Ltd., Petrolifera Petroleum Ltd., Vaquero Resources Ltd., and Standard Energy Ltd.

18) R. Graham Phoenix for Metcalfe & Mansfield Alternative Investments II Corp., Metcalfe & Mansfield Alternative Investments III Corp., Metcalfe & Mansfield Alternative Investments V Corp., Metcalfe & Mansfield Alternative Investments XI Corp., Metcalfe & Mansfield Alternative Investments XII Corp., Quanto Financial Corporation and Metcalfe & Mansfield Capital Corp.

Application granted; appeal dismissed.

FN* Leave to appeal refused at *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 2008 CarswellOnt 5432, 2008 CarswellOnt 5433 (S.C.C.).

FN1 Section 5.1 of the CCAA specifically authorizes the granting of releases to directors in certain circumstances.

FN2 Justice Georgina R. Jackson and Dr. Janis P. Sarra, "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters" in Sarra, ed., *Annual Review of Insolvency Law, 2007* (Vancouver: Thomson Carswell, 2007).

FN3 Citing Gibbs J.A. in *Chef Ready Foods*, *supra*, at pp.319-320.

FN4 The Legislative Debates at the time the CCAA was introduced in Parliament in April 1933 make it clear that the CCAA is patterned after the predecessor provisions of s. 425 of the *Companies Act 1985* (U.K.): see

House of Commons Debates (Hansard), supra.

FN5 See *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, s. 192; *Ontario Business Corporations Act*, R.S.O. 1990, c. B.16, s. 182.

FN6 A majority in number representing two-thirds in value of the creditors (s. 6)

FN7 *Steinberg Inc.* was originally reported in French: *Steinberg Inc. c. Michaud*, [1993] R.J.Q. 1684 (Que. C.A.). All paragraph references to *Steinberg Inc.* in this judgment are from the unofficial English translation available at 1993 CarswellQue 2055 (Que. C.A.)

FN8 Reed Dickerson, *The Interpretation and Application of Statutes* (1975) at pp.234-235, cited in Bryan A. Garner, ed., Black's Law Dictionary, 8th ed. (West Group, St. Paul, Minn., 2004) at 621.

END OF DOCUMENT

Tab 2

Case Name:

Canadian Airlines Corp. (Re)

IN THE MATTER OF Canadian Airlines Corporation and Canadian Airlines International Ltd.
Between
The Bank of Nova Scotia Trust Company of New York, As Trustee for the Holders of Senior Secured Notes and Montreal Trust Company of Canada, As Collateral Agent for the Holders of Senior Secured Notes, Plaintiffs, and
Canadian Airlines Corporation, Canadian Airlines International Ltd., Canadian Regional Airlines Ltd., Canadian Regional Airlines (1998) Ltd. and Canadian Airlines Fuel Corporation Inc., defendants

[2000] A.J. No. 1692

19 C.B.R. (4th) 1

Docket: 0001-05071, 0001-05044

Alberta Court of Queen's Bench
Judicial District of Calgary

Paperny J.

Oral Judgment: May 4, 2000.

(41 paras.)

Application by holders of senior secured notes in corporation for order lifting stay of proceedings against them in Companies' Creditors Arrangement Act proceeding to allow for appointment of receiver and manager over assets and property charged in their favour and for order appointing court officer with exclusive right to negotiate sale of assets or shares of corporation's subsidiary.

Counsel:

G. Morawetz, A.J. McConnell and R.N. Billington, for Bank of Nova Scotia Trust Co. of New York and Montreal Trust Co. of Canada.

A.L. Friend, Q. C., and H.M. Kay, Q. C., for Canadian Airlines.

S. Dunphy, for Air Canada and 853350 Alberta Ltd.

R. Anderson, Q.C., for Loyalty Group.

H. Gorman, for ABN AMRO Bank N.V.

P. McCarthy, for Monitor - Price Waterhouse Cooper.

D. Haigh, Q.C, and D. Nishimura, for Unsecured noteholders - Resurgence Asset Management.

C.J. Shaw, for Airline Pilots Association International.

G. Wells, for NavCanada.

D. Hardy, for Royal Bank of Canada.

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1 PAPERNY J. (orally):-- Montreal Trust Company of Canada, Collateral Agent for the holders of the Senior Secured Notes, and the Bank of Nova Scotia Trust Company of New York, Trustee for the holders of the Senior Secured Notes, apply for the following relief:

1. In the CCAA proceeding (Action No. 0001-05071) an order lifting the stay of proceedings against them contained in the orders of this court dated March 24, 2000 and April 19, 2000 to allow for the court-ordered appointment of Ernst & Young Inc. as receiver and manager over the assets and property charged in favour of the Senior Secured Noteholders; and
2. In Action No. 0001-05044, an order appointing Ernst & Young Inc. as a court officer with the exclusive right to negotiate the sale of the assets or shares of Canadian Regional Airlines (1998) Ltd.

2 Canadian Airlines Corporation ("CAC") is a Canadian based holding company which, through its majority owned subsidiary Canadian Airlines International Ltd. ("CAC") provides domestic, U.S.-Canada transborder and international jet air transportation services. CAC also provides regional transportation through its subsidiary Canadian Regional Airlines (1998) Ltd. ("Canadian Regional"). Canadian Regional is not an applicant under the CCAA proceedings.

3 The Senior Secured Notes were issued under an Indenture dated April 24, 1998 between CAC and the Trustee. The principal face amount is $175 million U.S. As well, there is interest outstanding. The Senior Secured Notes are directly and indirectly secured by a diverse package of assets and property of the CCAA applicants, including spare engines, rotables, repairables, hangar leases and ground equipment. The security comprises the key operational assets of CAC and CAIL. The security also includes the outstanding shares of Canadian Regional and the $56 million intercompany indebtedness owed by Canadian Regional to CAIL.

4 Under the terms of the Indenture, CAC is required to make an offer to purchase the Senior Secured Notes where there is a "change of control" of CAC. It is submitted by the Senior Secured Noteholders that Air Canada indirectly acquired control of CAC on January 4, 2000 resulting in a change of control. Under the Indenture, CAC is then required to purchase the notes at 101 percent of the outstanding principal, interest and costs. CAC did not do so. According to the Trustee, an Event of Default occurred, and on March 6, 2000 the Trustee delivered Notices of Intention to Enforce Security under the Bankruptcy and Insolvency Act.

5 On March 24, 2000, the Senior Secured Noteholders commenced Action No. 0001-05044 and brought an application for the appointment of a receiver over their collateral. On the same day, CAC and CAIL were granted CCAA protection and the Senior Secured Noteholders adjourned their application for a receiver. However, the Senior Secured Noteholders made further application that day for orders that Ernst & Young be appointed monitor over their security and for weekly payments from CAC and CAIL of $500,000 U.S. These applications were dismissed.

6 The CCAA Plan filed on April 25, 2000, proposes that the Senior Secured Noteholders constitute a separate class and offers them two alternatives:

1. To accept repayment of less than the outstanding amount; or
2. To be unaffected by the CCAA Plan and realize on their security.

7 On April 26th, 2000, the Senior Secured Noteholders met and unanimously rejected the first option. They passed a resolution to take steps to realize on the security.

8 The Senior Secured Noteholders argue that the time has come to permit them to realize on their security. They have already rejected the Plan and see no utility in waiting to vote in this regard on May 26th, 2000, the date set by this court.

9 The Senior Secured Noteholders submit that since the CCAA proceedings began five weeks ago, the following has occurred:

-interest has continued to accrue at approximately $2 million U.S. per month;

-the security has decreased in value by approximately $6 million Canadian;

-the Collateral Agent and the Trustee have incurred substantial costs;

-no amounts have been paid for the continued use of the collateral, which is key to the operations of CAIL;

-no outstanding accrued interest has been paid; and-they are the only secured creditor not getting paid.

10 The Senior Secured Noteholders emphasize that one of the end results of the Plan is a transfer of CAIL's assets to Air Canada. The Senior Secured Noteholders assert that the Plan is sponsored by this very solvent proponent, who is in a position to pay them in full. They are argue that Air Canada has made an economic decision not to do so and instead is using the CCAA to achieve its own objectives at their expense, an inappropriate use of the Act.

11 The Senior Secured Noteholders suggest that the Plan will not be impacted if they are permitted to realize on their security now instead of after a formal rejection of the Plan at the court scheduled vote on May 26, 2000. The Senior Secured Noteholders argue that for all of the preceding reasons lifting the stay would be in accordance with the spirit and intent of the CCAA.

12 The CCAA is remedial legislation which should be given a large and liberal interpretation: See, for example, Citibank Canada v. Chase Manhattan Bank of Canada (1991), 5 C.B.R. (3d) 165 (Ont. Gen. Div.). It is intended to permit the court to make orders which will effectively maintain the status quo for a period while the struggling company attempts to develop a plan to compromise its debts and ultimately continue operations for the benefit of both the company and its creditors: See for example, Meridian Development Inc. v. Toronto Dominion Bank (1984), 52 C.B.R. (N.S.) 109 (Alta. Q.B.), and Hongkong Bank of Canada v. Chef Ready Foods Ltd. (1990), 4 C.B.R. (3d) 311 (B.C.C.A.).

13 This aim is facilitated by the power to stay proceedings provided by Section 11 of the Act. The stay power is the key element of the CCAA process.

14 The granting of a stay under Section 11 is discretionary. On the debtor's initial application, the court may order a stay at its discretion for a period not to exceed 30 days. The burden of proof to obtain a stay extension under Section 11(4) is on the debtor. The debtor must satisfy the court that circumstances exist that make the request for a stay extension appropriate and that the debtor has acted, and is acting, in good faith and with due diligence. CAC and CAIL discharged this burden on April 19, 2000. However, unlike under the Bankruptcy and Insolvency Act, there is no statutory test under the CCAA to guide the court in lifting a stay against a certain creditor.

15 In determining whether a stay should be lifted, the court must always have regard to the particular facts. However, in every order in a CCAA proceeding the court is required to balance a number of interests. McFarlane J.A. states in his closing remarks of his reasons in Re Pacific National Lease Holding Corp. (1992), 15 C.B.R. (3d) 265 (B.C.C.A. [In Chambers]):

> In supervising a proceeding under the C.C.A.A. orders are made, and orders are varied as changing circumstances require. Orders depend upon a careful and delicate balancing of a variety of interests and problems.

16 Also see Blair J.'s decision in Campeau v. Olympia & York Developments Ltd. (1992), 14 C.P.C. (3d) 339 (Ont. Gen. Div.), for another example of the balancing approach.

17 As noted above, the stay power is to be used to preserve the status quo among the creditors of the insolvent company. Huddart J., as she then was, commented on the status quo in Re Alberta-Pacific Terminals Ltd (1991), 8 C.B.R. (3d) 99 (B.C.S.C.). She stated:

> The status quo is not always easy to find... Nor is it always easy to define. The preservation of the status quo cannot mean merely the preservation of the relative pre-stay debt status of each creditor. Other interests are served by the CCAA. Those of investors, employees, and landlords among them, and in the case of the Fraser Surrey terminal, the public too, not only of British Columbia, but also of the prairie provinces. The status quo is to be preserved in the sense that manoeuvres by creditors that would impair the financial position of the company while it attempts to reorganize are to be prevented, not in the sense that all creditors are to be treated equally or to be maintained at the same relative level. It is the company and all the interests its demise would affect that must be considered.

18 Further commentary on the status quo is contained in Quintette Coal Ltd. v. Nippon Steel Corp. (1990), 80 C.B.R. (N.S.) 98 (B.C.S.C.). Thackray J. comments that the maintenance of the status quo does not mean that every detail of the status quo must survive. Rather, it means that the debtor will be able to stay in business and will have breathing space to develop a proposal to remain viable.

19 Finally, in making orders under the CCAA, the court must never lose sight of the objectives of the legislation. These were concisely summarized by the chambers judge and adopted by the British Columbia Court of Appeal in Re Pacific National Lease Holding Corp. (1992), 15 C.B.R. (3d) 265 (B.C.C.A. [In Chambers]):

(1) The purpose of the CCAA is to allow an insolvent company a reasonable period of time to reorganize its affairs and prepare and file a plan for its continued operation subject to the requisite approval of the creditors and court.

(2) The CCAA is intended to serve not only the company's creditors but also a broad

constituency which includes the shareholders and employees.

(3) During the stay period, the Act is intended to prevent manoeuvres for positioning amongst the creditors of the company.

(4) The function of the court during the stay period is to play a 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.

(5) The status quo does not mean preservation of the relative pre-stay debt status of each creditor. Since the companies under CCAA orders continue to operate and having regard to the broad constituency of interests the Act is intended to serve, the preservation of the status quo is not intended to create a rigid freeze of relative pre-stay positions.

(6) The court has a broad discretion to apply these principles to the facts of the particular case.

20 At pages 342 and 343 of this text, Canadian Commercial Reorganization:

> Preventing Bankruptcy (Aurora: Canada Law Book, looseleaf), R.H. McLaren describes situations in which the court will lift a stay:
>
> 1. When the plan is likely to fail;
> 2. The applicant shows hardship (the hardship must be caused by the stay itself and be independent of any pre-existing condition of the applicant creditor);
> 3. The applicant shows necessity for payment (where the creditors' financial problems are created by the order or where the failure to pay the creditor would cause it to close and thus jeopardize the debtor's company's existence);
> 4. The applicant would be severely prejudiced by refusal to lift the stay and there would be no resulting prejudice to the debtor company or the positions of creditors;
> 5. It is necessary to permit the applicant to take steps to protect a right which could be lost by the passage of time;
> 6. After the lapse of a significant time period, the insolvent is no closer to a proposal than at the commencement of the stay period.

21 I now turn to the particular circumstances of the applications before me.

22 I would firstly address the matter of the Senior Secured Noteholders' current rejection of the compromise put forward under the Plan. Although they are in a separate class under CAC's Plan and can control the vote as it affects their interest, they are not in a position to vote down the Plan in its entirety. However, the Senior Secured Noteholders submit that where a plan offers two options to a class of creditors and the class has selected which option it wants, there is no purpose to be

served in delaying that class from proceeding with its chosen course of action. They rely on the Nova Metal Products Inc. v. Comiskey (Trustee of) (1990), 1 C.B.R. (3d) 101 (Oat. CA.) at 115, as just one of several cases supporting this proposition. Re Philip's Manufacturing Ltd. (1992), 9 C.B.R. (3d) 25 (B.C.C.A.) at pp. 27-28, leave to appeal to S.C.C. refused (1992), 15 C.B.R. (3d) 57 (note) (S.C.C.), would suggest that the burden is on the Senior Secured Noteholders to establish that the Plan is "doomed to fail". To the extent that Nova Metal and Philip's Manufacturing articulate different tests to meet in this context, the application of either would not favour the Senior Secured Noteholders.

23 The evidence before me suggests that progress may still be made in the negotiations with the representatives of the Senior Secured Noteholders and that it would be premature to conclude that any further discussions would be unsuccessful. The parties are continuing to explore revisions and alternative proposals which would satisfy the Senior Secured Noteholders.

24 Mr. Carty's affidavit sworn May 1, 2000, in response to these applications states his belief that these efforts are being made in good faith and that, if allowed to continue, there is a real prospect for an acceptable proposal to be made at or before the creditors' meeting on May 26, 2000. Ms. Allen's affidavit does not contain any assertion that negotiations will cease. Despite the emphatic suggestion of the Senior Secured Noteholders' counsel that negotiations would be "one way", realistically I do not believe that there is no hope of the Senior Secured Noteholders coming to an acceptable compromise.

25 Further, there is no evidence before me that would indicate the Plan is "doomed to fail". The evidence does disclose that CAC and CAIL have already achieved significant compromises with creditors and continue to work swiftly and diligently to achieve further progress in this regard. This is reflected in the affidavits of Mr. Carty and the reports from the Monitor.

26 In any case, there is a fundamental problem in the application of the Senior Secured Noteholders to have a receiver appointed in respect of their security which the certainty of a "no" vote at this time does not vitiate: It disregards the interests of the other stakeholders involved in the process. These include other secured creditors, unsecured creditors, employees, shareholders and the flying public. It is not insignificant that the debtor companies serve an important national need in the operation of a national and international airline which employs tens of thousands of employees. As previously noted, these are all constituents the court must consider in making orders under the CCAA proceeding.

27 Paragraph 11 of Mr. Carty's May 1, 2000 affidavit states as follows:

> In my opinion, the continuation of the stay of proceedings to allow the restructuring process to continue will be of benefit to all stakeholders including the holders of the Senior Secured Notes. A termination of the stay proceedings as regards the security of the holders of the Senior Secured Notes would immediately deprive CAIL of assets which are critical to its operational integrity

> and would result in grave disruption of CAIL's operations and could lead to the cessation of operations. This would result in the destruction of value for all stakeholders, including the holders of the Senior Secured Notes. Furthermore, if CAIL ceased to operate, it is doubtful that Canadian Re-gional Airlines (1998) Ltd. ("CRAL98"), whose shares form a significant part of the security package of the holders of the Senior Secured Notes, would be in a position to continue operating and there would be a very real possibility that the equity of CAIL and CRAL, valued at approximately $115 million for the purposes of the issuance of the Senior Secured Notes in 1998, would be largely lost. Further, if such seizure caused CAIL to cease operations, the market for the assets and equipment which are subject to the security of the holders of the Senior Secured Notes could well be adversely affected, in that it could either lengthen the time necessary to realize on these assets or reduce realization values.

28 The alternative to this Plan proceeding is addressed in the Monitor's reports to the court. For example, in Paragraph 8 of the Monitor's third report to the court states:

> The Monitor believes the if the Plan is not approved and implemented, CAIL will not be able to continue as a going concern. In that case, the only foreseeable alternative would be a liquidation of CAIL's assets by a receiver and manager and/or by a trustee. Under the Plan, CAIL's obligations to parties it considers to be essential in order to continue operations, including employees, customers, travel agents, fuel, maintenance, catering and equipment suppliers, and airport authorities, are in most cases to be treated as unaffected and paid in full. In the event of a liquidation, those parties would not, in most cases, be paid in full and, except for specific lien rights, statutory priorities or other legal protection, would rank as ordinary unsecured creditors. The Monitor estimates that the additional unsecured claims which would arise if CAIL were to cease operation as a going concern and be forced into liquidation would he in excess of $1.1 billion.

29 This evidence is uncontradicted and flies in the face of the Senior Secured Noteholders' assertion that realizing on their collateral at this point in time will not affect the Plan. Although, as the Senior Secured Noteholders heavily emphasized the Plan does contemplate a "no" vote by the Senior Secured Noteholders, the removal of their security will follow that vote. 9.8(c) of the Plan states that:

> If the Required Majority of Affected Secured Noteholders fails to approve the Plan, arrangements in form and substance satisfactory to the Applicants will have been made with the Affected Secured Noteholders or with a re-ceiver appointed over the assets comprising the Senior Notes Security, which arrangements provide for the transitional use by [CALL], and subsequent sale, of the assets comprising the Senior Notes Security.

30 On the other side of the scale, the evidence of the Senior Secured Noteholders is that the value of their security is well in excess of what they are owed. Paragraph 15(a) of the Monitor's third report to the court values the collateral at $445 million. The evidence suggests that they are not the only secured creditor going unpaid. CAIL is asking that they be permitted to continue the restructuring process and their good faith efforts to attempt to reach an acceptable proposal with the Senior Secured Noteholders until the date of the creditors meeting, which is in three weeks. The Senior Secured Noteholders have not established that they will suffer any material prejudice in the intervening period.

31 The appointment of a receiver at this time would negate the effect of the order staying proceedings and thwart the purposes of the CCAA.

32 Accordingly, I am dismissing the application, with leave to reapply in the event that the Senior Secured Noteholders vote to reject the Plan on May 26, 2000.

33 An alternative to receivership raised by the Senior Secured Noteholders was interim payment for use of the security. The Monitor's third report makes it clear that the debtor's cash flow forecasts would not permit such payments.

34 The Senior Secured Noteholders suggested Air Canada could make the payments and, indeed, that Air Canada should pay out the debt owed to them by CAC. It is my view that, in the absence of abuse of the CCAA process, simply having a solvent entity financially supporting a plan with a view to ultimately obtaining an economic benefit for itself does not dictate that that entity should be required to pay creditors in full as requested. In my view, the evidence before me at this time does not suggest that the CCAA process is being improperly used. Rather, the evidence demonstrates these proceedings to be in furtherance of the objectives of the CCAA.

35 With respect to the application to sell shares or assets of Canadian Regional, this application raises a distinct issue in that Canadian Regional is not one of the debtor companies. In my view, Paragraph 5(a) of Chief Justice Moore's March 24, 2000 order encompasses marketing the shares or assets of Canadian Regional. That paragraph stays, inter alia:

> ...any and all proceedings ... against or in respect of ... any of the Petitioners' property ... whether held by the Petitioners directly or indirectly, as principal or nominee, beneficially or otherwise...

36 As noted above, Canadian Regional is CAC's subsidiary, and its shares and assets are the "property" of CAC and marketing of these would constitute a "proceeding ... in respect of ... the Petitioners' property" within the meaning of Paragraph 5(a) and Section 11 of the CCAA.

37 If I am incorrect in my interpretation of Paragraph 5(a), I rely on the inherent jurisdiction of the court in these proceedings.

38 As noted above, the CCAA is to be afforded a large and liberal interpretation. Two of the landmark decisions in this regard hail from Alberta: Meridian Development Mc. v. Toronto Dominion Bank, supra, and Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd. (1988), 72 C.B.R. (NS.) 20 (Alta. Q.B.). At least one court has also recognized an inherent jurisdiction in relation to the CCAA in order to grant stays in relation to proceedings against third parties: Re Woodward's Ltd. (1993), 17 C.B.R. (3d) 236 (B.C.S.C.). Tysoe J. urged that although this power should be used cautiously, a prerequisite to its use should not be an inability to otherwise complete the reorganization. Rather, what must be shown is that the exercise of the inherent jurisdiction is important to the reorganization process. The test described by Tysoe J. is consistent with the critical balancing that must occur in CCAA proceedings. He states:

> In deciding whether to exercise its inherent jurisdiction, the court should weigh the interests of the insolvent company against the interests of parties who will be affected by the exercise of the inherent jurisdiction. If, in relative terms, the prejudice to the affected party is greater than the benefit that will be achieved by the insolvent company, the court should decline to its inherent jurisdiction. The threshold of prejudice will be much lower than the threshold required to persuade the court that it should not exercise its discretion under Section 11 of the CCAA to grant or continue a stay that is prejudicial to a creditor of the insolvent company (or other party affected by the stay).

39 The balancing that I have described above in the context of the receivership application equally applies to this application. While the threshold of prejudice is lower, the Senior Secured Noteholders still fail to meet it. I cannot see that it is important to the CCAA proceedings that the Senior Secured Noteholders get started on marketing Canadian Regional. Instead, it would be disruptive and en-danger the CCAA proceedings which, on the evidence before me, have progressed swiftly and in good faith.

40 The application in Action No. 0001-05044 is dismissed, also with leave to reapply after the vote on May 26, 2000.

41 I appreciate that the Senior Secured Noteholders will be disappointed and likely frustrated with the outcome of these applications. I would emphasize that on the evidence before me their rights are being postponed and not eradicated. Any hardship they experience at this time must yield to the greater hardship that the debtor companies and the other constituents would suffer were the stay to be lifted at this time.

PAPERNY J.

cp/s/qw/qlmmm

Tab 3

Case Name:

Stelco Inc. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C., c. C-36, as amended
AND IN THE MATTER OF a proposed plan of compromise or arrangement with respect to Stelco Inc., and other Applicants listed in Schedule "A"*
[* Editor's note: Schedule "A" was not attached to the copy received from the Court and therefore is not included in the judgment.]
APPLICATION UNDER the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

[2005] O.J. No. 1171

75 O.R. (3d) 5

253 D.L.R. (4th) 109

196 O.A.C. 142

2 B.L.R. (4th) 238

9 C.B.R. (5th) 135

138 A.C.W.S. (3d) 222

2005 CarswellOnt 1188

2005 CanLII 8671

Docket: M32289

Ontario Court of Appeal
Toronto, Ontario

S.T. Goudge, K.N. Feldman and R.A. Blair JJ.A.

Heard: March 18, 2005.
Judgment: March 31, 2005.

(79 paras.)

Creditors & debtors law -- Legislation -- Debtors' relief -- Companies' Creditors Arrangement Act -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Civil procedure -- Courts -- Jurisdiction -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Civil procedure -- Courts -- Superior courts -- Inherent jurisdiction -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Corporations and associations law -- Corporations -- Directors -- Appointment or election -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Corporations and associations law -- Corporations -- Directors -- Duties -- Business judgment rule -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Corporations and associations law -- Corporations -- Directors -- Duties -- Fiduciary duties -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Insolvency law -- Proposals -- Court approval -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Administrative law -- Natural justice -- Reasonable apprehension of bias -- Appeal from endorsement reported at [2005] O.J. No. 729 and reasons for judgment reported at [2005] O.J. No. 730 allowed.

Application by two former directors of Stelco for leave to appeal and appeal from the order of their removal from the board of directors. Stelco was engaged in an extensive economic restructuring while under statutory insolvency protection that involved court-appointed capital raising via a competitive bid process. The appellants were involved with two companies that purchased approximately 20 per cent of Stelco's publicly traded shares during the protection period and were subsequently appointed to its board of directors to fill vacancies caused by resignations. As part of the appointment process, the appellants were informed of their fiduciary duties and agreed that their companies would have no further involvement in the competitive bid process. Stelco's employees sought the appellants' removal from the board on the basis that the participation of two major

shareholder representatives would tilt the evaluation of the bids in favour of maximizing shareholder value at the expense of bids more favourable to the interests of the employees. The motions judge held that the involvement of the appellants on the board raised an unnecessary risk that their future conduct potentially jeopardized the integrity and neutrality of the capital raising process, and declared the appointments to be of no force and effect. The judge cited the inherent jurisdiction of the court as the basis for the order. The appellants submitted that the judge had no jurisdiction to make a removal order, and in the alternative, he erred in applying a reasonable bias test to the removal of directors. The appellants further submitted that the judge erred by interfering with the board's exercise of business judgment, and that the facts did not justify the removal order.

HELD: Application for leave and appeal allowed. The judge misconstrued his authority, and made an order that he was not empowered to make. The court had no statutory or inherent authority to interfere with the composition of the board of directors. The judge erred in declining to give effect to the business judgment rule, and was not entitled to usurp the role of the directors and management in conducting the company's restructuring efforts. The record did not support a finding that there was sufficient risk of misconduct to warrant a conclusion of oppression, nor was the level of such risk assessed. There was no statutory principle that envisaged screening the neutrality of the appellants in advance of their appointment to the board of Stelco. Legal remedies were available to the employees of Stelco in the event that the appellants engaged in conduct that breached their legal obligations to the corporation. The applicability of such remedies was dependent on actual misconduct rather than mere speculation. Therefore, an apprehension of bias approach was not appropriate in the corporate law context.

Statutes, Regulations and Rules Cited:

Canada Business Corporations Act ss. 1, 102, 106(3), 109(1), 111, 122(1)(a), 122(1)(b), 145, 145(2)(b), 241, 241(3)(e)

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 As Amended, ss. 11, 11(1), 11(3), 11(4), 11(6), 20

Appeal From:

Application for Leave to Appeal, and if leave be granted, an appeal from the order of Farley J. dated February 25, 2005 removing the applicants as directors of Stelco Inc., reported at: [2005] O.J. No. 729.

Counsel:

Jeffrey S. Leon and Richard B. Swan, for the appellants, Michael Woollcombe and Roland Keiper

Kenneth T. Rosenberg and Robert A. Centa, for the respondent United Steelworkers of America

Murray Gold and Andrew J. Hatnay, for the respondent Retired Salaried Beneficiaries of Stelco Inc., CHT Steel Company Inc., Stelpipe Ltd., Stelwire Ltd. and Welland Pipe Ltd.

Michael C.P. McCreary and Carrie L. Clynick, for USWA Locals 5328 and 8782

John R. Varley, for the Active Salaried Employee Representative

Michael Barrack, for Stelco Inc.

Peter Griffin, for the Board of Directors of Stelco Inc.

K. Mahar, for the Monitor

David R. Byers, for CIT Business Credit, Agent for the DIP Lender

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The judgment of the Court was delivered by

R.A. BLAIR J.A.:--

PART I - INTRODUCTION

1 Stelco Inc. and four of its wholly owned subsidiaries obtained protection from their creditors under the Companies' Creditors Arrangement Act[1] on January 29, 2004. Since that time, the Stelco Group has been engaged in a high profile, and sometimes controversial, process of economic restructuring. Since October 2004, the restructuring has revolved around a court-approved capital raising process which, by February 2005, had generated a number of competitive bids for the Stelco Group.

2 Farley J., an experienced judge of the Superior Court Commercial List in Toronto, has been supervising the CCAA process from the outset.

3 The appellants, Michael Woollcombe and Roland Keiper, are associated with two companies - Clearwater Capital Management Inc., and Equilibrium Capital Management Inc. - which, respectively, hold approximately 20% of the outstanding publicly traded common shares of Stelco. Most of these shares have been acquired while the CCAA process has been ongoing, and Messrs. Woollcombe and Keiper have made it clear publicly that they believe there is good shareholder value in Stelco in spite of the restructuring. The reason they are able to take this position is that there has been a solid turn around in worldwide steel markets, as a result of which Stelco, although remaining in insolvency protection, is earning annual operating profits.

4 The Stelco board of directors ("the Board") has been depleted as a result of resignations, and in January of this year Messrs. Woollcombe and Keiper expressed an interest in being appointed to the Board. They were supported in this request by other shareholders who, together with Clearwater and Equilibrium, represent about 40% of the Stelco common shareholders. On February 18, 2005, the Board appointed the appellants directors. In announcing the appointments publicly, Stelco said in a press release:

> After careful consideration, and given potential recoveries at the end of the company's restructuring process, the Board responded favourably to the requests by making the appointments announced today.
>
> Richard Drouin, Chairman of Stelco's Board of Directors, said: "I'm pleased to welcome Roland Keiper and Michael Woollcombe to the Board. Their experience and their perspective will assist the Board as it strives to serve the best interests of all our stakeholders. We look forward to their positive contribution."

5 On the same day, the Board began its consideration of the various competing bids that had been received through the capital raising process.

6 The appointments of the appellants to the Board incensed the employee stakeholders of Stelco ("the Employees"), represented by the respondent Retired Salaried Beneficiaries of Stelco and the respondent United Steelworkers of America ("USWA"). Outstanding pension liabilities to current and retired employees are said to be Stelco's largest long-term liability - exceeding several billion dollars. The Employees perceive they do not have the same, or very much, economic leverage in what has sometimes been referred to as 'the bare knuckled arena' of the restructuring process. At the same time, they are amongst the most financially vulnerable stakeholders in the piece. They see the appointments of Messrs. Woollcombe and Keiper to the Board as a threat to their well being in the restructuring process, because the appointments provide the appellants, and the shareholders they represent, with direct access to sensitive information relating to the competing bids to which other stakeholders (including themselves) are not privy.

7 The Employees fear that the participation of the two major shareholder representatives will tilt the bid process in favour of maximizing shareholder value at the expense of bids that might be more favourable to the interests of the Employees. They sought and obtained an order from Farley J. removing Messrs. Woollcombe and Keiper from their short-lived position of directors, essentially on the basis of that apprehension.

8 The Employees argue that there is a reasonable apprehension the appellants would not be able to act in the best interests of the corporation - as opposed to their own best interests as shareholders - in considering the bids. They say this is so because of prior public statements by the appellants about enhancing shareholder value in Stelco, because of the appellants' linkage to such a large

shareholder group, because of their earlier failed bid in the restructuring, and because of their opposition to a capital proposal made in the proceeding by Deutsche Bank (known as "the Stalking Horse Bid"). They submit further that the appointments have poisoned the atmosphere of the restructuring process, and that the Board made the appointments under threat of facing a potential shareholders' meeting where the members of the Board would be replaced en masse.

9 On the other hand, Messrs. Woollcombe and Keiper seek to set aside the order of Farley J. on the grounds that (a) he did not have the jurisdiction to make the order under the provisions of the CCAA, (b) even if he did have jurisdiction, the reasonable apprehension of bias test applied by the motion judge has no application to the removal of directors, (c) the motion judge erred in interfering with the exercise by the Board of its business judgment in filling the vacancies on the Board, and (d) the facts do not meet any test that would justify the removal of directors by a court in any event.

10 For the reasons that follow, I would grant leave to appeal, allow the appeal, and order the reinstatement of the applicants to the Board.

PART II - ADDITIONAL FACTS

11 Before the initial CCAA order on January 29, 2004, the shareholders of Stelco had last met at their annual general meeting on April 29, 2003. At that meeting they elected eleven directors to the Board. By the date of the initial order, three of those directors had resigned, and on November 30, 2004, a fourth did as well, leaving the company with only seven directors.

12 Stelco's articles provide for the Board to be made up of a minimum of ten and a maximum of twenty directors. Consequently, after the last resignation, the company's corporate governance committee began to take steps to search for new directors. They had not succeeded in finding any prior to the approach by the appellants in January 2005.

13 Messrs. Woollcombe and Keiper had been accumulating shares in Stelco and had been participating in the CCAA proceedings for some time before their request to be appointed to the Board, through their companies, Clearwater and Equilibrium. Clearwater and Equilibrium are privately held, Ontario-based, investment management firms. Mr. Keiper is the president of Equilibrium and associated with Clearwater. Mr. Woollcombe is a consultant to Clearwater. The motion judge found that they "come as a package."

14 In October 2004, Stelco sought court approval of its proposed method of raising capital. On October 19, 2004, Farley J. issued what has been referred to as the Initial Capital Process Order. This order set out a process by which Stelco, under the direction of the Board, would solicit bids, discuss the bids with stakeholders, evaluate the bids, and report on the bids to the court.

15 On November 9, 2004, Clearwater and Equilibrium announced they had formed an investor group and had made a capital proposal to Stelco. The proposal involved the raising of $125 million through a rights offering. Mr. Keiper stated at the time that he believed "the value of Stelco's equity

would have the opportunity to increase substantially if Stelco emerged from CCAA while minimizing dilution of its shareholders." The Clearwater proposal was not accepted.

16 A few days later, on November 14, 2004, Stelco approved the Stalking Horse Bid. Clearwater and Equilibrium opposed the Deutsche Bank proposal. Mr. Keiper criticized it for not providing sufficient value to existing shareholders. However, on November 29, 2004, Farley J. approved the Stalking Horse Bid and amended the Initial Capital Process Order accordingly. The order set out the various channels of communication between Stelco, the monitor, potential bidders and the stakeholders. It provided that members of the Board were to see the details of the different bids before the Board selected one or more of the offers.

17 Subsequently, over a period of two and a half months, the shareholding position of Clearwater and Equilibrium increased from approximately 5% as at November 19, to 14.9% as at January 25, 2005, and finally to approximately 20% on a fully diluted basis as at January 31, 2005. On January 25, Clearwater and Equilibrium announced that they had reached an understanding jointly to pursue efforts to maximize shareholder value at Stelco. A press release stated:

> Such efforts will include seeking to ensure that the interests of Stelco's equity holders are appropriately protected by its board of directors and, ultimately, that Stelco's equity holders have an appropriate say, by vote or otherwise, in determining the future course of Stelco.

18 On February 1, 2005, Messrs. Keiper and Woollcombe and others representatives of Clearwater and Equilibrium, met with Mr. Drouin and other Board members to discuss their views of Stelco and a fair outcome for all stakeholders in the proceedings. Mr. Keiper made a detailed presentation, as Mr. Drouin testified, "encouraging the Board to examine how Stelco might improve its value through enhanced disclosure and other steps." Mr. Keiper expressed confidence that "there was value to the equity of Stelco," and added that he had backed this view up by investing millions of dollars of his own money in Stelco shares. At that meeting, Clearwater and Equilibrium requested that Messrs. Woollcombe and Keiper be added to the Board and to Stelco's restructuring committee. In this respect, they were supported by other shareholders holding about another 20% of the company's common shares.

19 At paragraphs 17 and 18 of his affidavit, Mr. Drouin, summarized his appraisal of the situation:

> 17. It was my assessment that each of Mr. Keiper and Mr. Woollcombe had personal qualities which would allow them to make a significant contribution to the Board in terms of their backgrounds and their knowledge of the steel industry generally and Stelco in particular. In addition I was aware that their appointment to the Board was supported by approximately 40% of the shareholders. In the event that these shareholders successfully requisitioned a shareholders meeting they were in a position to determine the composition of the entire Board.

18. I considered it essential that there be continuity of the Board through the CCAA process. I formed the view that the combination of existing Board members and these additional members would provide Stelco with the most appropriate board composition in the circumstances. The other members of the Board also shared my views.

20 In order to ensure that the appellants understood their duties as potential Board members and, particularly that "they would no longer be able to consider only the interests of shareholders alone but would have fiduciary responsibilities as a Board member to the corporation as a whole," Mr. Drouin and others held several further meetings with Mr. Woollcombe and Mr. Keiper. These discussions "included areas of independence, standards, fiduciary duties, the role of the Board Restructuring Committee and confidentiality matters." Mr. Woollcombe and Mr. Keiper gave their assurances that they fully understood the nature and extent of their prospective duties, and would abide by them. In addition, they agreed and confirmed that:

a) Mr. Woollcombe would no longer be an advisor to Clearwater and Equilibrium with respect to Stelco;
b) Clearwater and Equilibrium would no longer be represented by counsel in the CCAA proceedings; and
c) Clearwater and Equilibrium then had no involvement in, and would have no future involvement, in any bid for Stelco.

21 On the basis of the foregoing - and satisfied "that Messrs. Keiper and Woollcombe would make a positive contribution to the various issues before the Board both in [the] restructuring and the ongoing operation of the business" - the Board made the appointments on February 18, 2005.

22 Seven days later, the motion judge found it "appropriate, just, necessary and reasonable to declare" those appointments "to be of no force and effect" and to remove Messrs. Woollcombe and Keiper from the Board. He did so not on the basis of any actual conduct on the part of the appellants as directors of Stelco but because there was some risk of anticipated conduct in the future. The gist of the motion judge's rationale is found in the following passage from his reasons (at para. 23):

> In these particular circumstances and aside from the Board feeling coerced into the appointments for the sake of continuing stability, I am not of the view that it would be appropriate to wait and see if there was any explicit action on behalf of K and W while conducting themselves as Board members which would demonstrate that they had not lived up to their obligations to be "neutral." They may well conduct themselves beyond reproach. But if they did not, the fallout would be very detrimental to Stelco and its ability to successfully emerge. What would happen to the bids in such a dogfight? I fear that it would be trying to put Humpty Dumpty back together again. The same situation would prevail even if K and W conducted themselves beyond reproach but with the Board continuing to

be concerned that they not do anything seemingly offensive to the bloc. The risk to the process and to Stelco in its emergence is simply too great to risk the wait and see approach.

PART III - LEAVE TO APPEAL

23 Because of the "real time" dynamic of this restructuring project, Laskin J.A. granted an order on March 4, 2005, expediting the appellants' motion for leave to appeal, directing that it be heard orally and, if leave be granted, directing that the appeal be heard at the same time. The leave motion and the appeal were argued together, by order of the panel, on March 18, 2005.

24 This court has said that it will only sparingly grant leave to appeal in the context of a CCAA proceeding and will only do so where there are "serious and arguable grounds that are of real and significant interest to the parties": Country Style Food Services Inc. (Re), (2002) 158 O.A.C. 30; [2002] O.J. No. 1377 (C.A.), at para. 15. This criterion is determined in accordance with a four-pronged test, namely,

a) whether the point on appeal is of significance to the practice;
b) whether the point is of significance to the action;
c) whether the appeal is prima facie meritorious or frivolous;
d) whether the appeal will unduly hinder the progress of the action.

25 Counsel agree that (d) above is not relevant to this proceeding, given the expedited nature of the hearing. In my view, the tests set out in (a) - (c) are met in the circumstances, and as such, leave should be granted. The issue of the court's jurisdiction to intervene in corporate governance issues during a CCAA restructuring, and the scope of its discretion in doing so, are questions of considerable importance to the practice and on which there is little appellate jurisprudence. While Messrs. Woollcombe and Keiper are pursuing their remedies in their own right, and the company and its directors did not take an active role in the proceedings in this court, the Board and the company did stand by their decision to appoint the new directors at the hearing before the motion judge and in this court, and the question of who is to be involved in the Board's decision making process continues to be of importance to the CCAA proceedings. From the reasons that follow it will be evident that in my view the appeal has merit.

26 Leave to appeal is therefore granted.

PART IV - THE APPEAL

The Positions of the Parties

27 The appellants submit that,

a) in exercising its discretion under the CCAA, the court is not exercising its

"inherent jurisdiction" as a superior court;

b) there is no jurisdiction under the CCAA to remove duly elected or appointed directors, notwithstanding the broad discretion provided by s. 11 of that Act; and that,

c) even if there is jurisdiction, the motion judge erred:

(i) by relying upon the administrative law test for reasonable apprehension of bias in determining that the directors should be removed;

(ii) by rejecting the application of the "business judgment" rule to the unanimous decision of the Board to appoint two new directors; and,

(iii) by concluding that Clearwater and Equilibrium, the shareholders with whom the appellants are associated, were focussed solely on a short-term investment horizon, without any evidence to that effect, and therefore concluding that there was a tangible risk that the appellants would not be neutral and act in the best interests of Stelco and all stakeholders in carrying out their duties as directors.

28 The respondents' arguments are rooted in fairness and process. They say, first, that the appointment of the appellants as directors has poisoned the atmosphere of the CCAA proceedings and, secondly, that it threatens to undermine the even-handedness and integrity of the capital raising process, thus jeopardizing the ability of the court at the end of the day to approve any compromise or arrangement emerging from that process. The respondents contend that Farley J. had jurisdiction to ensure the integrity of the CCAA process, including the capital raising process Stelco had asked him to approve, and that this court should not interfere with his decision that it was necessary to remove Messrs. Woollcombe and Keiper from the Board in order to ensure the integrity of that process. A judge exercising a supervisory function during a CCAA proceeding is owed considerable deference: Algoma Steel Inc. (2001), 25 C.B.R. (4th) 194, at para. 8.

29 The crux of the respondents' concern is well-articulated in the following excerpt from paragraph 72 of the factum of the Retired Salaried Beneficiaries:

> The appointments of Keiper and Woollcombe violated every tenet of fairness in the restructuring process that is supposed to lead to a plan of arrangement. One stakeholder group - particular investment funds that have acquired Stelco shares during the CCAA itself - have been provided with privileged access to the capital raising process, and voting seats on the Corporation's Board of Directors and Restructuring Committee. No other stakeholder has been treated in remotely the same way. To the contrary, the salaried retirees have been completely excluded from the capital raising process and have no say whatsoever in the Corporation's decision-making process.

30 The respondents submit that fairness, and the perception of fairness, underpin the CCAA process, and depend upon effective judicial supervision: see Olympia & York Development Ltd. v. Royal Trust (1993), 12 O.R. (3d) 500 (Gen. Div.); Re Ivaco Inc., (2004), 3 C.B.R. (5th) 33, at para. 15-16. The motion judge reasonably decided to remove the appellants as directors in the circumstances, they say, and this court should not interfere.

Jurisdiction

31 The motion judge concluded that he had the power to rescind the appointments of the two directors on the basis of his "inherent jurisdiction" and "the discretion given to the court pursuant to the CCAA." He was not asked to, nor did he attempt to rest his jurisdiction on other statutory powers imported into the CCAA.

32 The CCAA is remedial legislation and is to be given a liberal interpretation to facilitate its objectives: Babcock & Wilcox Canada Ltd. (Re), [2000] O.J. No. 786 (Sup. Ct.) at para. 11. See also, Re Chef Ready Foods Ltd. (1990), 4 C.B.R. (3d) 311 (B.C.C.A.) at p. 320; Re Lehndorff General Partners Ltd. (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div.). Courts have adopted this approach in the past to rely on inherent jurisdiction, or alternatively on the broad jurisdiction under s. 11 of the CCAA, as the source of judicial power in a CCAA proceeding to "fill in the gaps" or to "put flesh on the bones" of that Act: see Re Dylex Ltd. (1995), 31 C.B.R. (3d) 106 (Ont. Gen Div. [Commercial List]), Royal Oak Mines Inc. (Re) (1999), 7 C.B.R. (4th) 293 (Ont. Gen Div. [Commercial List]); and Westar Mining Ltd. (Re) (1992), 70 B.C.L.R. (2d) 6 (B.C.S.C.).

33 It is not necessary, for purposes of this appeal, to determine whether inherent jurisdiction is excluded for all supervisory purposes under the CCAA, by reason of the existence of the statutory discretionary regime provided in that Act. In my opinion, however, the better view is that in carrying out his or her supervisory functions under the legislation, the judge is not exercising inherent jurisdiction but rather the statutory discretion provided by s. 11 of the CCAA and supplemented by other statutory powers that may be imported into the exercise of the s. 11 discretion from other statutes through s. 20 of the CCAA.

Inherent Jurisdiction

34 Inherent jurisdiction is a power derived "from the very nature of the court as a superior court of law," permitting the court "to maintain its authority and to prevent its process being obstructed and abused." It embodies the authority of the judiciary to control its own process and the lawyers and other officials connected with the court and its process, in order "to uphold, to protect and to fulfill the judicial function of administering justice according to law in a regular, orderly and effective manner." See I.H. Jacob, "The Inherent Jurisdiction of the Court" (1970), 23 Current Legal Problems 27-28. In Halsbury's Laws of England, 4th ed. (London: Lexis-Nexis UK, 1973 -) vol. 37, at para. 14, the concept is described as follows:

> In sum, it may be said that the inherent jurisdiction of the court is a virile and

> viable doctrine, and has been defined as being the reserve or fund of powers, a residual source of powers, which the court may draw upon as necessary whenever it is just or equitable to do so, in particularly to ensure the observation of the due process of law, to prevent improper vexation or oppression, to do justice between the parties and to secure a fair trial between them.

35 In spite of the expansive nature of this power, inherent jurisdiction does not operate where Parliament or the Legislature has acted. As Farley J. noted in Royal Oak Mines, supra, inherent jurisdiction is "not limitless; if the legislative body has not left a functional gap or vacuum, then inherent jurisdiction should not be brought into play" (para. 4). See also, Baxter Student Housing Ltd. v. College Housing Cooperative Ltd., [1976] 2 S.C.R. 475 (S.C.C.) at 480; Richtree Inc. (Re), [2005] O.J. No. 251 (Sup. Ct.).

36 In the CCAA context, Parliament has provided a statutory framework to extend protection to a company while it holds its creditors at bay and attempts to negotiate a compromised plan of arrangement that will enable it to emerge and continue as a viable economic entity, thus benefiting society and the company in the long run, along with the company's creditors, shareholders, employees and other stakeholders. The s. 11 discretion is the engine that drives this broad and flexible statutory scheme, and that for the most part supplants the need to resort to inherent jurisdiction. In that regard, I agree with the comment of Newbury J.A. in Clear Creek Contracting Ltd. v. Skeena Cellulose Inc., [2003] B.C.J. No. 1335 (B.C.C.A.), (2003) 43 C.B.R. (4th) 187 at para. 46, that:

> ... the court is not exercising a power that arises from its nature as a superior court of law, but is exercising the discretion given to it by the CCAA. ... This is the discretion, given by s. 11, to stay proceedings against the debtor corporation and the discretion, given by s. 6, to approve a plan which appears to be reasonable and fair, to be in accord with the requirements and objects of the statute, and to make possible the continuation of the corporation as a viable entity. It is these considerations the courts have been concerned with in the cases discussed above,[2] rather than the integrity of their own process.

37 As Jacob observes, in his article "The Inherent Jurisdiction of the Court," supra, at p. 25:

> The inherent jurisdiction of the court is a concept which must be distinguished from the exercise of judicial discretion. These two concepts resemble each other, particularly in their operation, and they often appear to overlap, and are therefore sometimes confused the one with the other. There is nevertheless a vital juridical distinction between jurisdiction and discretion, which must always be observed.

38 I do not mean to suggest that inherent jurisdiction can never apply in a CCAA context. The court retains the ability to control its own process, should the need arise. There is a distinction, however - difficult as it may be to draw - between the court's process with respect to the

restructuring, on the one hand, and the course of action involving the negotiations and corporate actions accompanying them, which are the company's process, on the other hand. The court simply supervises the latter process through its ability to stay, restrain or prohibit proceedings against the company during the plan negotiation period "on such terms as it may impose."[3] Hence the better view is that a judge is generally exercising the court's statutory discretion under s. 11 of the Act when supervising a CCAA proceeding. The order in this case could not be founded on inherent jurisdiction because it is designed to supervise the company's process, not the court's process.

The Section 11 Discretion

39 This appeal involves the scope of a supervisory judge's discretion under s. 11 of the CCAA, in the context of corporate governance decisions made during the course of the plan negotiating and approval process and, in particular, whether that discretion extends to the removal of directors in that environment. In my view, the s. 11 discretion - in spite of its considerable breadth and flexibility - does not permit the exercise of such a power in and of itself. There may be situations where a judge in a CCAA proceeding would be justified in ordering the removal of directors pursuant to the oppression remedy provisions found in s. 241 of the CBCA, and imported into the exercise of the s. 11 discretion through s. 20 of the CCAA. However, this was not argued in the present case, and the facts before the court would not justify the removal of Messrs. Woollcombe and Keiper on oppression remedy grounds.

40 The pertinent portions of s. 11 of the CCAA provide as follows:

Powers of court	11(1) Notwithstanding anything in the Bankruptcy and Insolvency Act or the Winding-up Act, where an application is made under this Act in respect of a company, the court, on the application of any person interested in the matter, may, subject to this Act, on notice to any other person or without notice as it may see fit, make an order under this section.
Initial application court orders	(3) A court may, on an initial application in respect of a company, make an order on such terms as it may impose, effective for such period as the court deems necessary not exceeding thirty days.

(a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the

commencement of or proceeding with any other action, suit or proceeding against the company.

Other than initial application court orders

(4) A court may, on an application in respect of a company other than an initial application, make an order on such terms as it may impose.

(a) staying, until otherwise ordered by the court, for such period as the court deems necessary, all proceedings taken or that might be taken in respect of the company under an Act referred to in subsection (1);
(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
(c) prohibiting, until otherwise ordered by the court, the commencement of or proceeding with any other action, suit or proceeding against the company.

Burden of proof on application

(6) The court shall not make an order under subsection (3) or (4) unless

(a) the applicant satisfies the court that circumstances exist that make such an order appropriate; and
(b) in the case of an order under subsection (4), the applicant also satisfied the court that the applicant has acted, and is acting, in good faith and with due diligence.

41 The rule of statutory interpretation that has now been accepted by the Supreme Court of Canada, in such cases as R. v. Sharpe, [2001] 1 S.C.R. 45, at para. 33, and Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27, at para. 21 is articulated in E.A. Driedger, The Construction of Statutes, 2nd ed. (Toronto: Butterworths, 1983) as follows:

> Today, there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

See also Ruth Sullivan, Sullivan and Driedger on the Construction of Statutes, 4th ed. (Toronto: Butterworths, 2002) at page 262.

42 The interpretation of s. 11 advanced above is true to these principles. It is consistent with the purpose and scheme of the CCAA, as articulated in para. 38 above, and with the fact that corporate governance matters are dealt with in other statutes. In addition, it honours the historical reluctance of courts to intervene in such matters, or to second-guess the business decisions made by directors and officers in the course of managing the business and affairs of the corporation.

43 Mr. Leon and Mr. Swan argue that matters relating to the removal of directors do not fall within the court's discretion under s. 11 because they fall outside of the parameters of the court's role in the restructuring process, in contrast to the company's role in the restructuring process. The court's role is defined by the "on such terms as may be imposed" jurisdiction under subparagraphs 11(3)(a)-(c) and 11(4)(a)-(c) of the CCAA to stay, or restrain, or prohibit proceedings against the company during the "breathing space" period for negotiations and a plan. I agree.

44 What the court does under s. 11 is to establish the boundaries of the playing field and act as a referee in the process. The company's role in the restructuring, and that of its stakeholders, is to work out a plan or compromise that a sufficient percentage of creditors will accept and the court will approve and sanction. The corporate activities that take place in the course of the workout are governed by the legislation and legal principles that normally apply to such activities. In the course of acting as referee, the court has great leeway, as Farley J. observed in Lehndorff, supra, at para. 5, "to make order[s] so as to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors." But the s. 11 discretion is not open-ended and unfettered. Its exercise must be guided by the scheme and object of the Act and by the legal principles that govern corporate law issues. Moreover, the court is not entitled to usurp the role of the directors and management in conducting what are in substance the company's restructuring efforts.

45 With these principles in mind, I turn to an analysis of the various factors underlying the interpretation of the s. 11 discretion.

46 I start with the proposition that at common law directors could not be removed from office during the term for which they were elected or appointed: London Finance Corporation Limited v. Banking Service Corporation Limited (1923), 23 O.W.N. 138 (Ont. H.C.); Stephenson v. Vokes (1896), 27 O.R. 691 (Ont. H.C.). The authority to remove must therefore be found in statute law.

47 In Canada, the CBCA and its provincial equivalents govern the election, appointment and removal of directors, as well as providing for their duties and responsibilities. Shareholders elect directors, but the directors may fill vacancies that occur on the board of directors pending a further shareholders meeting: CBCA, ss. 106(3) and 111.[4] The specific power to remove directors is vested in the shareholders by s. 109(1) of the CBCA. However, s. 241 empowers the court - where it finds that oppression as therein defined exists - to "make any interim or final order it thinks fit," including (s. 241(3)(e)) "an order appointing directors in place of or in addition to all or any of the directors

then in office." This power has been utilized to remove directors, but in very rare cases, and only in circumstances where there has been actual conduct rising to the level of misconduct required to trigger oppression remedy relief: see, for example, Catalyst Fund General Partner I Inc. v. Hollinger Inc., [2004] O.J. No. 4722.

48 There is therefore a statutory scheme under the CBCA (and similar provincial corporate legislation) providing for the election, appointment, and removal of directors. Where another applicable statute confers jurisdiction with respect to a matter, a broad and undefined discretion provided in one statute cannot be used to supplant or override the other applicable statute. There is no legislative "gap" to fill. See Baxter Student Housing Ltd. v. College Housing Cooperative Ltd., supra, at p. 480; Royal Oak Mines Inc. (Re), supra; and Richtree Inc. (Re), supra.

49 At paragraph 7 of his reasons, the motion judge said:

> The board is charged with the standard duty of "manage[ing], [sic] or supervising the management, of the business and affairs of the corporation": s. 102(1) CBCA. *Ordinarily the Court will not interfere with the composition of the board of directors. However, if there is good and sufficient valid reason to do so, then the Court must not hesitate to do so to correct a problem.* The directors should not be required to constantly look over their shoulders for this would be the sure recipe for board paralysis which would be so detrimental to a restructuring process; thus interested parties should only initiate a motion where it is reasonably obvious that there is a problem, actual or poised to become actual. [emphasis added]

50 Respectfully, I see no authority in s. 11 of the CCAA for the court to interfere with the composition of a board of directors on such a basis.

51 Court removal of directors is an exceptional remedy, and one that is rarely exercised in corporate law. This reluctance is rooted in the historical unwillingness of courts to interfere with the internal management of corporate affairs and in the court's well-established deference to decisions made by directors and officers in the exercise of their business judgment when managing the business and affairs of the corporation. These factors also bolster the view that where the CCAA is silent on the issue, the court should not read into the s. 11 discretion an extraordinary power - which the courts are disinclined to exercise in any event - except to the extent that that power may be introduced through the application of other legislation, and on the same principles that apply to the application of the provisions of the other legislation.

The Oppression Remedy Gateway

52 The fact that s. 11 does not itself provide the authority for a CCAA judge to order the removal of directors does not mean that the supervising judge is powerless to make such an order, however. Section 20 of the CCAA offers a gateway to the oppression remedy and other provisions of the

CBCA and similar provincial statutes. Section 20 states:

> The provisions of this Act may be applied together with the provisions of any Act of Parliament or of the legislature of any province that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them.

53 The CBCA is legislation that "makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them." Accordingly, the powers of a judge under s. 11 of the CCAA may be applied together with the provisions of the CBCA, including the oppression remedy provisions of that statute. I do not read s. 20 as limiting the application of outside legislation to the provisions of such legislation dealing specifically with the sanctioning of compromises and arrangements between the company and its shareholders. The grammatical structure of s. 20 mandates a broader interpretation and the oppression remedy is, therefore, available to a supervising judge in appropriate circumstances.

54 I do not accept the respondents' argument that the motion judge had the authority to order the removal of the appellants by virtue of the power contained in s. 145(2)(b) of the CBCA to make an order "declaring the result of the disputed election or appointment" of directors. In my view, s. 145 relates to the procedures underlying disputed elections or appointments, and not to disputes over the composition of the board of directors itself. Here, it is conceded that the appointment of Messrs. Woollcombe and Keiper as directors complied with all relevant statutory requirements. Farley J. quite properly did not seek to base his jurisdiction on any such authority.

The Level of Conduct Required

55 Colin Campbell J. recently invoked the oppression remedy to remove directors, without appointing anyone in their place, in Catalyst Fund General Partner I Inc. v. Hollinger Inc., supra. The bar is high. In reviewing the applicable law, C. Campbell J. said (para. 68):

> Director removal is *an extraordinary remedy* and certainly should be *imposed most sparingly*. As a starting point, I accept the basic proposition set out in Peterson, "Shareholder Remedies in Canada"[5]:
>
> > SS. 18.172 *Removing and appointing directors to the board is an extreme form of judicial intervention.* The board of directors is elected by the shareholders, vested with the power to manage the corporation, and appoints the officers of the company who undertake to conduct the day-to-day affairs of the corporation. [Footnote omitted.] It is clear that the board of directors has control over policymaking and management of the corporation. *By tampering with a board, a court directly affects the management of the corporation.* If a reasonable balance between

> protection of corporate stakeholders and the freedom of management to conduct the affairs of the business in an efficient manner is desired, altering the board of directors should be *a measure of last resort*. The order could be suitable where the continuing presence of the incumbent directors is harmful to both the company and the interests of corporate stakeholders, and where the appointment of a new director or directors would remedy the oppressive conduct without a receiver or receiver-manager. [emphasis added]

56 C. Campbell J. found that the continued involvement of the Ravelston directors in the Hollinger situation would "significantly impede" the interests of the public shareholders and that those directors were "motivated by putting their interests first, not those of the company" (paras. 82-83). The evidence in this case is far from reaching any such benchmark, however, and the record would not support a finding of oppression, even if one had been sought.

57 Everyone accepts that there is no evidence the appellants have conducted themselves, as directors - in which capacity they participated over two days in the bid consideration exercise - in anything but a neutral fashion, having regard to the best interests of Stelco and all of the stakeholders. The motion judge acknowledged that the appellants "may well conduct themselves beyond reproach." However, he simply decided there was a risk - a reasonable apprehension - that Messrs. Woollcombe and Keiper would not live up to their obligations to be neutral in the future.

58 The risk or apprehension appears to have been founded essentially on three things: (1) the earlier public statements made by Mr. Keiper about "maximizing shareholder value"; (2) the conduct of Clearwater and Equilibrium in criticizing and opposing the Stalking Horse Bid; and (3) the motion judge's opinion that Clearwater and Equilibrium - the shareholders represented by the appellants on the Board - had a "vision" that "usually does not encompass any significant concern for the long-term competitiveness and viability of an emerging corporation," as a result of which the appellants would approach their directors' duties looking to liquidate their shares on the basis of a "short-term hold" rather than with the best interests of Stelco in mind. The motion judge transposed these concerns into anticipated predisposed conduct on the part of the appellants as directors, despite their apparent understanding of their duties as directors and their assurances that they would act in the best interests of Stelco. He therefore concluded that "the risk to the process and to Stelco in its emergence [was] simply too great to risk the wait and see approach."

59 Directors have obligations under s. 122(1) of the CBCA (a) to act honestly and in good faith with a view to the best interest of the corporation (the "statutory fiduciary duty" obligation), and (b) to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances (the "duty of care" obligation). They are also subject to control under the oppression remedy provisions of s. 241. The general nature of these duties does not change when the company approaches, or finds itself in, insolvency: Peoples Department Stores Inc (Trustee of). v. Wise, [2004] S.C.J. No. 64 (S.C.C.) at paras. 42-49.

60 In Peoples the Supreme Court noted that "the interests of the corporation are not to be confused with the interests of the creditors or those of any other stakeholders" (para. 43), but also accepted "as an accurate statement of the law that in determining whether [directors] 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" (para. 42). Importantly as well - in the context of "the shifting interest and incentives of shareholders and creditors" - the court stated (para. 47):

> In resolving these competing interests, it is incumbent upon the directors to act honestly and in good faith with a view to the best interests of the corporation. In using their skills for the benefit of the corporation when it is in troubled waters financially, the directors must be careful to attempt to act in its best interests by creating a "better" corporation, and not to favour the interests of any one group of stakeholders.

61 In determining whether directors have fallen foul of those obligations, however, more than some risk of anticipated misconduct is required before the court can impose the extraordinary remedy of removing a director from his or her duly elected or appointed office. Although the motion judge concluded that there was a risk of harm to the Stelco process if Messrs Woollcombe and Keiper remained as directors, he did not assess the level of that risk. The record does not support a finding that there was a sufficient risk of sufficient misconduct to warrant a conclusion of oppression. The motion judge was not asked to make such a finding, and he did not do so.

62 The respondents argue that this court should not interfere with the decision of the motion judge on grounds of deference. They point out that the motion judge has been case-managing the restructuring of Stelco under the CCAA for over fourteen months and is intimately familiar with the circumstances of Stelco as it seeks to restructure itself and emerge from court protection.

63 There is no question that the decisions of judges acting in a supervisory role under the CCAA, and particularly those of experienced commercial list judges, are entitled to great deference: see Algoma Steel Inc. v. Union Gas Limited (2003), 63 O.R. (3d) 78 (C.A.), at para. 16. The discretion must be exercised judicially and in accordance with the principles governing its operation. Here, respectfully, the motion judge misconstrued his authority, and made an order that he was not empowered to make in the circumstances.

64 The appellants argued that the motion judge made a number of findings without any evidence to support them. Given my decision with respect to jurisdiction, it is not necessary for me to address that issue.

The Business Judgment Rule

65 The appellants argue as well that the motion judge erred in failing to defer to the unanimous

decision of the Stelco directors in deciding to appoint them to the Stelco Board. It is well-established that judges supervising restructuring proceedings - and courts in general - will be very hesitant to second-guess the business decisions of directors and management. As the Supreme Court of Canada said in Peoples, supra, at para. 67:

> Courts are ill-suited and should be reluctant to second-guess the application of business expertise to the considerations that are involved in corporate decision making ...

66 In Brant Investments Ltd. v. KeepRite Inc. (1991), 3 O.R. (3d) 289 (C.A.) at 320, this court adopted the following statement by the trial judge, Anderson J.:

> Business decisions, honestly made, should not be subjected to microscopic examination. There should be no interference simply because a decision is unpopular with the minority.[6]

67 McKinlay J.A then went on to say:

> There can be no doubt that on an application under s. 234[7] the trial judge is required to consider the nature of the impugned acts and the method in which they were carried out. That does not meant that the trial judge should substitute his own business judgment for that of managers, directors, or a committee such as the one involved in assessing this transaction. Indeed, it would generally be impossible for him to do so, regardless of the amount of evidence before him. He is dealing with the matter at a different time and place; it is unlikely that he will have the background knowledge and expertise of the individuals involved; he could have little or no knowledge of the background and skills of the persons who would be carrying out any proposed plan; and it is unlikely that he would have any knowledge of the specialized market in which the corporation operated. In short, he does not know enough to make the business decision required.

68 Although a judge supervising a CCAA proceeding develops a certain "feel" for the corporate dynamics and a certain sense of direction for the restructuring, this caution is worth keeping in mind. See also Clear Creek Contracting Ltd. v. Skeena Cellulose Inc., supra, Sammi Atlas Inc. (Re) (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div.); Olympia & York Developments Ltd. (Re), supra; Re Alberta Pacific Terminals Ltd. (1991), 8 C.B.R. (3d) 99 (B.C.S.C.). The court is not catapulted into the shoes of the board of directors, or into the seat of the chair of the board, when acting in its supervisory role in the restructuring.

69 Here, the motion judge was alive to the "business judgment" dimension in the situation he faced. He distinguished the application of the rule from the circumstances, however, stating at para. 18 of his reasons:

> With respect I do not see the present situation as involving the "management of the business and affairs of the corporation," but rather as a quasi-constitutional aspect of the corporation entrusted albeit to the Board pursuant to s. 111(1) of the CBCA. I agree that where a board is actually engaged in the business of a judgment situation, the board should be given appropriate deference. However, to the contrary in this situation, I do not see it as a situation calling for (as asserted) more deference, but rather considerably less than that. With regard to this decision of the Board having impact upon the capital raising process, as I conclude it would, then similarly deference ought not to be given.

70 I do not see the distinction between the directors' role in "the management of the business and affairs of the corporation" (CBCA, s. 102) - which describes the directors' overall responsibilities - and their role with respect to a "quasi-constitutional aspect of the corporation" (i.e. in filling out the composition of the board of directors in the event of a vacancy). The "affairs" of the corporation are defined in s. 1 of the CBCA as meaning "the relationships among a corporation, it affiliates and the shareholders, directors and officers of such bodies corporate but does not include the business carried on by such bodies corporate." Corporate governance decisions relate directly to such relationships and are at the heart of the Board's business decision-making role regarding the corporation's business and affairs. The dynamics of such decisions, and the intricate balancing of competing interests and other corporate-related factors that goes into making them, are no more within the purview of the court's knowledge and expertise than other business decisions, and they deserve the same deferential approach. Respectfully, the motion judge erred in declining to give effect to the business judgment rule in the circumstances of this case.

71 This is not to say that the conduct of the Board in appointing the appellants as directors may never come under review by the supervising judge. The court must ultimately approve and sanction the plan of compromise or arrangement as finally negotiated and accepted by the company and its creditors and stakeholders. The plan must be found to be fair and reasonable before it can be sanctioned. If the Board's decision to appoint the appellants has somehow so tainted the capital raising process that those criteria are not met, any eventual plan that is put forward will fail.

72 The respondents submit that it makes no sense for the court to have jurisdiction to declare the process flawed only after the process has run its course. Such an approach to the restructuring process would be inefficient and a waste of resources. While there is some merit in this argument, the court cannot grant itself jurisdiction where it does not exist. Moreover, there are a plethora of checks and balances in the negotiating process itself that moderate the risk of the process becoming irretrievably tainted in this fashion - not the least of which is the restraining effect of the prospect of such a consequence. I do not think that this argument can prevail. In addition, the court at all times retains its broad and flexible supervisory jurisdiction - a jurisdiction which feeds the creativity that makes the CCAA work so well - in order to address fairness and process concerns along the way. This case relates only to the court's exceptional power to order the removal of directors.

The Reasonable Apprehension of Bias Analogy

73 In exercising what he saw as his discretion to remove the appellants as directors, the motion judge thought it would be useful to "borrow the concept of reasonable apprehension of bias ... with suitable adjustments for the nature of the decision making involved" (para. 8). He stressed that "there was absolutely no allegation against [Mr. Woollcombe and Mr. Keiper] of any actual 'bias' or its equivalent" (para. 8). He acknowledged that neither was alleged to have done anything wrong since their appointments as directors, and that at the time of their appointments the appellants had confirmed to the Board that they understood and would abide by their duties and responsibilities as directors, including the responsibility to act in the best interests of the corporation and not in their own interests as shareholders. In the end, however, he concluded that because of their prior public statements that they intended to "pursue efforts to maximize shareholder value at Stelco," and because of the nature of their business and the way in which they had been accumulating their shareholding position during the restructuring, and because of their linkage to 40% of the common shareholders, there was a risk that the appellants would not conduct themselves in a neutral fashion in the best interests of the corporation as directors.

74 In my view, the administrative law notion of apprehension of bias is foreign to the principles that govern the election, appointment and removal of directors, and to corporate governance considerations in general. Apprehension of bias is a concept that ordinarily applies to those who preside over judicial or quasi-judicial decision-making bodies, such as courts, administrative tribunals or arbitration boards. Its application is inapposite in the business decision-making context of corporate law. There is nothing in the CBCA or other corporate legislation that envisages the screening of directors in advance for their ability to act neutrally, in the best interests of the corporation, as a prerequisite for appointment.

75 Instead, the conduct of directors is governed by their common law and statutory obligations to act honestly and in good faith with a view to the best interests of the corporation, and to exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances (CBCA, s. 122(1)(a) and (b)). The directors also have fiduciary obligations to the corporation, and they are liable to oppression remedy proceedings in appropriate circumstances. These remedies are available to aggrieved complainants - including the respondents in this case - but they depend for their applicability on the director having engaged in conduct justifying the imposition of a remedy.

76 If the respondents are correct, and reasonable apprehension that directors may not act neutrally because they are aligned with a particular group of shareholders or stakeholders is sufficient for removal, all nominee directors in Canadian corporations, and all management directors, would automatically be disqualified from serving. No one suggests this should be the case. Moreover, as Iacobucci J. noted in Blair v. Consolidated Enfield Corp., [1995] 4 S.C.R. 5 (S.C.C.) at para. 35, "persons are assumed to act in good faith unless proven otherwise." With respect, the motion judge approached the circumstances before him from exactly the opposite direction. It is commonplace in

corporate/commercial affairs that there are connections between directors and various stakeholders and that conflicts will exist from time to time. Even where there are conflicts of interest, however, directors are not removed from the board of directors; they are simply obliged to disclose the conflict and, in appropriate cases, to abstain from voting. The issue to be determined is not whether there is a connection between a director and other shareholders or stakeholders, but rather whether there has been some conduct on the part of the director that will justify the imposition of a corrective sanction. An apprehension of bias approach does not fit this sort of analysis.

PART V - DISPOSITION

77 For the foregoing reasons, then, I am satisfied that the motion judge erred in declaring the appointment of Messrs. Woollcombe and Keiper as directors of Stelco of no force and effect.

78 I would grant leave to appeal, allow the appeal and set aside the order of Farley J. dated February 25, 2005.

79 Counsel have agreed that there shall be no costs of the appeal.

R.A. BLAIR J.A.
S.T. GOUDGE J.A. - I agree.
K.N. FELDMAN J.A. - I agree.

cp/ln/e/qljxh/qlkjg/qlgxc/qlmlt

1 R.S.C. 1985, c. C-36, as amended.

2 The reference is to the decisions in Dyle, Royal Oak Mines, and Westar, cited above.

3 See paragraph 43, infra, where I elaborate on this distinction.

4 It is the latter authority that the directors of Stelco exercised when appointing the appellants to the Stelco Board.

5 Dennis H. Peterson, Shareholder Remedies in Canada (Markham: LexisNexis ' Butterworths ' Looseleaf Service, 1989) at 18-47.

6 Or, I would add, unpopular with other stakeholders.

7 Now s. 241.

Tab 4

Case Name:

Stelco Inc. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, C. c-36, as amended
AND IN THE MATTER OF a proposed plan of compromise or arrangement with respect to Stelco Inc. and the other applicants listed in Schedule "A"
APPLICATION UNDER the Companies' Creditors Arrangement Act, R.S.C. 1985, C. c-36, as amended

[2005] O.J. No. 4733

78 O.R. (3d) 254

204 O.A.C. 216

15 C.B.R. (5th) 288

143 A.C.W.S. (3d) 419

2005 CarswellOnt 6283

2005 CanLII 40140

Docket: M33099 (C44332)

Ontario Court of Appeal
Toronto, Ontario

J.I. Laskin, M. Rosenberg and H.S. LaForme JJ.A.

Heard: November 2, 2005.
Judgment: November 4, 2005.

(32 paras.)

Creditors & debtors law -- Legislation -- Debtors' relief -- Companies' Creditors Arrangement Act -- Appeal by debenture holders from orders, reported at [2005] O.J. No. 4309, approving

agreements involving steel company in bankruptcy protection, necessary for success of company's plan of arrangement, dismissed -- Motions judge had jurisdiction to make orders where power of debenture holders to vote down proposal preserved and agreements had support of other stakeholders and Monitor -- Companies' Creditors Arrangement Act, s. 11.

Insolvency law -- Proposals -- Court approval -- Appeal by debenture holders from orders approving agreements involving steel company in bankruptcy protection, necessary for success of company's plan of arrangement, dismissed -- Motions judge had jurisdiction to make orders where orders did not amount to approval of plan of arrangement -- Debentures holders' power to vote down proposed plan not usurped -- Companies' Creditors Arrangement Act, s. 11.

Application by a committee of senior debenture holders for leave to appeal from orders authorizing Stelco to enter into agreements with two stakeholders and a finance provider. A group of equity holders supported the application, while other stakeholders and the Monitor supported the orders. Stelco and its four subsidiaries obtained protection from their creditors in 1994. Stelco's attempts over twenty months to restructure were unsuccessful, in part because certain stakeholders continually exercised veto powers. Stelco's board of directors negotiated agreements with the stakeholders, the Ontario government and the steelworkers union, and Tricap Management, necessary to the success of Stelco's proposed plan of arrangement. The debenture holders objected to terms of the agreements providing for fees payable to Tricap and providing Ontario with power to accept or reject members of Stelco's board of directors. The debenture holders did not propose an alternate plan of arrangement, but made it clear they would not support the one on the table. The motions judge stated in his reasons he was not approving Stelco's plan, but did not think the plan was doomed to fail. He scheduled a meeting of creditors to vote on the plan for November 2005.

HELD: Application allowed. Leave to appeal was granted and the appeal was dismissed. Leave to appeal was granted because the debenture holders raised a novel and important point that was significant to the action. The appeal was prima facie meritorious, and would not unduly interfere with Stelco's continuing negotiations. The appeal was dismissed because the judge had jurisdiction to make the orders approving the agreements, as the orders did not usurp the debenture holders' power to ultimately decide on whether or not to approve Stelco's plan. It was open to the motions judge to find the plan was not doomed to fail, despite the position of the debenture holders, because of the support the plan had from other stakeholders and the Monitor.

Statute, Regulations and Rules Cited:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, ss. 6, 11, 11(4), 13

Appeal From:

On appeal from the orders of Justice James M. Farley of the Superior Court of Justice made on October 4, 2005.

Counsel:

Robert W. Staley and Alan P. Gardner for the Informal Committee of Senior Debentureholders, Appellants

Michael E. Barrack and Geoff R. Hall for Stelco Inc., Respondent

Robert I. Thornton and Kyla E.M. Mahar for the Monitor, Respondent

John R. Varley for Salaried Active Employees, Respondents

Michael C.P. McCreary and David P. Jacobs for USW Locals 8782 and 5328, Respondents

George Karayannides for EDS Canada Inc., Respondent

Aubrey E. Kauffman for Tricap Management Ltd., Respondents

Ben Zarnett and Gale Rubenstein for the Province of Ontario, Respondents

Murray Gold for Salaried Retirees, Respondents

Kenneth T. Rosenberg for USW International, Respondents

Robert A. Centa for USWA, Respondents

George Glezos for AGF Management Ltd., Respondents

The judgment of the Court was delivered by

1 **M. ROSENBERG J.A.**:-- This appeal is another chapter in the continuing attempt by Stelco Inc. and four of its wholly-owned subsidiaries to emerge from protection from their creditors under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36. The appellant, an Informal Committee of Senior Debenture Holders who are Stelco's largest creditor, applies for leave to appeal under s. 13 of the CCAA and if leave be granted appeals three orders made by Farley J. on October 4, 2005 in the CCAA proceedings. These orders authorize Stelco to enter into agreements with two of its stakeholders and a finance provider. The appellant submits that the motions judge had no jurisdiction to make these orders and that the effect of these orders is to distort or skew the CCAA process. A group of Stelco's equity holders support the submissions of the appellant. The various other players with a stake in the restructuring and the court-appointed Monitor support the orders made by the motions judge.

2 Given the urgency of the matter it is only possible to give relatively brief reasons for my conclusion that while leave to appeal should be granted, the appeal should be dismissed.

THE FACTS

3 Stelco Inc. and the four wholly-owned subsidiaries obtained protection from their creditors under the CCAA on January 29, 1994. Thus, the CCAA process has been going on for over twenty months, longer than anyone expected. Farley J. has been managing the process throughout. The initial order made under s. 11 of the CCAA gives Stelco sole and exclusive authority to propose and file a plan of arrangement with its creditors. To date, attempts to restructure have been unsuccessful. In particular, a plan put forward by the Senior Debt Holders failed.

4 While there have no doubt been many obstacles to a successful restructuring, the paramount problem appears to be that stakeholders, the Ontario government and Stelco's unions, who do not have a formal veto (i.e. they do not have a right to vote to approve any plan of arrangement and reorganization) have what the parties have referred to as a functional veto. It is unnecessary to set out the reasons for these functional vetoes. Suffice it to say, as did the Monitor in its Thirty-Eighth Report, that each of these stakeholders is "capable of exercising sufficient leverage against Stelco and other stakeholders such that no restructuring could be completed without that stakeholder's support".

5 In an attempt to successfully emerge from CCAA protection with a plan of arrangement, the Stelco board of directors has negotiated with two of these stakeholders and with a finance provider and has reached three agreements: an agreement with the provincial government (the Ontario Agreement), an agreement with The United Steelworkers International and Local 8782 (the USW Agreement), and an agreement with Tricap Management Limited (the Tricap Agreement). Those agreements are intrinsic to the success of the Plan of Arrangement that Stelco proposes. However, the debt holders including this appellant have the ultimate veto. They alone will vote on whether to approve Stelco's Plan. The vote of the affected debt holders is scheduled for November 15, 2005.

6 The three agreements have terms to which the appellant objects. For example, the Tricap Agreement contemplates a break fee of up to $10.75 million depending on the circumstances. Tricap will be entitled to a break fee if the Plan fails to obtain the requisite approvals or if Tricap terminates its obligations to provide financing as a result of the Plan being amended without Tricap's approval. Half of the break fee becomes payable if the Plan is voted down by the creditors. Another example is found in the Ontario Agreement, which provides that the order sanctioning the Final Plan shall name the members of Stelco's board of directors and such members must be acceptable to the province. Consistent with the Order of March 30, 2005 and as required by the terms of the agreements themselves, Stelco sought court authorization to enter into the three agreements. We were told that, in any event, it is common practice to seek court approval of agreements of this importance. The appellant submits that the motions judge had no jurisdiction to make these orders.

7 There are a number of other facts that form part of the context for understanding the issues raised by this appeal. First, on July 18, 2005, the motions judge extended the stay of proceedings until September 9, 2005 and warned the stakeholders that this was a "real and functional deadline". While that date has been extended because Stelco was making progress in its talks with the stakeholders, the urgency of the situation cannot be underestimated. Something will have to happen to either break the impasse or terminate the CCAA process.

8 Second, on October 4, 2005, the motions judge made several orders, not just the orders to authorize Stelco to enter into the three agreements to which the appellant objects. In particular, the motions judge extended the stay to December and made an order convening the creditors meeting on November 15th to approve the Stelco Plan. The appellant does not object to the orders extending the stay or convening the meeting to vote on the Plan.

9 Third, the appellant has not sought permission to prepare and file its own plan of arrangement. At present, the Stelco Board's Plan is the only plan on the table and as the motions judge observed, "one must realistically appreciate that a rival financing arrangement at this stage, starting from essentially a standing start, would take considerable time for due diligence and there is no assurance that the conditions will be any less onerous than those extracted by Tricap".

10 Fourth, in his orders authorizing Stelco to enter into these agreements, the motions judge made it clear that these authorizations, "are not a sanction of the terms of the plan ... and do not prohibit Stelco from continuing discussions in respect of the Plan with the Affected Creditors".

11 Fifth, the independent Monitor has reviewed the Agreements and the Plan and supports Stelco's position.

12 Finally, and importantly, the Senior Debenture Holders that make up the appellant have said unequivocally that they will not approve the Plan. The motions judge recognized this in his reasons:

> The Bondholder group has indicated that it is firmly opposed to the plan as presently constituted. That group also notes that more than half of the creditors by $ value have advised the Monitor that they are opposed to the plan as presently constituted. ... The present plan may be adjusted (with the blessing of others concerned) to the extent that it, in a revised form, is palatable to the creditors (assuming that they do not have a massive change of heart as to the presently proposed plan).

LEAVE TO APPEAL

13 The parties agree on the test for granting leave to appeal under s. 13 of the CCAA. The moving party must show the following:

(a) the point on appeal is of significance to the practice;

(b) the point is of significance to the action;
(c) the appeal is prima facie meritorious; and
(d) the appeal will not unduly hinder the progress of the action.

14 In my view, the appellant has met this test. The point raised is a novel and important one. It concerns the jurisdiction of the supervising judge to make orders that do not merely preserve the status quo but authorize key elements of the proposed plan of arrangement. The point is of obvious significance in this action. If the motions judge's approvals were to be set aside, it is doubtful that the Plan could proceed. On the other hand, the appellant submits that the orders have created a coercive and unfair environment and that the Plan is doomed to fail. It was therefore wrong to authorize Stelco to enter into agreements, especially the Tricap Agreement, that could further deplete the estate. The appeal is prima facie meritorious. The matter appears to be one of first impression. It certainly cannot be said that the appeal is frivolous. Finally, the appeal will not unduly hinder the progress of the action. Because of the speed with which this court is able to deal with the case, the appeal will not unduly interfere with the continuing negotiations prior to the November 15th meeting.

15 For these reasons, I would grant leave to appeal.

ANALYSIS

Jurisdiction generally

16 The thrust of the appellant's submissions is that while the judge supervising a CCAA process has jurisdiction to make orders that preserve the status quo, the judge has no jurisdiction to make an order that, in effect, entrenches elements of the proposed Plan. Rather, the approval of the Plan is a matter solely for the business judgement of the creditors. The appellant submits that the orders made by the motions judge are not authorized by the statute or under the court's inherent jurisdiction and are in fact inconsistent with the scheme and objects of the CCAA. They submit that the orders made in this case have the effect of substituting the court's judgment for that of the debt holders who, under s. 6, have exclusive jurisdiction to approve the plan. Under s. 6, it is only after a majority in number representing two-thirds in value of the creditors vote to approve the plan that the court has a role in deciding whether to sanction the plan.

17 Underlying this argument is a concern on the part of the creditors that the orders are coercive, designed to force the creditors to approve a plan, a plan in which they have had no input and of which they disapprove.

18 In my view, the motions judge had jurisdiction to make the orders he did authorizing Stelco to enter into the agreements. Section 11 of the CCAA provides a broad jurisdiction to impose terms and conditions on the granting of the stay. In my view, s. 11(4) includes the power to vary the stay and allow the company to enter into agreements to facilitate the restructuring, provided that the creditors have the final decision under s. 6 whether or not to approve the Plan. The court's

jurisdiction is not limited to preserving the status quo. The point of the CCAA process is not simply to preserve the status quo but to facilitate restructuring so that the company can successfully emerge from the process. This point was made by Gibbs J.A. in Hongkong Bank v. Chef Ready Foods (1990), 4 C.B.R. (3d) 311 (B.C.C.A.) at para. 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. [Emphasis added.]

19 In my view, provided the orders do not usurp the right of the creditors to decide whether to approve the Plan the motions judge had the necessary jurisdiction to make them. The orders made in this case do not usurp the s. 6 rights of the creditors and do not unduly interfere with the business judgement of the creditors. The orders move the process along to the point where the creditors are free to exercise their rights at the creditors' meeting.

20 The argument that the orders are coercive and therefore unreasonably interfere with the rights of the creditors turns largely on the potential $10.75 million break fee that may become payable to Tricap. However, the motions judge has found as a fact that the break fee is reasonable. As counsel for Ontario points out, this necessarily entails a finding that the break fee is not coercive even if it could to some extent deplete Stelco's assets.

21 Further, the motions judge both in his reasons and in his orders made it clear that he was not purporting to sanction the Plan. As he said in his reasons, "I wish to be absolutely clear that I am not ruling on or considering in any way the fairness of the plan as presented". The creditors will have the ultimate say on November 15th whether this plan will be approved.

Doomed to fail

22 The appellant submits that the motions judge had no jurisdiction to approve orders that would facilitate a Plan that is doomed to fail. The authorities indicate that a court should not approve a process that will lead to a plan that is doomed to fail. The appellant says that it has made it as clear as possible that it does not accept the proposed Plan and will vote against it. In Re Inducon Development Corp. (1991), 8 C.B.R. (3d) 306 (Ont. Ct. (Gen. Div.)) at 310 Farley J. said that, "It is of course, ... fruitless to proceed with a plan that is doomed to failure at a further stage."

23 However, it is important to take into account the dynamics of the situation. In fact, it is the appellant's position that nothing will happen until a vote on a Plan is imminent or a proposal from Stelco is voted down; only then will Stelco enter into realistic negotiations with its creditors. It is apparent that the motions judge is of the view that the Plan is not doomed to fail; he would not have approved steps to continue the process if he thought it was. As Austin J. said in Bargain Harold's Discount Ltd. v. Paribas Bank of Canada (1992), 7 O.R. (3d) 362 (Div. Ct.) at 369:

> The jurisprudence is clear that if it is obvious that no plan will be found acceptable to the required percentages of creditors, then the application should be refused. *The fact that Paribas, the Royal Bank and K Mart now say there is no plan that they would approve, does not put an end to the inquiry.* All affected constituencies must be considered, including secured, preferred and unsecured creditors, employees, landlords, shareholders, and the public generally ... [Emphasis added.]

24 It must be a matter of judgment for the supervising judge to determine whether the Plan is doomed to fail. This Plan is supported by the other stakeholders and the independent Monitor. It is a product of the business judgment of the Stelco board as a way out of the CCAA process. It was open to the motions judge to conclude that the plan was not doomed to fail and that the process should continue. Despite its opposition to the Plan, the appellant's position inherently concedes the possibility of success, otherwise these creditors would have opposed the extension of the stay, opposed the order setting a date for approval of the plan and sought to terminate the CCAA proceedings.

25 The motions judge said this in his reasons:

> It seems to me that Stelco as an ongoing enterprise is getting a little shop worn/shopped worn. It would not be helpful to once again start a new general process to find the ideal situation [sic solution?]; rather the urgency of the situation requires that a reasonable solution be found.

He went on to state that in the month before the vote there "will be considerable discussion and negotiation as to the plan which will in fact be put to the vote" and that the present Plan may be adjusted. He urged the stakeholders and Stelco to "deal with this question in a positive way" and that "it is better to move forward than backwards, especially where progress is required". It is obvious that the motions judge has brought his judgment to bear and decided that the Plan or some version of it is not doomed to fail. I can see no basis for second-guessing the motions judge on that issue.

26 I should comment on a submission made by the appellant that no deference should be paid to the business judgment of the Stelco board. The appellant submits that the board is entitled to deference for most of the decisions made in the day-to-day operations during the CCAA process except whether a restructuring should proceed or a plan of arrangement should proceed. The

appellant submits that those latter decisions are solely the prerogative of the creditors by reason of s. 6. While there is no question that the ultimate decision is for the creditors, the board of directors plays an important role in the restructuring process. Blair J.A. made this clear in an earlier appeal to this court concerning Stelco reported at (2005), 75 O.R. (3d) 5 at para. 44:

> What the court does under s. 11 is to establish the boundaries of the playing field and act as a referee in the process. *The company's role in the restructuring,* and that of its stakeholders, is to work out a plan or compromise that a sufficient percentage of creditors will accept and the court will approve and sanction. The corporate activities that take place in the course of the workout are governed by the legislation and legal principles that normally apply to such activities. In the course of acting as referee, the court has great leeway, as Farley J. observed in Lehndorff, [1993] O.J. No. 14, supra, at para. 5, "to make order[s] so as to effectively maintain the status quo in respect of an insolvent company while it attempts to gain the approval of its creditors for the proposed compromise or arrangement which will be to the benefit of both the company and its creditors". But the s. 11 discretion is not open-ended and unfettered. Its exercise must be guided by the scheme and object of the Act and by the legal principles that govern corporate law issues. *Moreover, the court is not entitled to usurp the role of the directors and management in conducting what are in substance the company's restructuring efforts.* [Emphasis added.]

27 The approvals given by the motions judge in this case are consistent with these principles. Those orders allow the company's restructuring efforts to move forward.

28 The position of the appellant also fails to give any weight to the broad range of interests in play in a CCAA process. Again to quote Blair J.A. in the earlier Stelco case at para. 36:

> In the CCAA context, Parliament has provided a statutory framework to extend protection to a company while it holds its creditors at bay and attempts to negotiate a compromised plan of arrangement that will enable it to emerge and continue as a viable economic entity, *thus benefiting society and the company in the long run, along with the company's creditors, shareholders, employees and other stakeholders*. The s. 11 discretion is the engine that drives this broad and flexible statutory scheme, and that for the most part supplants the need to resort to inherent jurisdiction. [Emphasis added.]

29 For these reasons, I would not give effect to the submissions of the appellant.

Submissions of the equity holders

30 The equity holders support the position of the appellant. They point out that the Stelco CCAA situation is somewhat unique. While Stelco entered the process in dire straits, since then almost

unprecedented worldwide prices for steel have boosted Stelco's fortunes. In an endorsement of February 28, 2005, the motions judge recognized this unusual state of affairs:

> In most restructurings, on emergence the original shareholder equity, if it has not been legally "evaporated" because the insolvent corporations was so for under water, is very substantially diminished. For example, the old shares may be converted into new emergent shares at a rate of 100 to 1; 1,000 to 1; or even 12,000 to 1. ... Stelco is one of those rare situations in which a change of external circumstances ... may result in the original equity having a more substantial "recovery" on emergence than outline above."

31 The equity holders point out that while an earlier plan would have allowed the shareholders to benefit from the continued and anticipated growth in the Stelco equity, the present plan does not include any provision for the existing shareholders. I agree with counsel for Stelco that these arguments are premature. They raise issues for the supervising judge if and when he is called upon to exercise his discretion under s. 6 to sanction the Plan of arrangement.

DISPOSITION

32 Accordingly, I would dismiss the appeal. On behalf of the court, I wish to thank all counsel for their very helpful written and oral submissions that made it possible to deal with this appeal expeditiously.

M. ROSENBERG J.A.
J.I. LASKIN J.A. -- I agree.
H.S. LaFORME J.A. -- I agree.

cp/e/qw/qlsxl/qlkjg/qlgxc

Tab 5

Case Name:

Timminco Ltd. (Re)

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 Timminco Limited and Bécancour Silicon Inc., Applicants

[2012] O.J. No. 1949

2012 ONSC 2515

Court File Nos. CV-12-9539-00CL and CV-09-378701-00CP

Ontario Superior Court of Justice
Commercial List

G.B. Morawetz J.

Heard: March 26, 2012.
Judgment: April 27, 2012.

(25 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Motion by plaintiff in class proceeding/creditor of company under CCAA protection to lift stay of proceedings allowed in part -- Stay lifted only to permit plaintiff to seek leave to appeal to Supreme Court of Canada procedural judgment about running of limitations period for class proceeding -- TO lift stay entirely would take focus of company's few remaining executives away from restructuring to deal with class proceeding, potentially causing prejudice to other stakeholders.

Bankruptcy and insolvency law -- Proceedings -- Practice and procedure -- Stays -- Motion by plaintiff in class proceeding/ creditor of company under CCAA protection to lift stay of proceedings allowed in part -- Stay lifted only to permit plaintiff to seek leave to appeal to Supreme Court of Canada procedural judgment about running of limitations period for class proceeding -- TO lift stay entirely would take focus of company's few remaining executives away from restructuring to deal with class proceeding, potentially causing prejudice to other stakeholders.

Civil litigation -- Civil procedure -- Parties -- Class or representative actions -- Procedure --

Motion by plaintiff in class proceeding/creditor of company under CCAA protection to lift stay of proceedings allowed in part -- Stay lifted only to permit plaintiff to seek leave to appeal to Supreme Court of Canada procedural judgment about running of limitations period for class proceeding -- TO lift stay entirely would take focus of company's few remaining executives away from restructuring to deal with class proceeding, potentially causing prejudice to other stakeholders.

Motion by Penneyfeather for an order lifting a January 2012 stay of proceedings to permit Penneyfeather to continue a class proceeding against Timminco and others. Timminco was pursuing a restructuring process intended to maximize recovery for stakeholders. It continued to operate as a going concern with a greatly-reduced staff of 10 employees including the president and three executive officers. The class proceeding was commenced in May 2009. Settlement discussions had been terminated and there was a pending motion to strike portions of the statement of claim. Penneyfeather planned to seek leave to appeal to the Supreme Court of Canada an order declaring that the three-year limitation period provided in the Securities Act was not suspended by the operation of the Class Proceedings Act. Timminco consented to lift the stay to permit Penneyfeather to pursue this leave application only. Timminco submitted that key members of its executive team would have to expend considerable time dealing with Penneyfeather's class proceeding if the stay was lifted completely, thereby taking their focus away from the restructuring process.

HELD: Motion allowed in part. If forced to spend significant amounts of time dealing with Penneyfeather's class action in the coming months, the Timminco executive team would be unable to focus on the sales and restructuring process to the potential detriment of Timminco's other stakeholders. A delay in the sales process could have a negative impact on Timminco. It was premature to lift the stay other than with respect to the leave application.

Statutes, Regulations and Rules Cited:

Class Proceedings Act, S.O. 1992, c. 6, s. 12, s. 28

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

Securities Act, R.S.O. 1990, c. S.5, s. 138.14

Counsel:

James C. Orr and N. Mizobuchi, for St. Clair Penneyfeather, Plaintiff in Class Proceeding, *Penneyfeather v. Timminco Limited et al.*

P. O'Kelly and A. Taylor, for the Applicants.

P. LeVay, for the Photon Defendants.

A. Lockhart, for Wacker Chemie AG.

K.D. Kraft, for Chubb Insurance Company of Canada.

D.J. Bell, for John P. Walsh.

A. Hatnay and James Harnum for Mercer Canada, Administrator of the Timminco Haley Plan.

S. Weisz, for FTI Consulting Canada Inc., Monitor.

ENDORSEMENT

1 G.B. MORAWETZ J.:-- St. Clair Penneyfeather, the Plaintiff in the *Penneyfeather v. Timminco Limited, et al* action, Court File No. CV-09-378701-00CP (the "Class Action"), brought this motion for an order lifting the stay of proceedings, as provided by the Initial Order of January 3, 2012 and extended by court order dated January 27, 2012, and permitting Mr. Penneyfeather to continue the Class Action against Timminco Limited ("Timminco"), Dr. Heinz Schimmelbusch, Mr. Robert Dietrich, Mr. Rene Boisvert, Mr. Arthur R. Spector, Mr. Jack Messman, Mr. John C. Fox, Mr. Michael D. Winfield, Mr. Mickey M. Yaksich and Mr. John P. Walsh.

2 The Class Action was commenced on May 14, 2009 and has been case managed by Perell J. The following steps have taken place in the litigation:

(a) a carriage motion;
(b) a motion to substitute the Representative Plaintiff;
(c) a motion to force disclosure of insurance policies;
(d) a motion for leave to appeal the result of the insurance motion which was heard by the Divisional Court and dismissed;
(e) settlement discussions;
(f) when settlement discussions were terminated, Perell J. declined an expedited leave hearing and instead declared any limitation period to be stayed;
(g) a motion for particulars; and
(h) a motion served but not heard to strike portions of the Statement of Claim.

3 On February 16, 2012, the Court of Appeal for Ontario set aside the decision of Perell J. declaring that s. 28 of the *Class Proceedings Act* suspended the running of the three-year limitation period under s. 138.14 of the *Securities Act*.

4 The Plaintiffs' counsel received instructions to seek leave to appeal the decision of the Court of Appeal for Ontario to the Supreme Court of Canada. The leave materials were required to be served and filed by April 16, 2012.

5 On April 10, 2012, the following endorsement was released in respect of this motion:

> The portion of the motion dealing with lifting the stay for the Plaintiff to seek leave to appeal the recent decision of the Court of Appeal for Ontario to the Supreme Court of Canada on the limitation period issue was not opposed. This portion of the motion is granted and an order shall issue to give effect to the foregoing. The balance of the requested relief is under reserve.

6 Counsel to Mr. Penneyfeather submits that, apart from the leave to appeal issues, there are steps that may occur before Perell J. as a result of the Court of Appeal ruling. Counsel references that the Defendants may bring motions for partial judgment and the Plaintiff could seek to have the court proceed with leave and certification with any order to be granted *nunc pro tunc* pursuant to s. 12 of the *Class Proceedings Act*.

7 Counsel to Mr. Penneyfeather submits that the three principal objectives of the *Class Proceedings Act* are judicial economy, access to justice and behaviour modification. (See *Western Canadian Shopping Centres Inc. v. Dutton*, [2001] 2 S.C.R. 534 at paras. 27-29.), and under the *Securities Act*, the deterrent represented by private plaintiffs armed with a realistic remedy is important in ensuring compliance with continuous disclosure rules.

8 Counsel submits that, in this situation, there is only one result that will not do violence to a primary legislative purpose and that is to lift the stay to permit the Class Action to proceed on the condition that any potential execution excludes Timminco's assets. Counsel further submits that, as a practical result, this would limit recovery in the Class Action to the proceeds of the insurance policies, or in the event that the insurers decline coverage because of fraud, to the personal assets of those officers and directors found responsible for the fraud.

9 Counsel to Mr. Penneyfeather takes the position that the requested outcome is consistent with the judicial principal that the CCAA is not meant as a refuge insulating insurers from providing appropriate indemnification. (See *Algoma Steel Corp. v. Royal Bank of Canada*, [1992] O.J. No. 889 at paras. 13-15 (C.A.) and *Re Carey Canada Inc.* [2006] O.J. No. 4905 at paras. 7, 16-17.)

10 In this case, counsel contends that, when examining the relative prejudice to the parties, the examination strongly favours lifting the stay in the manner proposed since the insurance proceeds are not available to other creditors and there would be no financial unfairness caused by lifting the stay.

11 The position put forward by Mr. Penneyfeather must be considered in the context of the CCAA proceedings. As stated in the affidavit of Ms. Konyukhova, the stay of proceedings was put in place in order to allow Timminco and Bécancour Silicon Inc. ("BSI" and, together with Timminco, the "Timminco Entities") to pursue a restructuring and sales process that is intended to maximize recovery for the stakeholders. The Timminco Entities continue to operate as a going concern, but with a substantially reduced management team. The Timminco Entities currently have

only ten active employees, including Mr. Kalins, President, General Counsel and Corporate Secretary and three executive officers (the "Executive Team").

12 Counsel to the Timminco Entities submits that, if Mr. Penneyfeather is permitted to pursue further steps in the Class Action, key members of the Executive Team will be required to spend significant amounts of their time dealing with the Class Action in the coming months, which they contend is a key time in the CCAA proceedings. Counsel contends that the executive team is currently focussing on the CCAA proceedings and the sales process.

13 Counsel to the Timminco Entities points out that the Executive Team has been required to direct most of their time to restructuring efforts and the sales process. Currently, the "stalking horse" sales process will continue into June 2012 and I am satisfied that it will require intensive time commitments from management of the Timminco Entities.

14 It is reasonable to assume that, by late June 2012, all parties will have a much better idea as to when the sales process will be complete.

15 The stay of proceedings is one of the main tools available to achieve the purpose of the CCAA. The stay provides the Timminco Entities with a degree of time in which to attempt to arrange an acceptable restructuring plan or sale of assets in order to maximize recovery for stakeholders. The court's jurisdiction in granting a stay extends to both preserving the *status quo* and facilitating a restructuring. See *Re Stelco Inc.*, [2005] O.J. No. 1171 (C.A.) at para. 36.

16 Further, the party seeking to lift a stay bears a heavy onus as the practical effect of lifting a stay is to create a scenario where one stakeholder is placed in a better position than other stakeholders, rather than treating stakeholders equally in accordance with their priorities. See *Canwest Global Communications Corp. (Re)*, [2011] O.J. No. 1590 (S.C.J.) at para. 27.

17 Courts will consider a number of factors in assessing whether it is appropriate to lift a stay, but those factors can generally be grouped under three headings: (a) the relative prejudice to parties; (b) the balance of convenience; and (c) where relevant, the merits (*i.e.* if the matter has little chance of success, there may not be sound reasons for lifting the stay). See *Canwest Global Communications (Re), supra*, at para. 27.

18 Counsel to the Timminco Entities submits that the relative prejudice to the parties and the balance of convenience clearly favours keeping the stay in place, rather than to allow the Plaintiff to proceed with the SCC leave application. As noted above, leave has been granted to allow the Plaintiff to proceed with the SCC leave application. Counsel to the Timminco Entities further submits that, while the merits are vigorously disputed by the Defendants in the context of a Class Action, the Timminco Entities will not ask this court to make any determinations based on the merits of the Plaintiff's claim.

19 I can well recognize why Mr. Penneyfeather wishes to proceed. The objective of the Plaintiff

in the Class Action is to access insurance proceeds that are not available to other creditors. However, the reality of the situation is that the operating side of Timminco is but a shadow of its former self. I accept the argument put forth by counsel to the Applicant that, if the Executive Team is required to spend significant amounts of time dealing with the Class Action in the coming months, it will detract from the ability of the Executive Team to focus on the sales process in the CCAA proceeding to the potential detriment of the Timminco Entities' other stakeholders. These are two competing interests. It seems to me, however, that the primary focus has to be on the sales process at this time. It is important that the Executive Team devote its energy to ensuring that the sales process is conducted in accordance with the timeliness previously approved. A delay in the sales process may very well have a negative impact on the creditors of Timminco. Conversely, the time sensitivity of the Class Action has been, to a large extent, alleviated by the lifting of the stay so as to permit the leave application to the Supreme Court of Canada.

20 It is also significant to recognize the submission of counsel on behalf of Mr. Walsh. Counsel to Mr. Walsh takes the position that Mr. Penneyfeather has nothing more than an "equity claim" as defined in the CCAA and, as such, his claim (both against the company and its directors who, in turn, would have an equity claim based on indemnity rights) would be subordinated to any creditor claims. Counsel further submits that of all the potential claims to require adjudication, presumably, equity claims would be the least pressing to be adjudicated and do not become relevant until all secured and unsecured claims have been paid in full.

21 In my view, it is not necessary for me to comment on this submission, other than to observe that to the extent that the claim of Mr. Penneyfeather is intended to access certain insurance proceeds, it seems to me that the prosecution of such claim can be put on hold, for a period of time, so as to permit the Executive Team to concentrate on the sales process.

22 Having considered the relative prejudice to the parties and the balance of convenience, I have concluded that it is premature to lift the stay at this time, with respect to the Timminco Entities, other than with respect to the leave application to the Supreme Court of Canada. It also follows, in my view, that the stay should be left in place with respect to the claim as against the directors and officers. Certain members of this group are involved in the Executive Team and, for the reasons stated above, I am satisfied that it is not appropriate to lift the stay as against them.

23 With respect to the claim against Photon, as pointed out by their counsel, it makes no sense to lift the stay only as against Photon and leave it in place with respect to the Timminco Entities. As counsel submits, the Timminco Entities have an interest in both the legal issues and the factual issues that may be advanced if Mr. Penneyfeather proceeds as against Photon, as any such issues as are determined in Timminco's absence may cause unfairness to Timminco, particularly, if Mr. Penneyfeather later seeks to rely on those findings as against Timminco. I am in agreement with counsel's submission that to make such an order would be prejudicial to Timminco's business and property. In addition, I accept the submission that it would also be unfair to Photon to require it to answer Mr. Penneyfeather's allegations in the absence of Timminco as counsel has indicated that

Photon will necessarily rely on documents and information produced by Timminco as part of its own defence.

24 I am also in agreement with the submission that it would be wasteful of judicial resources to permit the class proceedings to proceed as against Photon but not Timminco as, in addition to the duplicative use of court time, there would be the possibility of inconsistent findings on similar or identical factual issues and legal issues. For these reasons, I have concluded that it is not appropriate to lift the stay as against Photon.

25 In the result, the motion dealing with issues not covered by the April 10, 2012 endorsement is dismissed without prejudice to the rights of the Plaintiff to renew his request no sooner than 75 days after today's date.

G.B. MORAWETZ J.

cp/e/qljel/qlpmg/qlced

---- End of Request ----
Email Request: Current Document: 1
Time Of Request: Thursday, October 04, 2012 16:28:33

Tab 6

Case Name:

Canwest Global Communications Corp. (Re)

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, C-36, as amended
AND IN THE MATTER OF a proposed plan of compromise or arrangement of Canwest Global Communications Corp. and the other applicants listed on Schedule "A"

[Editor's note:
Schedule A was not attached to the copy received from the Court and therefore is not included in the judgment.]

[2009] O.J. No. 5379

61 C.B.R. (5th) 200

2009 CarswellOnt 7882

Court File No. CV-09-8241-OOCL

Ontario Superior Court of Justice
Commercial List

S.E. Pepall J.

Heard: December 8, 2009.
Judgment: December 15, 2009.

(52 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Compromises and arrangements -- Claims -- Application in this Companies' Creditors Arrangement Act matter for an order declaring that the relief sought by the "GS Parties" was subject to an Oct. 6, 2009 stay of proceedings granted -- Cross-motion by the GS Parties for an order lifting the stay so that they could pursue their motion challenging pre-filing conduct of the CMI entities, etc., dismissed -- The substance and subject matter of the motion were certainly encompassed by the stay -- The balance of convenience, the assessment of relative prejudice and the relevant merits favoured the position of the CMI Entities on the lift stay motion.

Bankruptcy and insolvency law -- Proceedings -- Practice and procedure -- Stays -- Application in this Companies' Creditors Arrangement Act matter for an order declaring that the relief sought by the "GS Parties" was subject to an Oct. 6, 2009 stay of proceedings granted -- Cross-motion by the GS Parties for an order lifting the stay so that they could pursue their motion challenging pre-filing conduct of the CMI entities, etc., dismissed -- The substance and subject matter of the motion were certainly encompassed by the stay -- The balance of convenience, the assessment of relative prejudice and the relevant merits favoured the position of the CMI Entities on the lift stay motion.

Application by the CCAA applicants and the "CMI entities" for an order declaring that the relief sought by the "GS parties" was subject to the stay of proceedings granted on Oct. 6, 2009. Cross-motion by GS Parties for an order lifting the stay so they could pursue their motion challenging pre-filing conduct of the CMI entities, etc. The Ad Hoc Committee of Noteholders and the Special Committee of the Board of Directors supported the position of the CMI Entities. In essence, the GS Parties' motion sought to undo the transfer of the CW Investments Co. shares from 441 to CMI or to require CMI to perform and not disclaim the shareholders agreement as though the shares had not been transferred.

HELD: GS Parties' motions dismissed, save for a portion dealing with para. 59 of the initial order on consent; CMI Entities' motion granted with the exception of a strike portion, which was moot. The first issue was caught by the stay of proceedings and the second was properly addressed if and when CMI sought to disclaim the shareholders agreement. The substance of the GS Parties' motion was a "proceeding" subject to the stay under para. 15 of the initial order prohibiting the commencement of all proceedings against or in respect of the CMI Entitites, or affecting the CMI business or property. The relief sought would also involve "the exercise of any right or remedy affecting the CMI business or the CMI property" which was stayed under para. 16 of the initial order. The substance and subject matter of the motion were certainly encompassed by the stay. The real question was whether the stay ought to be lifted in this case. If the stay were lifted, the prejudice to CMI would be great and the proceedings contemp lated by the GS Parties would be extraordinarily disruptive. The GS Parties were in no worse position than any other stakeholder who was precluded from relying on rights that arise upon an insolvency default. The balance of convenience, the assessment of relative prejudice and the relevant merits favoured the position of the CMI Entities on the lift stay motion. The onus to lift the stay was on the moving party. The stay was performing the essential function of keeping stakeholders at bay in order to give CMI Entities a reasonable opportunity to develop a restructuring plan.

Statutes, Regulations and Rules Cited:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 32, s. 11.02

Counsel:

Lyndon Barnes, Alex Cobb and Shawn Irving for the CMI Entities.

Alan Mark and Alan Merskey for the Special Committee of the Board of Directors of Canwest.

David Byers and Maria Konyukhova for the Monitor, FTI Consulting Canada Inc.

Benjamin Zarnett and Robert Chadwick for the Ad Hoc Committee of Noteholders.

K. McElcheran and G. Gray for GS Parties.

Hugh O'Reilly and Amanda Darrach for Canwest Retirees and the Canadian Media Guild.

Hilary Clarke for Senior Secured Lenders to LP Entities.

Steve Weisz for CIT Business Credit Canada Inc.

REASONS FOR DECISION

S.E. PEPALL J.:--

Relief Requested

1 The CCAA applicants and partnerships (the "CMI Entities") request an order declaring that the relief sought by GS Capital Partners VI Fund L.P., GSCP VI AA One Holding S.ar.1 and GS VI AA One Parallel Holding S.ar.1 (the "GS Parties") is subject to the stay of proceedings granted in my Initial Order dated October 6, 2009. The GS Parties bring a cross-motion for an order that the stay be lifted so that they may pursue their motion which, among other things, challenges pre-filing conduct of the CMI Entities. The Ad Hoc Committee of Noteholders and the Special Committee of the Board of Directors support the position of the CMI Entities. All of these stakeholders are highly sophisticated. Put differently, no one is a commercial novice. Such is the context of this dispute.

Background Facts

2 Canwest's television broadcast business consists of the CTLP TV business which is comprised of 12 free-to-air television stations and a portfolio of subscription based specialty television channels on the one hand and the Specialty TV Business on the other. The latter consists of 13 specialty television channels that are operated by CMI for the account of CW Investments Co. and its subsidiaries and 4 other specialty television channels in which the CW Investments Co. ownership interest is less than 50%.

3 The Specialty TV Business was acquired jointly with Goldman Sachs from Alliance Atlantis in August, 2007. In January of that year, CMI and Goldman Sachs agreed to acquire the business of

Alliance Atlantis through a jointly owned acquisition company which later became CW Investments Co. It is a Nova Scotia Unlimited Liability Corporation ("NSULC").

4 CMI held its shares in CW Investments Co. through its wholly owned subsidiary, 4414616 Canada Inc. ("441"). According to the CMI Entities, the sole purpose of 441 was to insulate CMI from any liabilities of CW Investments Co. As a NSULC, its shareholders may face exposure if the NSULC is liquidated or becomes bankrupt. As such, 441 served as a "blocker" to potential liability. The CMI Entities state that similarly the GS parties served as "blockers" for Goldman Sachs' part of the transaction.

5 According to the GS Parties, the essential elements of the deal were as follows:

(i) GS would acquire at its own expense and at its own risk, the slower growth businesses;
(ii) CW Investments Co. would acquire the Specialty TV Business and that company would be owned by 441 and the GS Parties under the terms of a Shareholders Agreement;
(iii) GS would assist CW Investments Co. in obtaining separate financing for the Specialty TV Business;
(iv) Eventually Canwest would contribute its conventional TV business on a debt free basis to CW Investments Co. in return for an increased ownership stake in CW Investments Co.

6 The GS Parties also state that but for this arrangement, Canwest had no chance of acquiring control of the Specialty TV Business. That business is subject to regulation by the CRTC. Consistent with policy objectives, the CRTC had to satisfy itself that CW Investments Co. was not controlled either at law or in fact by a non-Canadian.

7 A Shareholders Agreement was entered into by the GS parties, CMI, 441, and CW Investments Co. The GS Parties state that 441 was a critical party to this Agreement. The Agreement reflects the share ownership of each of the parties to it: 64.67% held by the GS Parties and 35.33% held by 441. It also provides for control of CW Investments Co. by distribution of voting shares: 33.33% held by the GS Parties and 66.67% held by 441. The Agreement limits certain activities of CW Investments Co. without the affirmative vote of a director nominated to its Board by the GS Parties. The Agreement provides for call and put options that are designed to allow the GS parties to exit from the investment in CW Investments Co. in 2011, 2012, and 2013. Furthermore, in the event of an insolvency of CMI, the GS parties have the ability to effect a sale of their interest in CW Investments Co. and require as well a sale of CMI's interest. This is referred to as the drag-along provision. Specifically, Article 6.10(a) of the Shareholders Agreement states:

> Notwithstanding the other provisions of this Article 6, if an Insolvency Event occurs in respect of CanWest and is continuing, the GS Parties shall be entitled to sell all of their Shares to any *bona fide* Arm's Length third party or parties at a

> price and on other terms and conditions negotiated by GSCP in its discretion provided that such third party or parties acquires all of the Shares held by the CanWest Parties at the same price and on the same terms and conditions, and in such event, the CanWest Parties shall sell their Shares to such third party or parties at such price and on such terms and conditions. The Corporation and the CanWest Parties each agree to cooperate with and assist GSCP with the sale process (including by providing protected purchasers designated by GSCP with confidential information regarding the Corporation (subject to a customary confidentiality agreement) and with access to management).

8 The Agreement also provided that 441 as shareholder could transfer its CW Investments Co. shares to its parent, CMI, at any time, by gift, assignment or otherwise, whether or not for value. While another specified entity could not be dissolved, no prohibition was placed on the dissolution of 441. 441 had certain voting obligations that were to be carried out at the direction of CMI. Furthermore, CMI was responsible for ensuring the performance by 441 of its obligations under the Shareholders Agreement.

9 On October 5, 2009, pursuant to a Dissolution Agreement between 441 and CMI and as part of the winding-up and distribution of its property, 441 transferred all of its property, namely its 352,986 Class A shares and 666 Class B preferred shares of CW Investments Co., to CMI. CMI undertook to pay and discharge all of 441's liabilities and obligations. The material obligations were those contained in the Shareholders Agreement. At the time, 441 and CW Investments Co. were both solvent and CMI was insolvent. 441 was subsequently dissolved.

10 For the purposes of these two motions only, the parties have agreed that the court should assume that the transfer and dissolution of 441 was intended by CMI to provide it with the benefit of all the provisions of the CCAA proceedings in relation to contractual obligations pertaining to those shares. This would presumably include both the stay provisions found in section 11 of the CCAA and the disclaimer provisions in section 32 .

11 The CMI Entities state that CMI's interest in the Specialty TV Business is critical to the restructuring and recapitalization prospects of the CMI Entities and that if the GS parties were able to effect a sale of CW Investments Co. at this time, and on terms that suit them, it would be disastrous to the CMI Entities and their stakeholders. Even the overhanging threat of such a sale is adversely affecting the negotiation of a successful restructuring or recapitalization of the CMI Entities.

12 On October 6, 2009, I granted an Initial Order in these proceedings. CW Investments Co. was not an applicant. The CMI Entities requested a stay of proceedings to allow them to proceed to develop a plan of arrangement or compromise to implement a consensual "pre-packaged" recapitalization transaction. The CMI Entities and the Ad Hoc Committee of 8% Noteholders had agreed on terms of such a transaction that were reflected in a support agreement and term sheet.

Those noteholders who support the term sheet have agreed to vote in favour of the plan subject to certain conditions one of which is a requirement that the Shareholders Agreement be amended.

13 The Initial Order included the typical stay of proceedings provisions that are found in the standard form order promulgated by the Commercial List Users Committee. Specifically, the order stated:

> 15. THIS COURT ORDERS that until and including November 5, 2009, or such later date as this Court may order (the "Stay Period"), no proceeding or enforcement process in any court or tribunal (each, a "Proceeding") shall be commenced or continued against or in respect of the CMI Entities, the Monitor or the CMI CRA or affecting the CMI Business or the CMI Property, except with the written consent of the applicable CMI Entity, the Monitor and the CMI CRA (in respect of Proceedings affecting the CMI Entities, the CMI Property or the CMI Business), the CMI CRA (in respect of Proceedings affecting the CMI Entities, the CMI property or the CMI Business), the CMI CRA (in respect of Proceedings affecting the CMI CRA), or with leave of this Court, and any and all Proceedings currently under way against or in respect of the CMI Entities or the CMI CRA or affecting the CMI Business or the CMI Property are hereby stayed and suspended pending further Order of this Court. In the case of the CMI CRA, no Proceeding shall be commenced against the CMI CRA or its directors and officers without prior leave of this Court on seven (7) days notice to Stonecrest Capital Inc.
>
> 16. THIS COURT ORDERS that during the Stay Period, all rights and remedies of any individual, firm, corporation, governmental body or agency, or any other entities (all of the foregoing, collectively being "Persons" and each being a "Person") against or in respect of the CMI Entities, the Monitor and/or the CMI CRA, or affecting the CMI Business or the CMI Property, are hereby stayed and suspended except with the written consent of the applicable CMI Entity, the Monitor and the CMI CRA (in respect of rights and remedies affecting the CMI Entities, the CMI Property or the CMI Business), the CMI CRA (in respect of rights or remedies affecting the CMI CRA), or leave of this Court, provided that nothing in this Order shall (i) empower the CMI Entities to carry on any business which the CMI Entities are not lawfully entitled to carry on, (ii) exempt the CMI Entities from compliance with statutory or regulatory provisions relating to health, safety or the environment, (iii) prevent the filing of any registration to preserve or perfect a security interest, or (iv) prevent the registration of a claim for lien.

14 The GS parties were not given notice of the CCAA application. On November 2, 2009, they brought a motion that, among other things, seeks to set aside the transfer of the shares from 441 to CMI or, in the alternative, require CMI to perform and not disclaim the Shareholders Agreement as

if the shares had not been transferred. On November 10, 2009 the GS parties purported to revive 441 by filing Articles of Revival with the Director of the CBCA. The CMI Entities were not notified nor was any leave of the court sought in this regard. In an amended notice of motion dated November 19, 2009 (the "main motion"), the GS Parties request an order:

(a) Setting aside and declaring void the transfer of the shares from 441 to CMI;
(b) declaring that the rights and remedies of the GS Parties in respect of the obligations of 441 under the Shareholders Agreement are not affected by these CCAA proceedings in any way whatsoever;
(c) in the alternative to (a) and (b), an order directing CMI to perform all of the obligations that bound 441 immediately prior to the transfer;
(d) in the alternative to (a) and (b), an order declaring that the obligations that bound 441 immediately prior to the transfer, may not be disclaimed by CMI pursuant to section 32 of the CCAA or otherwise; and
(e) if necessary, a trial of the issues arising from the foregoing.

15 They also requested an order amending paragraph 59 of the Initial Order but that issue has now been resolved and I am satisfied with the amendment proposed.

16 The CMI Entities then brought a motion on November 24, 2009 for an order that the GS motion is stayed. As in a game of chess, on December 3, 2009, the GS Parties served a cross-motion in which, if required, they seek leave to proceed with their motion.

17 In furtherance of their main motion, the GS Parties have expressed a desire to examine 4 of the 5 members of the Special Committee of the Board of Directors of Canwest. That Committee was constituted, among other things, to oversee the restructuring. The GS Parties have also demanded an extensive list of documentary production. They also seek to impose significant discovery demands upon the senior management of CanWest.

Issues

18 The issues to be determined on these motions are whether the relief requested by the GS Parties in their main motion is stayed based on the Initial Order and if so, whether the stay should be lifted. In addition, should the relief sought in paragraph 1(e) of the main motion be struck.

Positions of Parties

19 In brief, the parties' positions are as follows. The CMI Entities submit that the GS Parties' motion is a "proceeding" that is subject to the stay under paragraph 15 of the Initial Order. In addition, the relief sought by them involves "the exercise of any right or remedy affecting the CMI Business or the CMI Property" which is stayed under paragraph 16 of the Initial Order. The stay is consistent with the purpose of the CCAA. They submit that the subject matter of the motion should

be caught so as to prevent the GS parties from gaining an unfair advantage over other stakeholders of the CMI Entities and to ensure that the resources of the CMI Entities are devoted to developing a viable restructuring plan for the benefit of all stakeholders. They also state that CMI's interest in CW Investments Co. is a significant portion of its enterprise value. They state further that their actions were not in breach of the Shareholders Agreement and in any event, debtor companies are able to organize their affairs in order to benefit from the CCAA stay. Furthermore, any loss suffered by the GS Parties can be quantified.

20 In paragraph 1(e) of the main motion, the GS parties seek to prevent CMI from disclaiming the obligations of 441 that existed immediately prior to the transfer of the shares to CMI. If this relief is not stayed, the CMI Entities submit that it should be struck out pursuant to Rule 25.11(b) and (c) as premature and improper. They also argue that section 32 of the CCAA provides a procedure for disclaimer of agreements which the GS Parties improperly seek to circumvent.

21 Lastly, the CMI Entities state that the bases on which a CCAA stay should be lifted are very limited. Most of the grounds set forth in *Re Canadian Airlines Corp.*[1] which support the lifting of a stay are manifestly inapplicable. As to prejudice, the GS parties are in no worse position than any other stakeholder who is precluded from relying on rights that arise on an insolvency default. In contrast, the prejudice to the CMI Entities would be debilitating and their resources need to be devoted to their restructuring. The GS Parties' rights would not be lost by the passage of time. The GS Parties' motion is all about leverage and a desire to improve the GS Parties' negotiating position submits counsel for the CMI Entities.

22 The Ad Hoc Committee of Noteholders, as mentioned, supports the CMI Entities' position. In examining the context of the dispute, they submit that the Shareholders Agreement permitted and did not prohibit the transfer of 441's shares. Furthermore, the operative obligations in that agreement are obligations of CMI, not 441. It is the substance of the GS Parties' claims and not the form that should govern their ability to pursue them and it is clearly encompassed by the stay. The Committee relies on *Chef Ready Foods Ltd. v. Hongkong Bank of Canada*[2] in support of their position on timing.

23 The Special Committee also supports the CMI Entities. It submits that the primary relief sought by the GS parties is a declaration that their contracts to and with CW Investments cannot or should not be disclaimed. The debate as to whether 441 could properly be assimilated into CMI is no more than an alternate argument as to why such disclaimer can or cannot occur. They state that the subject matter of the GS Parties' motion is premature.

24 The GS Parties submit that the stay does not prevent parties affected by the CCAA proceedings from bringing motions within the CCAA proceedings themselves. The use of CCAA powers and the scope of the stay provided in the Initial Order and whether it applies to the GS Parties' motion are proper questions for the court charged with supervising the CCAA process. They also argue that the motion would facilitate negotiation between key parties, raises the important

preliminary issue of the proper scope and application of section 32 of the CCAA, and avoids putting the Monitor in the impossible position of having to draw legal conclusions as to the scope of CMI's power to disclaim. The court should be concerned with pre-filing conduct including the reason for the share transfer, the timing, and CMI's intentions.

25 Even if the stay is applicable, the GS parties submit that it should be lifted. In this regard, the court should consider the balance of convenience, the relative prejudice to parties, and where relevant, the merits of the proposed action. The court should also consider whether the debtor company has acted and is acting in good faith. The GS Parties were the medium by which the Specialty TV Business became part of Canwest. Here, all that is being sought is a reversal of the false and highly prejudicial start to these restructuring proceedings. It is necessary to take steps now to protect a right that could be lost by the passage of time. The transfer of the shares exhibited bad faith on the part of Canwest. 441 insulated CW Investments Co. and the Specialty TV Business from the insolvency of CMI and thereby protected the contractual rights of the GS Parties. The manifest harm to the GS Parties that invited the motion should be given weight in the court's balancing of prejudices. Concerns as to disruption of the restructuring process could be met by imposing conditions on the lifting of a stay as, for example, the establishment of a timetable.

Discussion

(a) Legal Principles

26 First I will address the legal principles applicable to the granting and lifting of a CCAA stay.

27 The stay provisions in the CCAA are discretionary and are extraordinarily broad. Section 11.02 (1) and (2) states:

> 11.02 (1) A court may, on an initial application in respect of a debtor company, make an order on any terms that it may impose, effective for the period that the court considers necessary, which period may not be more than 30 days,
>
> (a) staying, until otherwise ordered by the court, all proceedings taken or that might be taken in respect of the company under the Bankruptcy and Insolvency Act or the Winding-up and Restructuring Act;
> (b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and
> (c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.
> (2) A court may, on an application in respect of a debtor company other than an initial application, make an order, on any terms that it may impose,
> (a) staying until otherwise ordered by the court, for any period that the court considers necessary, all proceedings taken or that might be taken in respect

of the company under an Act referred to in paragraph (1)(a);

(b) restraining, until otherwise ordered by the court, further proceedings in any action, suit or proceeding against the company; and

(c) prohibiting, until otherwise ordered by the court, the commencement of any action, suit or proceeding against the company.

28 The underlying purpose of the court's power to stay proceedings has frequently been described in the case law. It is the engine that drives the broad and flexible statutory scheme of the CCAA: *Re Stelco Inc*[3] and the key element of the CCAA process: *Re Canadian Airlines Corp.*[4] The power to grant the stay is to be interpreted broadly in order to permit the CCAA to accomplish its legislative purpose. As noted in *Re Lehndorff General Partner Ltd.*[5], the power to grant a stay extends to effect the position of a company's secured and unsecured creditors as well as other parties who could potentially jeopardize the success of the restructuring plan and the continuance of the company. As stated by Farley J. in that case,

> "It has been held that the intention of the CCAA is to prevent any manoeuvres for positioning among the creditors during the period required to develop a plan and obtain approval of creditors. Such manoeuvres could give an aggressive creditor an advantage to the prejudice of others who are less aggressive and would undermine the company's financial position making it even less likely that the plan will succeed. ... The possibility that one or more creditors may be prejudiced should not affect the court's exercise of its authority to grant a stay of proceedings under the CCAA because this affect is offset by the benefit to all creditors and to the company of facilitating a reorganization. The court's primary concerns under the CCAA must be for the debtor and *all* of the creditors."[6] (Citations omitted)

29 The all encompassing scope of the CCAA is underscored by section 8 of the Act which precludes parties from contracting out of the statute. See *Chef Ready Foods Ltd. v. Hongkong Bank of Canada*[7] in this regard.

30 Two cases dealing with stays merit specific attention. *Campeau v. Olympia & York Developments Ltd.*[8] was a decision granted in the early stages of the evolution of the CCAA. In that case, the plaintiffs brought an action for damages including the loss of share value and loss of opportunity both against a company under CCAA protection and a bank. The statement of claim had been served before the company's CCAA filing. The plaintiff sought to lift the stay to proceed with its action. The bank sought an order staying the action against it pending the disposition of the CCAA proceedings. Blair J. examined the stay power described in the CCAA, section 106 of the Courts of Justice Act[9] and the court's inherent jurisdiction. He refused to lift the stay and granted the stay in favour of the bank until the expiration of the CCAA stay period. Blair J. stated that the plaintiff's claims may be addressed more expeditiously in the CCAA proceeding itself.[10] Presumably this meant through a claims process and a compromise of claims. The CCAA stay

precludes the litigating of claims comparable to the plaintiff's in *Campeau*. If it were otherwise, the stay would have no meaningful impact.

31 The decision of *Chef Ready Foods Ltd. v. Hongkong Bank of Canada* is also germane to the case before me. There, the Bank demanded payment from the debtor company and thereafter the debtor company issued instant trust deeds to qualify for protection under the CCAA. The bank commenced proceedings on debenture security and the next day the company sought relief under the CCAA. The court stayed the bank's enforcement proceedings. The bank appealed the order and asked the appellate court to set aside the stay order insofar as it restrained the bank from exercising its rights under its security. The B.C. Court of Appeal refused to do so having regard to the broad public policy objectives of the CCAA.

32 As with the imposition of a stay, the lifting of a stay is discretionary. There are no statutory guidelines contained in the Act. According to Professor R.H. McLaren in his book "Canadian Commercial Reorganization: Preventing Bankruptcy"[11], an opposing party faces a very heavy onus if it wishes to apply to the court for an order lifting the stay. In determining whether to lift the stay, the court should consider whether there are sound reasons for doing so consistent with the objectives of the CCAA, including a consideration of the balance of convenience, the relative prejudice to parties, and where relevant, the merits of the proposed action: *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*[12]. That decision also indicated that the judge should consider the good faith and due diligence of the debtor company.[13]

33 Professor McLaren enumerates situations in which courts will lift a stay order. The first six were cited by Paperny J. in 2000 in *Re Canadian Airlines Corp.*[14] and Professor McLaren has added three more since then. They are:

1. When the plan is likely to fail.
2. The applicant shows hardship (the hardship must be caused by the stay itself and be independent of any pre-existing condition of the applicant creditor).
3. The applicant shows necessity for payment (where the creditors' financial problems are created by the order or where the failure to pay the creditor would cause it to close and thus jeopardize the debtor's company's existence).
4. The applicant would be significantly prejudiced by refusal to lift the stay and there would be no resulting prejudice to the debtor company or the positions of creditors.
5. It is necessary to permit the applicant to take steps to protect a right which could be lost by the passing of time.
6. After the lapse of a significant time period, the insolvent is no closer to a proposal than at the commencement of the stay period.
7. There is a real risk that a creditor's loan will become unsecured during the stay period.
8. It is necessary to allow the applicant to perfect a right that existed prior to the

commencement of the stay period.

9. It is in the interests of justice to do so.

(b) Application

34 Turning then to an application of all of these legal principles to the facts of the case before me, I will first consider whether the subject matter of the main motion of the GS Parties is captured by the stay and then will address whether the stay should be lifted.

35 In analyzing the applicability of the stay, I must examine the substance of the main motion of the GS Parties and the language of the stay found in paragraphs 15 and 16 of my Initial Order.

36 In essence, the GS Parties' motion seeks to:

(i) undo the transfer of the CW Investments Co. shares from 441 to CMI or
(ii) require CMI to perform and not disclaim the Shareholders Agreement as though the shares had not been transferred.

37 It seems to me that the first issue is caught by the stay of proceedings and the second issue is properly addressed if and when CMI seeks to disclaim the Shareholders Agreement.

38 The substance of the GS Parties' motion is a "proceeding" that is subject to the stay under paragraph 15 of the Initial Order which prohibits the commencement of all proceedings against or in respect of the CMI Entities, or affecting the CMI Business or the CMI Property. The relief sought would also involve "the exercise of any right or remedy affecting the CMI Business or the CMI Property" which is stayed under paragraph 16 of the Initial Order.

39 When one examines the relief requested in detail, the application of the stay is clear. The GS Parties ask first for an order setting aside and declaring void the transfer of the shares from 441. As the shares have been transferred to the CMI Entities presumably pursuant to section 6.5(a) of the Shareholders Agreement, this is relief "affecting the CMI Property". Secondly, the GS Parties ask for a declaration that the rights and remedies of the GS Parties in respect of the obligations of 441 are not affected by the CCAA proceedings. This relief would permit the GS Parties to require CMI to tender the shares for sale pursuant to section 6.10 of the Shareholders Agreement. This too is relief affecting the CMI Entities and the CMI Property. Thirdly, they ask for an order directing CMI to perform all of the obligations that bound 441 prior to the transfer. This represents the exercise of a right or remedy against CMI and would affect the CMI Business and CMI Property in violation of paragraph 16 of the Initial Order. This is also stayed by virtue of paragraph 15. Fourthly, the GS Parties seek an order declaring that the obligations that bound 441 prior to the transfer may not be disclaimed. This both violates paragraph 16 of the Initial Order and also seeks to avoid the express provisions contained in the recent amendments to the CCAA that address disclaimer.

40 Accordingly, the substance and subject matter of the GS Parties' motion are certainly encompassed by the stay. As Mr. Barnes for the CMI Entities submitted, had CMI taken the steps it did six months ago and the GS Parties commenced a lawsuit, the action would have been stayed. Certainly to the extent that the GS Parties are seeking the freedom to exercise their drag along rights, these rights should be captured by the stay.

41 The real question, it seems to me, is whether the stay should be lifted in this case. In considering the request to lift the stay, it is helpful to consider the context and the provisions of the Shareholders Agreement. In his affidavit sworn November 24, 2009, Mr. Strike, the President of Corporate Development & Strategy Implementation of Canwest Global and its Recapitalization Officer, states that the joint acquisition from Alliance Atlantis was intensely and very carefully negotiated by the parties and that the negotiation was extremely complex and difficult. "Every aspect of the deal was carefully scrutinized, including the form, substance and precise terms of the Initial Shareholders Agreement." The Shareholders Agreement was finalized following the CRTC approval hearing. Among other things:

- Article 2.2 (b) provides that CMI is responsible for ensuring the performance by 441 of its obligations under the Shareholders Agreement.
- Article 6.1 contains a restriction on the transfer of shares.
- Article 6.5 addresses permitted transfers. Subsection (a) expressly permits each shareholder to transfer shares to a parent of the shareholder. CMI was the parent of the shareholder, 441.
- Article 6.10 provides that notwithstanding the other provisions of Article 6, if an insolvency event occurs (which includes the commencement of a CCAA proceeding), the GS Parties may sell their shares and cause the Canwest parties to sell their shares on the same terms. This is the drag along provision.
- Article 6.13 prohibits the liquidation or dissolution of another company[15] without the prior written consent of one of the GS Parties[16].

42 The recital of these provisions and the absence of any prohibition against the dissolution of 441 indicate that there is a good arguable case that the Shareholders Agreement, which would inform the reasonable expectations of the parties, permitted the transfer and dissolution.

43 The GS Parties are in no worse position than any other stakeholder who is precluded from relying on rights that arise upon an insolvency default. As stated in *San Francisco Gifts Ltd.*[17]:

> "The Initial Order enjoined all of San Francisco's landlords from enforcing contractual insolvency clauses. This is a common prohibition designed, at least in part, to avoid a creditor frustrating the restructuring by relying on a contractual breach occasioned by the very insolvency that gave rise to proceedings in the first place."[18]

44 Similarly, in *Norcen Energy Resources Ltd.*[19], one of the debtor's joint venture partners in certain petroleum operations was unable to rely on an insolvency clause in an agreement that provided for the immediate replacement of the operator if it became bankrupt or insolvent.

45 If the stay were lifted, the prejudice to CMI would be great and the proceedings contemplated by the GS Parties would be extraordinarily disruptive. The GS Parties have asked to examine 4 of the 5 members of the Special Committee. The Special Committee is a committee of the Board of Directors of Canwest. Its mandate includes, among other things, responsibility for overseeing the implementation of a restructuring with respect to all, or part of the business and/or capital structure of Canwest. The GS Parties have also requested an extensive list of documentary production including all documents considered by the Special Committee and any member of that Committee relating to the matters at issue; all documents considered by the Board of Directors and any member of the Board of Directors relating to the matters at issue; all documents evidencing the deliberations, discussions and decisions of the Special Committee and the Board of Directors relating to the matters at issue; all documents relating to the matters at issue sent to or received by Leonard Asper, Derek Burney, David Drybrough, David Kerr, Richard Leipsic, John Maguire, Margot Micillef, Thomas Strike, and Hap Stephen, the Chief Restructuring Advisor appointed by the court. As stated by Mr. Strike in his affidavit sworn November 24, 2009,

> "The witnesses that the GS Parties propose to examine include the most senior executives of the CMI Entities; those who are most intensely involved in the enormously complex process of achieving a successful going concern restructuring or recapitalization of the CMI Entities. Myself, Mr. Stephen, Mr. Maguire and the others are all working flat out on trying to achieve a successful restructuring or recapitalization of the CMI Entities. Frankly, the last thing we should be doing at this point is preparing for a forensic examination, in minute detail, over events that have taken place over the past several months. At this point in the restructuring/recapitalization process, the proposed examination would be an enormous distraction and would significantly prejudice the CMI Entities' restructuring and recapitalization efforts."

46 While Mr. McElcheran for the GS Parties submits that the examinations and the scope of the examinations could be managed, in my view, the litigating of the subject matter of the motion would undermine the objective of protecting the CMI Entities while they attempt to restructure. The GS Parties continue to own their shares in CW Investments Co. as does CMI. CMI continues to operate the Specialty TV Business. Furthermore, CMI cannot sell the shares without the involvement of the Monitor and the court. None of these facts have changed. The drag along rights are stayed (although as Mr. McElcheran said, it is the cancellation of those rights that the GS Parties are concerned about.)

47 A key issue will be whether the CMI Parties can then disclaim that Agreement or whether they should be required to perform the obligations which previously bound 441. This issue will no doubt

arise if and when the CMI Entities seek to disclaim the Shareholders Agreement. It is premature to address that issue now. Furthermore, section 32 of the CCAA now provides a detailed process for disclaimer. It states:

> 32.(1) Subject to subsections (2) and (3), a debtor company may -- on notice given in the prescribed form and manner to the other parties to the agreement and the monitor -- disclaim or resiliate any agreement to which the company is a party on the day on which proceedings commence under this Act. The company may not give notice unless the monitor approves the proposed disclaimer or resiliation.
>
> (2) Within 15 days after the day on which the company gives notice under subsection (1), a party to the agreement may, on notice to the other parties to the agreement and the monitor, apply to a court for an order that the agreement is not to be disclaimed or resiliated.
>
> (3) If the monitor does not approve the proposed disclaimer or resiliation, the company may, on notice to the other parties to the agreement and the monitor, apply to a court for an order that the agreement be disclaimed or resiliated.
>
> (4) In deciding whether to make the order, the court is to consider, among other things,
>
> (a) whether the monitor approved the proposed disclaimer or resiliation;
>
> (b) whether the disclaimer or resiliation would enhance the prospects of a viable compromise or arrangement being made in respect of the company; and
>
> (c) whether the disclaimer or resiliation would likely cause significant financial hardship to a party to the agreement.

48 Section 32, therefore, provides the scheme and machinery for the disclaimer of an agreement. If the monitor approves the disclaimer, another party may contest it. If the monitor does not approve the disclaimer, permission of the court must be obtained. It seems to me that the issues surrounding any attempt at disclaimer in this case should be canvassed on the basis mandated by Parliament in section 32 of the amended Act.

49 In my view, the balance of convenience, the assessment of relative prejudice and the relevant merits favour the position of the CMI Entities on this lift stay motion. As to the issue of good faith, the question is whether, absent more, one can infer a lack of good faith based on the facts outlined in the materials filed including the agreed upon admission by the CMI Entities. The onus to lift the stay is on the moving party. I decline to exercise my discretion to lift the stay on this basis.

50 Turning then to the factors listed by Professor McLaren, again I am not persuaded that based

on the current state of affairs, any of the factors are such that the stay should be lifted. In light of this determination, there is no need to address the motion to strike paragraph 1(e) of the GS Parties' main motion.

51 The stay of proceedings in this case is performing the essential function of keeping stakeholders at bay in order to give the CMI Entities a reasonable opportunity to develop a restructuring plan. The motions of the GS Parties are dismissed (with the exception of that portion dealing with paragraph 59 of the Initial Order which is on consent) and the motion of the CMI Entities is granted with the exception of the strike portion which is moot.

52 The Monitor, reasonably in my view, did not take a position on these motions. Its counsel, Mr. Byers, advised the court that the Monitor was of the view that a commercial resolution was the best way to resolve the GS Parties' issues. It is difficult to disagree with that assessment.

S.E. PEPALL J.

cp/e/qlrds/qljxr/qlced/qlaxw/qlcas

1 (2000), 19 C.B.R. (4th) 1.

2 [1990] B.C.J. No. 2384 (C.A.) at p. 4.

3 (2005), 75 O.R. (3d) 5 (C.A.) at para. 36.

4 (2000), 19 C.B.R. (4th) 1.

5 (1993), 17 C.B.R. (3d) 24.

6 Ibid, at p. 32.

7 Supra, note 2

8 (1992) 14 C.B.R. (3d) 303.

9 R.S.O. 1990, c. C.43.

10 Supra, note 6 at paras. 24 and 25.

11 (Aurora: Canada Law Book, looseleaf) at para. 3.3400.

12 (2007), 33 C.B.R. (5th) 50 (Sask. C.A.) at para. 68.

13 Ibid, at para. 68.

14 Supra, note 3.

15 This was 4414641 Canada Inc. but not 4414616 Canada Inc., the company in issue before me.

16 Specifically, GS Capital Partners VI Fund, L.P.

17 5 C.B.R. (5th) 92 at para. 37.

18 Ibid, at para. 37.

19 (1988), 72 C.B.R. (N.S.) 1.

Tab 7

Case Name:

Bank of Montreal v. NFC Acquisition GP Inc.

IN THE MATTER OF a Plan of Compromise or Arrangement of NFC Acquisition GP Inc., NFC Acquisition Corp. and NFC Land Holdings Corp.
RE: Bank of Montreal, Applicant, and NFC Acquisition GP Inc., NFC Acquisition Corp., NFC Land Holdings Corp., New Food Classics, and NFC Acquisition L.P., Respondents

[2012] O.J. No. 785

2012 ONSC 1244

Court Files Nos. CV-12-9554-00CL and CV-12-9616-00CL

Ontario Superior Court of Justice
Commercial List

D.M. Brown J.

Heard: February 22, 2012.
Judgment: February 22, 2012.

(18 paras.)

Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Motion by secured creditor to lift stay of proceedings to permit it to apply for appointment of receiver allowed -- Initial order was made which approved sales process and made of additional commitments under DIP facility available if sales process successful -- Sales process ultimately unsuccessful, DIP lender delivered notice of sales process default and withdrew funding, debtor company's board resigned and debtor company ceased operations -- No alternative to appointing receiver as sales process had fallen apart, DIP lender had served notice of sales process default and debtors had no access to funds -- No prospect of successful CCAA process.

Bankruptcy and insolvency law -- Proceedings -- Practice and procedure -- Stays -- Motion by secured creditor to lift stay of proceedings to permit it to apply for appointment of receiver allowed -- Initial order was made which approved sales process and made of additional commitments under

DIP facility available if sales process successful -- Sales process ultimately unsuccessful, DIP lender delivered notice of sales process default and withdrew funding, debtor company's board resigned and debtor company ceased operations -- No alternative to appointing receiver as sales process had fallen apart, DIP lender had served notice of sales process default and debtors had no access to funds -- No prospect of successful CCAA process.

Motion by a secured creditor for an order lifting the stay of proceedings in the Creditors' Companies Arrangement Act ("CCAA") matter to permit it to apply to appoint a receiver over the assets of the debtor companies. In January 2012, an initial order was made under the CCAA in respect of the debtor companies which approved a sale process in respect of the companies and the availability of additional commitments under the DIP facility which was tied to the success of the sales process. Three offers were received as a result of the sales process. However, two of the bidders ultimately withdrew from the sales process. The remaining bidder was prepared to proceed, but required the DIP lender to advance the remaining $7 million in the DIP facility. The DIP lender delivered notice that a sales process default had occurred under the DIP facility and no further funding was availably. Subsequently, the debtor's board of director's resigned, the employees were advised there was no work and the company ceased operations. The secured creditor, who was also the DIP lender, sought to lift the stay and appoint a receiver. The motion was supported by the monitor and was not opposed by any party.

HELD: Application allowed. There was no alternative to appointing a receiver. The sales process had fallen apart and the DIP lender declined to make further advances and had served a notice of sales process default, which resulted in the debtors having no further access to funds. Furthermore, the board of directors had resigned, which reduced the prospects of a successful CCAA process to nil.

Statutes, Regulations and Rules Cited:

Creditors' Companies Arrangement Act,

Counsel:

E. Lamek and C. Fell, for the Monitor and proposed Receiver, FTI Consulting Canada Inc.

C. Prophet and F. Lamie, for the Applicant, Bank of Montreal.

D. Bish and A. Slavens, for the NFC Debtors.

P. Osborne and B. Gray, for certain Directors of the Debtors.

D. Bulas, for Edgestone Capital.

H. Chaiton, for Westco MultiTemp Distribution Centres Inc.

REASONS FOR DECISION

D.M. BROWN J.:--

I. Motion to lift a *CCAA* stay to appoint a receiver

1 The Bank of Montreal, the senior secured creditor of the debtor respondents, NFC Acquisition GP Inc., NFC Acquisition Corp., NFC Land Holdings Corp., New Food Classics, and NFC Acquisition L.P. (the "Debtors"), moves for an order lifting the stay of proceedings in the *CCAA* matter (CV-12-9554-00CL) to permit it to apply to appoint FTI Consulting Canada Inc. as receiver of all of the property, assets and undertaking of the Debtors.

II. Background events

2 NFC produces ground and formed meats and held a 40% market share of the market for frozen burgers sold in grocery stores. On January 17, 2012 Morawetz J. made an Initial Order under the *CCAA* in respect of NFC Acquisition GP Inc., NFC Acquisition Corp. and NFC Land Holdings Corp. (the "NFC Entities"). Two features of the Initial Order are of particular relevance to this motion. First, the Court approved a sale process in respect of the NFC Entities. Second, under the terms of the approved DIP facility, the availability of additional commitments under the facility beyond the initial $3.5 million was tied to the success of the sales process - if a Sales Process Default occurred, there would be no further availability of funds under the DIP Facility.

3 The Monitor, FTI Consulting Canada Inc., has filed a Third Report dated February 21, 2012 describing the results of the sales process. Three final offers were received by the February 13, 2012 deadline. The Monitor then worked with NFC management to refine the terms of two bids.

4 On February 13 a Major Customer of NFC advised the company that it had one day to match a competitive bid from another supplier of certain products which had proposed to reduce its prices to the Major Customer. The Monitor informed the two final bidders of this development. Between February 13 and 20 discussions took place amongst the Monitor, NFC, the two final bidders and the Major Customer to ascertain whether a transaction could be structured that would result in a going concern sale of the NFC Saskatoon production facility, or possibly both NFC production facilities.

5 Under the terms of the Sales Process NFC had until the close of business on February 17 to put forward to BMO, in its capacity as DIP Lender, a form of agreement of purchase and sale so that the bank could determine whether it would make further advances under the DIP Facility.

6 On February 17 one of the two final bidders withdrew from the sales process. The remaining bidder was prepared to proceed with an amended offer, but one which would require the DIP

Lender to advance the remaining $7 million in the DIP Facility.

7 On Monday, February 20 BMO delivered a notice that a Sales Process Default had occurred under the DIP Facility. Further funding was no longer available to the Debtors. That evening the Board of NFC resigned *en masse*. Management posted notices at the Debtors' facilities advising the employees that no work would be available for them the next day, Tuesday, February 21. That has led the Monitor to make the following recommendation:

> In light of the delivery of the Default Notice by BMO, the resignation of the NFC Board of Directors and management, the lack of funding for NFC's business and the perishable nature of NFC's inventory, the Monitor is of the view that it is vital to have an immediate and orderly shut-down of the NFC manufacturing operations and a swift transition to a court-appointed receivership of the assets of NFC. The Monitor is hopeful that a buyer for the closed NFC manufacturing faculties can be quickly identified among the parties that participated in the Transaction Process, and that the manufacturing facilities can be sold on a turn-key basis in a short period of time, rather than liquidated.
>
> The Monitor has prepared a cash flow projection for the conduct of a shut-down receivership for the assets of NFC, which would be funded pursuant to Receiver's Certificates. BMO has agreed to fund such Receiver Certificate amounts on a basis and priority consistent with the existing DIP Facility and DIP Charge.

8 As of February 20, 2012 the Debtors owed BMO approximately $24.5 million. BMO is the senior secured creditor and the DIP Lender. The priority position of the BMO is not in dispute.

9 BMO applies for a lifting of the stay in the *CCAA* proceeding and the appointment of a receiver over the Debtors to secure the property and assets of the Debtors, including the perishable food inventory, and to proceed with an orderly realization and maximization of the value of the Debtors' assets. Paragraph 36(b) of the Initial Order provided that upon the occurrence of an event of default under the Definitive Documents, BMO, as DIP Lender, could apply to the court for the appointment of a receiver. A Sale Process Default is a Specified Event of Default, and BMO gave notice of such a default this past Monday.

10 FTI has consented to act as receiver of the Debtors.

II. Analysis

11 In *Canwest Global Communications Corp. (Re)* (2009), 61 C.B.R. (5th) 200 (S.C.J.) Pepall J. summarized the principles which should guide a court when facing a request to lift a stay of proceedings under the *CCAA*:

32 As with the imposition of a stay, the lifting of a stay is discretionary. There are no statutory guidelines contained in the Act. According to Professor R.H. McLaren in his book "Canadian Commercial Reorganization: Preventing Bankruptcy", an opposing party faces a very heavy onus if it wishes to apply to the court for an order lifting the stay. In determining whether to lift the stay, the court should consider whether there are sound reasons for doing so consistent with the objectives of the CCAA, including a consideration of the balance of convenience, the relative prejudice to parties, and where relevant, the merits of the proposed action: *ICR Commercial Real Estate (Regina) Ltd. v. Bricore Land Group Ltd.*, [2007] S.J. No. 313. That decision also indicated that the judge should consider the good faith and due diligence of the debtor company.

33 Professor McLaren enumerates situations in which courts will lift a stay order. The first six were cited by Paperny J. in 2000 in *Re Canadian Airlines Corp.*, [2000] A.J. No. 1692, and Professor McLaren has added three more since then. They are:

1. When the plan is likely to fail.
2. The applicant shows hardship (the hardship must be caused by the stay itself and be independent of any pre-existing condition of the applicant creditor).
3. The applicant shows necessity for payment (where the creditors' financial problems are created by the order or where the failure to pay the creditor would cause it to close and thus jeopardize the debtor's company's existence).
4. The applicant would be significantly prejudiced by refusal to lift the stay and there would be no resulting prejudice to the debtor company or the positions of creditors.
5. It is necessary to permit the applicant to take steps to protect a right which could be lost by the passing of time.
6. After the lapse of a significant time period, the insolvent is no closer to a proposal than at the commencement of the stay period.
7. There is a real risk that a creditor's loan will become unsecured during the stay period.
8. It is necessary to allow the applicant to perfect a right that existed prior to the commencement of the stay period.
9. It is in the interests of justice to do so.

12 Turning to the present case, BMO gave notice of its motion by e-mail yesterday to those on the Service List in the *CCAA* proceedings. Under the circumstances such short notice was

necessary, and I validate the short service.

13 No party has appeared to oppose the motions to lift the stay and appoint a receiver. The Monitor supports the lifting of the stay and the appointment of a receiver. The Monitor also advised that the Saskatoon local of the employees' union does not oppose the orders sought.

14 Quite frankly, on the evidence before me, I see no other alternative than appointing a receiver. The Sales Process has fallen apart as a result of the inability to work out an arrangement with the Major Customer. Consistent with the terms of the DIP Facility approved in the Initial Order, BMO, as DIP Lender, has declined to make further advances and has served a notice of Sales Process Default. As a result, the Debtors have no access to further working funds.

15 The Board of the Debtors resigned *en masse* two days ago; the Debtors are rudderless, reducing the prospects of a viable proposal in the *CCAA* process down to nil. The Monitor advises that management instructed employees not to report to work yesterday, so the Debtors are not carrying on any business at the moment. A significant inventory of meat products sits in the Saskatoon facility, although the Monitor advises that any fresh meat either has been shipped out or frozen. In a very real sense the Debtors have ceased carrying on business as a going concern.

16 The appointment of a receiver is required to stabilize this situation for the benefit of all stakeholders of the Debtors.

17 BMO has filed a draft receivership order which contains some amendments to the Commercial List Model Receivership Order. I reviewed the proposed amendments with counsel in open court and heard submissions and explanations on some of the proposed changes. No party opposes the proposed draft receivership order. BMO and the receiver clarified that with respect to paragraphs 24 and 26 of the proposed order, the receiver will be bound by the terms of the February 7, 2012 letter from the Monitor to Westco which was placed before the court on the motion to obtain the February 16, 2012 extension order. BMO and the receiver confirmed, at the request of Debtors' counsel, that the orders sought would not terminate the existing *CCAA* proceedings.

18 In sum, I conclude that the pressing circumstances in which the Debtors find themselves make it just and reasonable to appoint a receiver over them. I therefore grant BMO's motion to lift the stay of proceedings in the *CCAA* matter, and I grant the Bank's motion to appoint FTI Consulting as receiver over the Debtors. I have signed the draft orders submitted by BMO.

D.M. BROWN J.

cp/e/qlacx/qljxr/qljxh/qlana

Tab 8

Indexed as:

Campeau v. Olympia & York Developments Ltd.

Between
Robert Campeau, Robert Campeau Inc., 75090 Ontario Inc., and Robert Campeau Investments Inc., Plaintiffs, and Olympia & York Developments Limited, 857408 Ontario Inc., and National Bank of Canada, Defendants

[1992] O.J. No. 1946

14 C.B.R. (3d) 303

14 C.P.C. (3d) 339

1992 CarswellOnt 185

35 A.C.W.S. (3d) 679

Action Nos. 92-CQ-19675 and B-125/92

Ontario Court of Justice - General Division
Toronto, Ontario

Blair J.

September 21, 1992

(14 pp.)

Practice -- Insolvency -- Stay of proceedings -- General principles -- Defendant protected by Companies' Creditors Arrangement Act.

Application for lifting a stay imposed by an order granted under section 11 of the Companies' Creditors Arrangement. The second defendant also applied for an order staying the separate action against it. The plaintiffs' action against the defendants was for the sum of $1 billion for damages allegedly suffered following breaches of contract and fiduciary duties by the defendants. The plaintiffs' claim against the second defendant directly involved certain acts of the first defendant.

HELD: Application dismissed. The second defendants' application allowed. There might be great prejudice to the first defendant if its attention was diverted from the corporate restructuring process. There was no prejudice to the plaintiffs whose rights were not precluded but merely postponed. The courts' power under section 11 extended to restraining conduct which could impair the debtor's ability to focus on the business purpose of negotiating a compromise.

STATUTES, REGULATIONS AND RULES CITED:

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.
Courts of Justice Act, R.S.O. 1990, c. C-43, s. 106.
Personal Property Security Act, R.S.O. 1990, c. P.10, s. 17(1).
Ontario Rules of Civil Procedure, Rule 6.01(1).

Stephen T. Goudge, Q.C. and Peter C. Wardle, for the Plaintiffs.
Peter F.C. Howard, for the Defendant, National Bank of Canada.
Yoine Goldstein, for the Defendants, Olympia & York Developments Limited and 857408 Ontario Inc.

BLAIR J.:-- These Motions raise questions regarding the Court's power to stay proceedings. Two competing interests are to be weighed in the balance, namely,

a) the interests of a debtor which has been granted the protection of the Companies Creditors Arrangement Act, R.S.C. 1985, c. C-36, and the "breathing space" offered by a s. 11 stay in such proceedings, on the one hand, and,
b) the interests of a unliquidated contingent claimant to pursue an action against that debtor and an arms length third party, on the other hand.

At issue is whether the Court should resort to an interplay between its specific power to grant a stay, under s. 11 of the CCAA, and its general power to do so under the Courts of Justice Act, R.S.O. 1990, Chap C-43 in order to stay the action completely; or whether it should lift the s. 11 stay to allow the action to proceed; or whether it should exercise some combination of these powers.

Background and Overview

This action was commenced on April 28, 1992, and the Statement of Claim was served before May 14, 1992, the date on which an Order was made extending the protection of the CCAA to Olympia & York Developments Limited and a group of related companies ("Olympia & York", or "O & Y" or the "Olympia & York Group").

The plaintiffs are Robert Campeau and three Campeau family corporations which, together with Mr. Campeau, held the control block of shares of Campeau Corporation. Mr. Campeau is the former Chairman and CEO of Campeau Corporation, said to have been one of North America's largest real estate development companies, until its recent rather high profile demise. It is the fall of that empire which forms the subject matter of the lawsuit.

The Claim against the Olympia & York Defendants

The story begins, according to the Statement of Claim, in 1987, after Campeau Corporation had completed a successful leveraged buy-out of Allied Stores Corporation, a very large retailer based in the United States. Olympia & York had aided in funding the Allied takeover by purchasing half of Campeau Corporation's interest in the Scotia Plaza in Toronto and subsequently also purchasing 10% of the shares of Campeau Corporation. By late 1987, it is alleged, the relationship between Mr. Campeau and Mr. Paul Reichman (one of the principals of Olympia & York) had become very close, and an agreement had been made whereby Olympia & York was to provide significant financial support, together with the considerable expertise and the experience of its personnel, in connection with Campeau Corporation's subsequent bid for control of Federated Stores Inc (a second major U.S. department store chain). The story ends, so it is said, in 1991 after Mr. Campeau had been removed as Chairman and CEO of Campeau Corporation and that Company, itself, had filed for protection under the CCAA (from which it has since emerged, bearing the new name of Camdev Corp.).

In the meantime, un September, 1989, the Olympia & York defendants, through Mr. Paul Reichman, had entered unto a shareholders' agreement with the plaintiffs in which, it us further alleged, Olympia & York obliged itself to develop and implement expeditiously a viable restructuring plan for Campeau Corporation. The allegation that Olympia & York breached this obligation by failing to develop and implement such a plan, together with the further assertion that the O & Y Defendants actually frustrated Mr. Campeau's efforts to restructure Campeau Corporation's Canadian real estate operation, lies at the heart of the Campeau action. The Plaintiffs plead that as a result they have suffered very substantial damages, including the loss of the value of their shares in Campeau Corporation, the loss of the opportunity of completing a refinancing deal with the Edward DeBartolo Corporation, and the loss of the opportunity on Mr. Campeau's part to settle his personal obligations on terms which would have preserved his position as Chairman and CEO and majority shareholder of Campeau Corporation.

Damages are claimed in the amount of $1 billion, for breach of contract or, alternatively, for breach of fiduciary duty. Punitive damages in the amount of $250 million ore also sought.

The Claim against National Bank of Canada

Similar damages, in the amount of $1 billion (but no punitive damages), are claimed against the Defendant National Bank of Canada, as well. The causes of action against the Bank are framed as breach of fiduciary duty, negligence, and breach of the provisions of S. 17(1) of the Personal

Property Security Act. They arise out of certain alleged acts of misconduct on the part of the Bank's representatives on the Board of Directors of Campeau Corporation.

In 1988 the Plaintiffs had pledged some of their shares in Campeau Corporation to the Bank as security for a loan advanced in connection with the Federated Stores transaction. In early 1990, one of the Plaintiffs defaulted on its obligations under the loan and the Bank took control of the pledged shares. Thereafter, the Statement of Claim alleges, the Bank became more active in the management of Campeau, through its nominees on the Board.

The Bank had two such nominees. Olympia & York had three. There were twelve directors in total. What is asserted against the Bank is that its directors, in cooperation with the Olympia & York directors, acted in a way to frustrate Campeau's restructuring efforts and favoured the interests of the Bank as a secured lender rather than the interests of Campeau Corporation, of which they were directors. In particular, it is alleged that the Bank's representatives failed to ensure that the DeBartolo refinancing was implemented and, indeed, actively supported Olympia & York's efforts to frustrate it, and in addition, that they supported Olympia & York's efforts to refuse to approve or delay the sale of real estate assets.

THE MOTIONS

There are two motions before me.

The first motion is by the Campeau Plaintiffs to lift the stay imposed by the Order of May 14, 1992 under the CCAA and to allow them to pursue their action against the Olympia & York defendants. They argue that a plaintiff's right to proceed with an action ought not lightly to be precluded; that this action is uniquely complex and difficult; and that the claim is better and more easily dealt with in the context of the action rather than in the context of the present CCAA proceedings. Counsel acknowledge that the factual bases of the claims against Olympia & York and the Bank are closely intertwined and that the claim for damages is the same, but argue that the causes of action asserted against the two are different. Moreover, they submit, this is not the usual kind of situation where a stay is imposed to control the process and avoid inconsistent findings when the same parties are litigating the same issues in parallel proceedings.

The second motion is by National Bank, which of course opposes the first motion, and which seeks an order staying the Campeau' action as against it as well, pending the disposition of the CCAA proceedings. Counsel submits that the factual substratum of the claim against the Bank is dependent entirely on the success of the allegations against the Olympia & York defendants, and that the claim against those defendants is better addressed within the parameters of the CCAA proceedings. He points out also that if the action were to be taken against the Bank alone, his client would be obliged to bring Olympia & York back into the action as third parties in any event.

The Power to Stay

The Court has always had an inherent jurisdiction to grant a stay of proceedings whenever it is just and convenient to do so, in order to control its process or prevent an abuse of that process: see Canada Systems Group (Est) Ltd. v. Allendale Mutual Insurance Co. (1982), 29 C.P.C. 60 (H.C.), and cases referred to therein. In the civil context, this general power is also embodied in the very broad terms of s. 106 of the Courts of Justice Act, R.S.O. 1990, Chap. C. 43, which provides as follows:

> s. 106. A court, on its own initiative or on motion by any person, whether or not a party, may stay any proceeding in the court on such terms as are considered just.

Recently, Mr. Justice O'Connell has observed that this discretionary power is "highly dependent on the facts of each particular case": Arab Monetary Fund v. Hashim (unreported), [1992] O.J. No. 1330.

Apart from this inherent and general jurisdiction to stay proceedings, there are many instances where the Court is specifically granted the power to stay in a particular context, by virtue of statute or under the Rules of Civil Procedure. The authority to prevent multiplicity of proceedings in the same court, under Rule 6.01(1), is an example of the latter. The power to stay judicial and extra-judicial proceedings under s. 11 of the CCAA, is an example of the former. Section 11 of the CCAA provides as follows:

> s. 11 Notwithstanding anything in the Bankruptcy Act or the Winding-up Act, whenever an application has been made under this Act in respect of any company, the court, on the application of any person interested in the matter, may, on notice to any other person or without notice as it may see fit,
>
> (a) make an order staying, until such time as the court may prescribe or until any further order, all proceedings taken or that might be taken in respect of the company under the Bankruptcy Act and the Winding-up Act or either of them;
> (b) restrain further proceedings in any action, suit or proceeding against the company on such terms as the court sees fit; and
> (c) make an order that no suit, action or other proceeding shall be proceeded with or commenced against the company except with the leave of the court and subject to such terms as the court imposes.

The Power to Stay in the Context of CCAA Proceedings

By its formal title the CCAA is known as "An Act to facilitate compromises and arrangements between companies and their creditors". To ensure the effective nature of such a "facilitative" process it is essential that the debtor company be afforded a respite from the litigious and other rights being exercised by creditors, while it attempts to carry on as a going concern and to

negotiate an acceptable corporate restructuring arrangement with such creditors.

In this respect it has been observed that the CCAA is "to be used as a practical and effective way of restructuring corporate indebtedness.": see the case comment following the report of Norcen Energy Resources Ltd. v. Oakwood Petroleums Ltd. (1988), 72 C.B.R. (N.S.) 1 (Q.B.), and the approval of that remark as "a perceptive observation about the attitude of the courts" by Gibbs J.A. in Quintette Coal Ltd. v. Nippon Steel Corp. (1990), 51 B.C.L.R. (2d) 105 at p. 113 (B.C.C.A.).

Gibbs J.A. continued with this comment:

> To the extent that a general principle can be extracted from the few cases directly on point, and the others in which there is persuasive obiter, it would appear to be that the courts have concluded that under s. 11 there is a discretionary power to the or company the effect of which is, or would be, seriously to impair the ability of the debtor company to continue in business during the compromise or arrangement negotiating period. (emphasis added)

I agree with those sentiments and would simply add that, in my view, the restraining power extends as well to conduct which could seriously impair the debtor's ability to focus and concentrate its efforts on the business purpose of negotiating the compromise or arrangement.

I must have regard to these foregoing factors while I consider, as well, the general principles which have historically governed the Court's exercise of its power to stay proceedings. These principles were reviewed by Mr. Justice Montgomery in Canada Systems Group (EST) Ltd. v. Allendale Mutual Insurance, supra (a "Mississauga Derailment" case), at pp. 65-66. The balance of convenience must weigh significantly in favour of granting the stay, as a party's right to have access to the courts must not be lightly interfered with. The Court must be satisfied that a continuance of the proceeding would serve as an injustice to the party seeking the stay, in the sense that it would be oppressive or vexatious or an abuse of the process of the court in some other way. The stay must not cause an injustice to the plaintiff. On all of these issues the onus of satisfying the Court is on the party seeking the stay: see also, Weight Watchers International Inc. v. Weight Watchers of Ont. Ltd. (1972), 25 D.L.R. (3d) 419, 5 C.P.R. (2d) 122, appeal allowed by consent without costs (sub nom. Weight Watchers of Ont. Ltd. v. Weight Watchers Int. Inc.) 42 D.L.R. (3d) 320n., 10 C.P.R. (2d) 96n (Fed. C.A.), where Mr. Justice Heald recited the foregoing principles from Empire Universal Films Ltd. et. al. v. Rank et al., [1947] O.R. 775 at p. 779.

Canada Systems Group (EST) Ltd. v. Allendale Mutual Insurance, supra, is a particularly helpful authority, although the question in issue there was somewhat different than those in issue on these motions. The case was one of several hundred arising out of the Mississauga derailment in November 1979, all of which actions were being case managed by Montgomery J. These actions were all part of what Montgomery J. called "a controlled stream" of litigation involving a large number of claims and innumerable parties. Similarly, while the Olympia & York proceedings under

the CCAA do not involve a large number of separate actions, they do involve numerous Applicants, an even larger number of very substantial claimants, and a diverse collection of intricate and broad sweeping issues. In that sense the CCAA proceedings are a controlled stream of litigation. Maintaining the integrity of the flow is an important consideration.

DISPOSITION

I have concluded that the proper way to approach this situation is to continue the stay imposed under the CCAA prohibiting the action against the Olympia & York defendants, and in addition, to impose a stay, utilizing the Court's general jurisdiction in that regard, preventing the continuation of the action against National Bank as well. The stays will remain in effect for as long as the s. 11 stay remains operative, unless otherwise provided by order of this Court.

In making these orders, I see no prejudice to the Campeau Plaintiffs. The processing of their action is not being precluded, but merely postponed. Their claims may, indeed, be addressed more expeditiously than might have otherwise been the case, as they may be dealt with -- at least for the purposes of that proceeding in the CCAA proceeding itself. On the other hand, there might be great prejudice to Olympia & York if its attention is diverted from the corporate restructuring process and it is required to expend time and energy in defending an action of the complexity and dimension of this one. While there may not be a great deal of prejudice to National Bank in allowing the action to proceed against it, I am satisfied that there is little likelihood of the action proceeding very far or very effectively unless and until Olympia & York -- whose alleged misdeeds are the real focal point of the attack on both sets of defendants -- is able to participate.

In addition to the foregoing, I have considered the following factors in the exercise of my discretion:

1. Counsel for the Plaintiffs argued that the Campeau claim must be dealt with, either in the action or in the CCAA proceedings and that it cannot simply be ignored. I agree. However, in my view, it is more appropriate, and in fact is essential, that the claim be addressed within the parameters of the CCAA proceedings rather than outside, in order to maintain the integrity of those proceedings. Were it otherwise, the numerous creditors in that mammoth proceeding would have no effective way of assessing the weight to be given to the Campeau claim in determining their approach to the acceptance or rejection of the Olympia & York Plan filed under the Act.
2. In this sense, the Campeau claim -- like other secured, undersecured, unsecured, and contingent claims -- must be dealt with as part of a "controlled stream" of claims that are being negotiated with a view to facilitating a compromise and arrangement between Olympia & York and its creditors. In weighing "the good management" of the two sets of proceedings -- i.e. the action and the CCAA proceeding -- the scales tip in favour of dealing with the Campeau claim in the

context of the latter: see HM Attorney General v. Arthur Andersen & Co. (United Kingdom) and other, [1989] E.C.C. 224 (Eng. C.A.), cited in Arab Monetary Fund v. Hashim, supra.

I am aware, when saying this that in the Initial Plan of Compromise and Arrangement filed by the Applicants with the Court on August 21, 1992, the Applicants have chosen to include the Campeau plaintiffs amongst those described as "Persons not Affected by the Plan". This treatment does not change the issues, in my view, as it is up to the Applicants to decide how they wish to deal with that group of "creditors" in presenting their Plan, and up to the other creditors to decide whether they will accept such treatment. In either case, the matter is being dealt with, as it should be, within the context of the CCAA proceedings.

3. Pre-judgment interest will compensate the Plaintiffs for any delay caused by the imposition of the stays, should the action subsequently proceed and the Plaintiffs ultimately be successful.
4. While there may not be great prejudice to National Bank if the action were to continue against it alone and the causes of action asserted against the two groups of defendants are different, the complex factual situation is common to both claims and the damages are the same. The potential of two different inquiries at two different times into those same facts and damages is not something that should be encouraged. Such multiplicity of inquiries should in fact be discouraged, particularly where -- as is the case here -- the delay occasioned by the stay is relatively short (at least in terms of the speed with which an action like this Campeau action is likely to progress.

CONCLUSION

Accordingly, an Order will go as indicated, dismissing the Notion of the Campeau Plaintiffs and allowing the Motion of National Bank. Each stay will remain in effect until the expiration of the stay period under the CCAA unless extended or otherwise dealt with by the court prior to that time. Costs to the Defendants in any event of the cause in the Campeau action. I will fix the amounts if counsel wish me to do so.

BLAIR J.

Tab 9

Liquor Control Board of Ontario v. Magnotta Winery Corporation et al.; Attorney General of Ontario, Intervenor [Indexed as: Liquor Control Board of Ontario v. Magnotta Winery Corp.]

97 O.R. (3d) 665

Ontario Superior Court of Justice,
Divisional Court,

Carnwath, Bellamy and Pierce JJ.

June 12, 2009

Administrative law -- Freedom of information -- Materials prepared for mediation of court proceedings between LCBO and respondent exempted from disclosure by common-law settlement privilege and s. 19(b) of Freedom of Information and Protection of Privacy Act -- Freedom of Information and Protection of Privacy Act, R.S.O. 1990, c. F.31, s. 19.

Evidence -- Privilege -- Settlement privilege -- Materials prepared for mediation of court proceedings between LCBO and respondent exempted from disclosure by common-law settlement privilege and s. 19(b) of Freedom of Information and Protection of Privacy Act -- Freedom of Information and Protection of Privacy Act, R.S.O. 1990, c. F.31, s. 19.

The Information and Privacy Commissioner held that certain materials (the "disputed records") prepared for the mediation of seven court proceedings between the applicant and the respondent Magnotta were not exempt from release under s. 19 of the Freedom of Information and Protection of Privacy Act and that the common-law settlement privilege did not attach to the disputed records. The applicant applied for judicial review of that decision.

Held, the application should be granted.

Common-law settlement privilege exempted the disputed records from disclosure. The communications between the applicant and Magnotta originated in [page666] confidence. They were the subject of a strong confidentiality agreement. In order for parties to arrive at a settlement, they must be assured of confidentiality so that discussions can be free and frank. There is a significant public interest in protecting the confidentiality of settlement discussions to make the

process as effective as possible. As the identity and motivation of the requester of the disputed records were unknown, the competing public policy interests were those created by FIPPA versus the interest in promoting settlements of disputes through confidential settlement negotiations. In the circumstances of this case, the public policy interest in encouraging settlement as embodied in the common-law concept of settlement privilege trumped the public policy interest in transparency of government action.

Section 19(b) of FIPPA exempts from disclosure records that were prepared by or for Crown counsel for use in giving legal advice or in contemplation of or for use in litigation. The qualification of the applicant's counsel as "Crown counsel" was conceded for the purposes of the s. 19 exemption. The applicant used the disputed records (which included its mediation briefs, legal opinions and unfiled affidavit material) in mediating seven court proceedings which were then ongoing between it and Magnotta. Mediation is an integral part of the litigation process. The applicant was entitled to withhold disclosure of the disputed documents.

Cases referred to

2747-3174 Quebec Inc. v. Quebec (Regis des permis d'alcool), [1996] 3 S.C.R. 919, [1996] S.C.J. No. 112, 140 D.L.R. (4th) 577, 205 N.R. 1, J.E. 96-2212, 42 Admin. L.R. (2d) 1, 66 A.C.W.S. (3d) 1012; Bard v. Longevity Acrylics Inc., [2002] O.J. No. 1373, [2002] O.T.C. 249, 18 C.C.E.L. (3d) 256, 114 A.C.W.S. (3d) 166 (S.C.J.); Blank v. Canada (Minister of Justice), [2006] 2 S.C.R. 319, [2006] S.C.J. No. 39, 2006 SCC 39, 270 D.L.R. (4th) 257, 352 N.R. 201, J.E. 2006-1723, 47 Admin. L.R. (4th) 84, 51 C.P.R. (4th) 1, 40 C.R. (6th) 1, 150 A.C.W.S. (3d) 401, EYB 2006-109504; General Accident Assurance Co. v. Chrusz (1999), 45 O.R. (3d) 321, [1999] O.J. No. 3291, 180 D.L.R. (4th) 241, 124 O.A.C. 356, 38 C.P.C. (4th) 203, 92 A.C.W.S. (3d) 26 (C.A.); I. Waxman & Sons Ltd. v. Texaco Canada Ltd., [1968] 2 O.R. 452, [1968] O.J. No. 1174, 69 D.L.R. (2d) 543 (C.A.), affg [1968] 1 O.R. 642, [1968] O.J. No. 1068, 67 D.L.R. (2d) 295 (H.C.J.); Kelvin Energy Ltd. v. Lee , [1992] 3 S.C.R. 235, [1992] S.C.J. No. 88, 97 D.L.R. (4th) 616, 143 N.R. 191, J.E. 92-1625, 51 Q.A.C. 49, 36 A.C.W.S. (3d) 362; M. (A.) v. Ryan, [1997] 1 S.C.R. 157, [1997] S.C.J. No. 13, 143 D.L.R. (4th) 1, 207 N.R. 81, [1997] 4 W.W.R. 1, J.E. 97-408, 85 B.C.A.C. 81, 29 B.C.L.R. (3d) 133, 34 C.C.L.T. (2d) 1, 8 C.P.C. (4th) 1, 4 C.R. (5th) 220, 42 C.R.R. (2d) 37; Middelkamp v. Fraser Valley Real Estate Board, [1992] B.C.J. No. 1947, 96 D.L.R. (4th) 227, 17 B.C.A.C. 134, 71 B.C.L.R. (2d) 276, 10 C.P.C. (3d) 109, 45 C.P.R. (3d) 213, 35 A.C.W.S. (3d) 814 (C.A.); Ontario (Attorney General) v. Ontario (Information and Privacy Commission, Inquiry Officer) (2002), 62 O.R. (3d) 167, [2002] O.J. No. 4596, 220 D.L.R. (4th) 467, 167 O.A.C. 125, 48 Admin. L.R. (3d) 279, 22 C.P.R. (4th) 169, 118 A.C.W.S. (3d) 642, 56 W.C.B. (2d) 72 (C.A.), affg [2001] O.J. No. 4876, 208 D.L.R. (4th) 327, 152 O.A.C. 145, 41 Admin. L.R. (3d) 117, 16 C.P.R. (4th) 1, 110 A.C.W.S. (3d) 6, 52 W.C.B. (2d) 157 (D iv. Ct.) (sub nom. Ontario (Attorney General) v. Big Canoe); Ontario (Children's Lawyer) v. Ontario (Information and Privacy Commissioner) (2005), 75 O.R. (3d) 309, [2005] O.J. No. 1426, 253 D.L.R. (4th) 489, 196 O.A.C. 350, 29 Admin. L.R. (4th) 86, 17 R.F.L. (6th) 32, 138 A.C.W.S. (3d) 778 (C.A.), affg (2003), 66 O.R. (3d) 692,

[2003] O.J. No. 3522, 231 D.L.R. (4th) 727, 177 O.A.C. 1, 8 Admin. L.R. (4th) 251, 45 R.F.L. (5th) 285, 125 A.C.W.S. (3d) 193 (Div. Ct.); Rogacki v. Belz (2003), 67 O.R. (3d) 330, [2003] O.J. No. 3809, 232 D.L.R. (4th) 523, 41 C.P.C. (5th) 78, 125 A.C.W.S. (3d) 806 (C.A.); [page667] Rudd v. Trossacs Investments Inc. (2006), 79 O.R. (3d) 687, [2006] O.J. No. 922, 265 D.L.R. (4th) 718, 208 O.A.C. 95, 27 C.P.C. (6th) 147, 146 A.C.W.S. (3d) 224 (Div. Ct.); Rush & Tompkins Ltd. v. Greater London Council, [1989] 1 A.C. 1280, [1988] 3 All E.R. 737, 43 Build. L.R. 1, 22 Con. L.R. 114 (H.L.); Slavutych v. Baker, [1976] 1 S.C.R. 254, [1975] S.C.J. No. 29, 55 D.L.R. (3d) 224, 3 N.R. 587, [1975] 4 W.W.R. 620, 75 CLLC Â14,263 at 497, 38 C.R.N.S. 306; Sparling v. Southam Inc. (1988), 66 O.R. (2d) 225, [1988] O.J. No. 1745, 41 B.L.R. 22, 12 A.C.W.S. (3d) 205 (H.C.J.)

Statutes referred to

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Rules and regulations referred to

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APPLICATION for judicial review of decisions of the Information and Privacy Commissioner.

Jill Dougherty and April Brousseau, for applicant.

Ian Roher, for respondents Magnotta Group of Companies.

William Challis and Allison Knight, for respondent Information and Privacy Commissioner.

Leslie McIntosh and Erin Rizok, for intervenor Attorney General of Canada.

The judgment of the court was delivered by

CARNWATH J.: --

Overview

[1] The Liquor Control Board of Ontario (the "LCBO") applies for judicial review of two decisions of the Information and Privacy Commissioner of Ontario (the "IPC/Commissioner"). The decisions relate to some of the mediation materials (the "disputed records") which were the subject of a confidentiality [page668] agreement prepared for the mediation of seven court proceedings between the LCBO and the respondent, Magnotta companies ("Magnotta"). The IPC held that the disputed records were not exempt from release under s. 19 of the Freedom of Information and Protection of Privacy Act, R.S.O. 1990, c. F.31 ("FIPPA").

[2] Section 19 of FIPPA provides an exemption which allows an institution to refuse to disclose certain records, as follows:

> 19. A head may refuse to disclose a record,
>
> (a) that is subject to solicitor-client privilege;
> (b) that was prepared by or for Crown counsel for use in giving legal advice or in contemplation of or for use in litigation . . .

[3] The first branch of s. 19 ("Branch 1") exempts from disclosure communications that fall within the solicitor-client privilege. The second branch ("Branch 2") exempts from disclosure records that were prepared by or for Crown counsel for use in giving legal advice or in contemplation of or for use in litigation.

[4] Many of the disputed records in question were prepared by the LCBO's counsel, whose qualification as "Crown counsel" is conceded for purposes of s. 19 exemption. The disputed records were prepared for a mediation and settlement, if possible, of a number of court proceedings which were then ongoing between the LCBO and Magnotta. The LCBO used the disputed records (which included its mediation briefs, legal opinions and unified affidavit materials) in mediating the court proceedings. Also in the possession of the LCBO were mediation materials prepared by Magnotta for use in the mediation. The LCBO alleges it intended to use its materials in future steps in the litigation if the mediation was unsuccessful. The LCBO also takes the position that those records, including the Magnotta material, were prepared by or for Crown counsel, for use in litigation, both

at the mediation stage and at later stages in the litigation, if necessary.

[5] Magnotta has supported the LCBO throughout the dealings with the IPC and adopts its submissions.

[6] In two long and detailed orders, Order P0-2405 and Reconsideration Order PO-2538-R, the IPC ruled that common-law settlement privilege did not attach to the disputed records, nor did the second branch of s. 19 of FIPPA ("prepared by or for Crown counsel . . .") exempt the records from disclosure.

[7] The LCBO, Magnotta and the Attorney General for Ontario (the "Intervenor") all seek an order in the nature of certiorari, quashing or setting aside the IPC's orders as they relate to the disputed records. [page669]

[8] These applications raise two questions:

(a) Does common-law settlement privilege exempt the disputed records from disclosure?
(b) Are records prepared by or for Crown counsel, in respect of the mediation and settlement of ongoing litigation, exempt from disclosure under s. 19 of FIPPA?

My answer to each of these questions is "Yes".

Background Facts

[9] Between 1996 and 2000, Magnotta commenced two judicial review applications and a defamation action against the LCBO, and the LCBO commenced four related defamation actions against Magnotta. Two of those defamation actions were subject to case management and mandatory mediation under the Rules of Civil Procedure, R.R.O. 1990, Reg. 194, as amended, rule 24.1 ("Rules").

[10] Between 1997 and 2000, the LCBO and Magnotta made several efforts to resolve all the litigation between them by means of mediation and a number of informal settlement attempts. Ultimately, the parties arranged for a further mediation before the Honourable Mr. George Adams with respect to all the applications and actions between the parties.

[11] In order to participate in the mediation, all parties were required to execute a mediation agreement which included the following confidentiality provisions:

> Statements made and documents produced in the mediation session and not otherwise discoverable shall not be subject to disclosure through discovery or any other process; shall be confidential; and shall not be admissible into evidence for any purpose, including impeaching credibility;

[12] Prior to the mediation sessions, both parties filed mediation materials. The LCBO filed two mediation briefs (one with respect to the judicial reviews and the other with respect to the defamation actions) and a number of affidavits and legal opinions, all of which were prepared by external counsel for use in the litigation with Magnotta. Magnotta, in turn, filed mediation materials which ultimately found their way into the LCBO's possession. The IPC found those Magnotta documents in the custody and control of the LCBO not to be exempt from disclosure to the Requester.

[13] The LCBO and Magnotta succeeded in reaching a mediated settlement. External counsel for the parties corresponded after the mediation throughout the remainder of 2000 and most of 2001 for the purpose of drafting the Minutes of Settlement and finalizing [page670] and implementing the terms of the settlement. The parties then executed Minutes of Settlement, which contained extensive confidentiality provisions. During that period, the litigation between the parties remained outstanding. None of the actions or judicial review applications was dismissed until January of 2002.

[14] The LCBO subsequently received a request under FIPPA from an unidentified Requester, seeking access to "a copy of the complete record of the mediated settlement between Magnotta and the LCBO, including copies of all agreements pertaining to the mediated settlement, all Minutes of Settlement between the parties and all related documentation pertaining to the mediated settlement".

[15] The LCBO granted partial access to the records sought but denied access to the remainder of the records pursuant to a number of exemptions under FIPPA, including s. 19. The LCBO notified Magnotta of the request, as an affected party, and Magnotta also opposed the release of the disputed records. The records to which the LCBO denied access and which are in issue in this application consist of:

(a) the mediation briefs and other mediation materials (including affidavits and legal opinions) prepared by the LCBO's external counsel and used in the mediation of the litigation between the LCBO and Magnotta;
(b) a chronology prepared by Magnotta's counsel, which was also used in the mediation;
(c) the Minutes of Settlement reached in that mediation; and
(d) the correspondence relating to finalizing and implementing the Minutes of Settlement.

[16] The Requester appealed the LCBO's decision to the IPC. The IPC wrote to the LCBO and Magnotta (as an affected party), inviting them to make representations and enclosing materials explaining the IPC's procedures. Those materials indicated (among other things) that representations could include unsworn or sworn statements of fact and that "affidavits are optional, unless the adjudicator explicitly requires them". Both the LCBO and Magnotta made extensive submissions to the IPC and provided supporting documents and jurisprudence. Neither Magnotta nor the LCBO

filed affidavit materials.

[17] The LCBO took the position that the disputed records in issue were exempt under the second branch of s. 19 of FIPPA, since they had been prepared by or for Crown counsel, for use in the litigation between the LCBO and Magnotta, both in order to [page671] pursue the possible settlement of the litigation through mediation and, if the mediation was unsuccessful, to use in later stages of the litigation. The IPC allowed the Requester's appeal and directed the LCBO to release the disputed records in issue to the Requester (subject to a number of deletions based on other sections of FIPPA, which are not the subject of these judicial review applications).

[18] The IPC ruled that a mediation of ongoing litigation is not part of the litigation process and that materials prepared by or for Crown counsel for use in mediation are not prepared for the dominant purpose of litigation and are not subject to the s. 19 exemption. The IPC also ruled that s. 19 does not encompass settlement privilege. With respect to the argument that the disputed records in issue were also prepared for use in later stages of the litigation, if necessary, the IPC ruled that "the only evidence I have before me to substantiate that intention is the LCBO's bare assertion to that effect".

[19] The LCBO requested the IPC to reconsider its decision. In light of the IPC's comments about the lack of evidence concerning the intended use of the disputed records in issue, the LCBO supplied an affidavit from its senior vice-president and general counsel, confirming that the disputed records were prepared both for use in the mediation and in later stages of the litigation. The Adjudicator reviewed the affidavit, rejected it on the basis that it was fresh evidence and ruled that he was functus officio and not in a position to reconsider his order in respect of most of the grounds raised. Nevertheless, he then proceeded to comment extensively on the affidavit and the LCBO's submissions in a lengthy reconsideration order. The IPC refused the LCBO's reconsideration request in relation to the disputed records in issue, by Reconsideration Order PO-2538-R.

[20] By Notice of Application for Judicial Review dated February 5, 2007, the LCBO applied for judicial review of the IPC's orders on the basis that the IPC had erred in law in interpreting s. 19 and common-law settlement privilege, in ruling that a mediation of outstanding litigation is not part of the litigation process, in holding that materials prepared for use in such a mediation are not prepared for use in litigation and in rejecting the LCBO's affidavit materials.

Order PO-2405

[21] Order PO-2405 was issued on June 30, 2005, over the signature of Senior Adjudicator John Higgins (the "Adjudicator"). In analyzing s. 19 of the Act, as it then was, the Adjudicator began as follows: [page672]

Section 19 of the Act reads:

> A head may refuse to disclose a record that is subject to solicitor-client privilege or that was prepared by or for Crown counsel for use in giving legal advice or in contemplation of or for use in litigation.

Section 19 contains two branches. Branch 1 includes two common law privileges:

-- solicitor-client communication privilege; and

-- litigation privilege

Branch 2 is based on the closing words of this section, which refer to 'a record . . . that was prepared by or for Crown counsel for use in giving legal advice or in contemplation of or for use in litigation'. It contains two analogous statutory privileges that apply in the context of Crown counsel giving legal advice or conducting litigation.

[22] After reviewing the submissions of the LCBO and Magnotta, the Adjudicator found the submissions raised the following questions:

(1) Does the modern principle of statutory interpretation favour the inclusion of settlement privilege within the scope of s. 19?
(2) Does common-law litigation privilege under Branch 1 encompass settlement privilege?
(3) If common-law litigation privilege under Branch 1 does not encompass settlement privilege, are the records nevertheless subject to common-law litigation privilege under Branch 1?
(4) Do the words, "prepared by or for Crown counsel in contemplation of or for use in litigation" in Branch 2 encompass records prepared for use in the mediation or settlement of litigation? If so, were the records prepared by or for Crown counsel for that purpose?
(5) In the event that the settlement negotiations had failed, were the records prepared "by or for Crown counsel for use in litigation" within the meaning of Branch 2?
(6) Are the records subject to Branch 1 solicitor-client communication privilege?
(7) Were the records "prepared by or for Crown counsel for use in giving legal advice" within the meaning of Branch 2?

[23] The Adjudicator answered all of the seven questions with "No". [page673]

Reconsideration Order PO-2538-R

[24] The list of records still in dispute between the LCBO and Magnotta, on the one hand, and IPC, on the other, are:

Record Number	Description	Notes
1	Chronology of [affected party] and LCBO Events	Reconsideration request relates to portions ordered disclosed
6	[Affected party] and LCBO and LLBO and [affected party] et al. and LCBO - Mediation Brief of the Respondent/Defendant LCBO	*
7	[Affected party] and LCBO -- Mediation Brief of th LCBO (Defamation)	*
8	[Affected party] and LCBO and LLBO -- Affidavits for Mediation	*
16	Minutes of Settlement	*
54-58	Documents relating to implementation of mediated settlement (comprising various documents totaling 241 pages)	Reconsideration request relates to all pages ordered disclosed in full or in part, except pages 1-2. 5-9, 12-15, 54-60,127-130, 132-134, 171- 176, 196-207, 209 - 210 and 211 of Records 54-58

[25] After reviewing s. 18 of the IPC's Code of Procedure (the "Code"), the Adjudicator acknowledged an accidental error within the meaning of s. 18 and corrected it. Apart from that, he found he was functus officio and not in a position to reconsider the order. Nevertheless, he went on to review the arguments of the LCBO and Magnotta explaining his action by noting that they had gone to considerable effort to explain their basis for disagreeing with his decision. This discussion went on for 19 pages of analysis involving solicitor-client privilege, litigation privilege and settlement privilege, all in their relation to s. 19 of FIPPA. He concluded that Order P0-2405 should stand, subject to the minor correction.

Standard of Review

[26] All parties submit that the standard of review of an adjudicator's decision under s. 19 of FIPPA is correctness. We agree. [page674]

Analysis

(a) Does common law settlement privilege exempt the disputed records from disclosure?

[27] A discussion of settlement privilege requires a comparison of three privileges -- solicitor-client privilege, litigation privilege and settlement privilege.

Solicitor-Client Privilege

[28] Solicitor-client privilege protects the direct communications -- both oral and documentary -- prepared by the lawyer or client and flowing between them, in connection with the provision of legal advice. The communication must be intended to be made in confidence, in the course of seeking or providing legal advice, and must be advice based upon the professional's expertise in law.

[29] Solicitor-client privilege is no longer considered to be a rule of evidence, but a substantive rule that has evolved into a fundamental civil and constitutional right. Solicitor-client privilege is not absolute, but it is a privilege that is as close to absolute as possible to ensure public confidence and retain relevance. It will only yield in certain clearly defined circumstances and does not involve a balancing of interests on a case-by-case basis.

[30] Solicitor-client privilege applies to government and in-house lawyers. The determination of whether there is a solicitor-client relationship in any given circumstance, and thus whether the communications are subject to solicitor-client privilege, depends on the nature of the relationship, the subject-matter of the advice and the circumstances in which the advice was sought and rendered (excerpted from Robert W. Hubbard, Susan Magotiaux and Suzanne M. Duncan, The Law of Privilege in Canada, looseleaf (Aurora, Ont.: Canada Law Book Inc., 2006) at 11-3 ("Hubbard")).

Litigation Privilege

[31] Litigation privilege, also called work product privilege, applies to communications between a lawyer and third parties or a client and third parties, or to communications generated by the lawyer or client for the dominant purpose of litigation when litigation is contemplated, anticipated or ongoing. Generally, it is information that counsel or persons under counsel's direction have prepared, gathered or annotated. [page675]

[32] Litigation privilege is not a class or absolute privilege and, unlike solicitor-client privilege, has not evolved into a substantive rule of law.

[33] Information sought to be protected by litigation privilege must have been created for the dominant purpose of use in actual, anticipated or contemplated litigation.

[34] Litigation privilege can protect documents that set out the lawyer's mental impressions, strategies, legal theories or draft questions. These documents do not have to be from or sent to the client. This is the first broad category of documents that are most often protected by litigation privilege as part of the lawyer's brief. The second broad class of documents includes communications by the lawyer, client or third party, created for the purpose of litigation, e.g., witness statements, expert opinions and other documents from third parties.

[35] Litigation privilege allows a lawyer a "zone of privacy" to prepare draft questions and

arguments, strategy or legal theories.

[36] The elements required in order to claim work product or litigation privilege over documents or communications are as follows:

(a) the documents or communications must be prepared, gathered or annotated by counsel or persons under counsel's direction;
(b) the preparation must be done in a realistic anticipation of litigation;
(c) if there is more than one purpose or use for the document, facts must reveal that the dominant purpose was for the anticipated litigation;
(d) there must be no requirement under legal rules governing the proceeding to disclose the documents or facts; and,
(e) there has been no prior waiver of documents or facts by disclosure to the opposing party.

(excerpted from Hubbard, above, at 12-2 -- 2.1-3.)

Settlement Privilege

The public policy rationale

[37] When parties share information in furtherance of settling disputes, that information is generally subject to privilege from disclosure. The documents containing the information are often, but not always, marked as being "without prejudice". [page676]

[38] In Ontario, as early as 1968, Fraser J. analyzed the public policy considerations which supported non-disclosure of information shared during the course of settlement discussions and negotiations. He concluded:

> In my opinion the privilege as so often stated, is intended to encourage amicable settlements and to protect parties to negotiations for that purpose. It is in the public interest that it not be given a restrictive application.

(I. Waxman & Sons Ltd. v. Texaco Canada Ltd., [1968] 1 O.R. 642, [1968] O.J. No. 1068 (H.C.J.), at p. 656 O.R.)

[39] The Ontario Court of Appeal confirmed Fraser J.'s judgment:

> We find ourselves in agreement with the conclusions reached by Fraser J., and also with his analysis, in the main, of the very numerous decisions referred to in his reasons for judgment . . . .

(I. Waxman & Sons Ltd v. Texaco Canada Ltd., [1968] 2 O.R. 452, [1968] O.J. No. 1174 (C.A.), at p. 453 O.R.)

[40] In 1988, the House of Lords concluded:

> In my view, this advantage does not outweigh the damage that would be done to the conduct of settlement negotiations if solicitors thought that what was said and written between them would become common currency available to all other parties to the litigation. In my view the general public policy that applies to protect genuine negotiations from being admissible in evidence should also be extended to protect those negotiations from being discoverable to third parties.

(Rush & Tompkins Ltd. v. Greater London Council, [1988] 3 All E.R. 737, [1989] 1 A.C. 1280 (H.L.), at p. 744 All E.R. ("Rush")).

[41] In British Columbia, the Court of Appeal endorsed the public policy basis for nondisclosure of settlement discussions. McEachern C.J.B.C. said:

> . . . I find myself in agreement with the House of Lords that the public interest in the settlement of disputes generally requires "without prejudice" documents or communications created for, or communicated in the course of, settlement negotiations to be privileged. I would classify this as a "blanket", prima facie common law, or "class" privilege because it arises from settlement negotiations and protects the class of communications exchanged in the course of that worthwhile endeavour.

(Middelkamp v. Fraser Valley Real Estate Board, [1992] B.C.J. No. 1947, 96 D.L.R. (4th) 227 (C.A.), at pp. 232-33 D.L.R. ("Middelkamp")).

[42] Chief Justice McEachern went on to say [(Middelkamp, at p. 233 D.L.R.)]:

> In my judgment this privilege protects documents and communications created for such purposes both from production to other parties to the negotiations and to strangers, and extends as well to admissibility, and whether or not a settlement is reached. This is because, as I have said, a party communicating a proposal related to settlement, or responding to one, usually [page677] has no control over what the other side may do with such documents. Without such protection, the public interest in encouraging settlements will not be served.

[43] Also in Middelkamp, Locke J.A. agreed, although he concluded the issue had to be determined on a "case-by-case" analysis rather than the class privilege proposed by Chief Justice McEachern. At pp. 250-51 D.L.R., he stated:

> With all respect I cannot in law see one reason why this province, alone in the Commonwealth, should not recognize the overriding importance of this protection from the eyes of a third party. To refuse is to inhibit and penalize one who wishes to settle. It

> is easy to envisage a building owner loath to compromise the minor claim of a small sub-contractor because of concern an admission of fact would be held against him in another major subcontractors proceeding.
>
> All the cases emphasize that no bars should be placed in the way of one who wishes to compromise, and to allow the production is by definition to inhibit. Such barriers to settlement should only be permitted if the other competing interest absolutely demands it.

[44] In 1992, the Supreme Court of Canada also stressed the public policy aspect of settlement negotiations in Kelvin Energy Ltd. v. Lee, [1992] 3 S.C.R. 235, [1992] S.C.J. No. 88, 97 D.L.R. (4th) 616, at p. 259 S.C.R. ("Kelvin"). The court quoted with approval the following statement from Sparling v. Southam Inc. (1988), 66 O.R. (2d) 225, [1988] O.J. No. 1745 (H.C.J.), at p. 230 O.R. ("Sparling"):

> . . . the Courts consistently favour the settlement of lawsuits in general. To put it another way, there is an overriding public interest in favour of settlement. This policy promotes the interest of litigants generally by saving them the expense of trial of disputed issues, and it reduces the strain upon an already overburdened provincial Court system.

[45] There is strong support for a public-policy based class privilege for settlement privilege. However, that support comes from cases where the court analyzes each claim in the context of its particular facts.

[46] The case-by-case analysis is preferable. It is particularly important in the following instances:

> (a) where discussions have led to a settlement, the litigation has resolved, but an argument arises over the terms of the settlement;
> (b) where the interests of third parties in other litigation might be affected; and
> (c) where there is a dispute over whether litigation was "in contemplation". [page678]

I conclude that any analysis undertaken to establish common-law settlement privilege must be done on a case-by-case analysis.

[47] I point out in the matter before us, there is no argument over the terms of the settlement. There is no evidence of interests of third parties in other litigation which might be affected by the settlement. There is no dispute over whether litigation was "in contemplation". Litigation had begun with a vengeance.

[48] Nevertheless, a case-by-case analysis must be undertaken, given that the development of settlement privilege continues as is so often the case with the common law. At its current stage, it is not yet a class or absolute privilege, nor has it evolved into a substantive rule of law.

The Difference between Solicitor-Client Privilege and Litigation Privilege

[49] Solicitor-client privilege is a class privilege which never ends, unless waived or unless the communication is in furtherance of[page680] a crime. Litigation privilege ends with the litigation. As stated by Fish J. in Blank v. Canada (Minister of Justice), [2006] 2 S.C.R. 319, [2006] S.C.J. No. 39, at para. 37 ("Blank"):

> Thus, the principle "once privileged, always privileged", so vital to the solicitor-client privilege, is foreign to the litigation privilege. The litigation privilege, unlike the solicitor-client privilege, is neither absolute in scope nor permanent in duration.

[50] Solicitor-client privilege requires a communication between a solicitor and a client. Litigation privilege is available to parties whether represented by a solicitor or not [(Blank, at para. 32)]:

> Unlike the solicitor-client privilege, the litigation privilege arises and operates even in the absence of a solicitor-client relationship, and it applies indiscriminately to all litigants, whether or not they are represented by counsel: see Alberta (Treasury Branches) v. Ghermezian (1999), 242 A.R. 326, 1999 ABQB 407. A self-represented litigant is no less in need of, and therefore entitled to, a "zone" or "chamber" of privacy. Another important distinction leads to the same conclusion. Confidentiality, the sine qua non of the solicitor-client privilege, is not an essential component of the litigation privilege. In preparing for trial, lawyers as a matter of course obtain information from third parties who have no need nor any expectation of confidentiality; yet the litigation privilege attaches nonetheless.

[Emphasis in original]

The Difference between Solicitor-Client Privilege and Settlement Privilege

[51] Solicitor-client privilege is a class privilege which never ends unless waived or unless the communication is in furtherance of [page679] a crime. Settlement privilege is not a class privilege. Its existence must be established on a case-by-case analysis first applying the "Wigmore" test, as described in Slavutych v. Baker, [1976] 1 S.C.R. 254, [1975] S.C.J. No. 29, at p. 260 S.C.R.:

> (1) The communications must originate in a confidence that they will not be disclosed.
> (2) The element of confidentiality must be essential to the maintenance of the

relationship in which the communications arose.

(3) The relationship must be one which, in the opinion of the community, ought to be "sedulously fostered".

(4) The injury caused to the relationship by disclosure of the communications must be greater than the benefit gained for the correct disposal of the litigation.

[52] The Supreme Court of Canada re-affirmed the approach in Slavutych, making it clear that privilege is to be determined on a case-by-case basis (see M. (A.) v. Ryan, [1997] 1 S.C.R. 157, [1997] S.C.J. No. 13, at para. 20; see, also, Rudd v. Trossacs Investments Inc. (2006), 79 O.R. (3d) 687, [2006] O.J. No. 922 (Div. Ct.), at para. 26 ("Rudd")).

The Difference between Litigation Privilege and Settlement Privilege

[53] Litigation privilege ends with the litigation. Settlement privilege continues past termination of the litigation, absent those circumstances noted in para. 45, above. Litigation privilege meets the need for a protected zone of privacy to help in the investigation and preparation of a case for trial -- the adversary process. Settlement privilege is also a process in the adversary system -- one which permits the parties to focus on avoiding a trial, without jeopardizing the ability to return to a true adversarial position. Obviously, certain communications will be common to both should the attempts at settlement fail. While it is understandable that some authorities refer to settlement privilege as being part of litigation privilege, such is not the case. While both privileges started as rules of evidence, settlement privilege, in particular, has advanced to the point where it is now regarded as key in the promotion of settlements.

Application of the "Wigmore" Test to the Facts of this Case

[54] The communications between the LCBO and Magnotta originated in confidence. They were the subject of a strong [page680] confidentiality agreement. The first Wigmore condition has been satisfied.

[55] In order for the parties to arrive at a settlement, they must be assured of confidentiality so that discussions can be free and frank. Confidentiality is essential to meaningful settlement discussions. The second Wigmore condition has been satisfied.

[56] Starting with the House of Lords in Rush, above, and running through to the Supreme Court of Canada in Kelvin, above, courts in Canada have consistently favoured the settlement of lawsuits. In Kelvin, at p. 259 S.C.R., p. 634 D.L.R., the Supreme Court cited with approval the statement of Callaghan A.C.J.H.C. in Sparling, above, at p. 230 O.R.:

> In approaching this matter, I believe it should be observed at the outset that the Courts consistently favour the settlement of lawsuits in general. To put it another way, there is an overriding public interest in favour of settlement. This policy promotes the interests of litigants generally by saving them the expense of trial of disputed issues,

> and it reduces the strain upon an already overburdened provincial court system.

(Sparling v. Southam Inc., supra, at p. 28)

(Emphasis added)

(See, also, Bard v. Longevity Acrylics Inc., [2002] O.J. No. 1373, 18 C.C.E.L. (3d) 256 (S.C.J.), at para. 29 ("Bard"); Rudd, above.)

> [57] In Rudd, the Divisional Court found, at para. 33:
>
> > The third Wigmore condition requires a determination whether the relationship in which the communication is given is one which should be "sedulously fostered". The Rules of Civil Procedure require mandatory mediation of many civil disputes in order to assist the parties in arriving at a settlement and thus reduce the costs of litigation. There is clearly a significant public interest in protecting the confidentiality of discussions at mediation in order to make the process as effective as possible.

[58] I conclude the law is well-settled that there is a significant public interest in protecting the confidentiality of settlement discussions in order to make the process as effective as possible. Confidentiality of settlement discussions should be "sedulously fostered". The third Wigmore condition is satisfied.

[59] The fourth stage of the Wigmore test requires a balancing of the public interest in disclosure of government records called for by FIPPA against the public interest in preserving the confidentiality of communications during settlement negotiations. It is to this balancing I now turn.

Transparency in Government Action vs. Settlement Privilege

[60] The Requester in this matter is anonymous. We have no knowledge of why the Requester seeks the information in the disputed records. If there is a public policy reason that would [page681] support and explain why the Requester is entitled to obtain the otherwise privileged information vis-à-vis the Requester, we do not know what it is. Absent such an explanation, the competing public policy interests in this matter are simply those created by FIPPA versus the interest in promoting settlements of disputes through confidential settlement negotiations.

[61] The IPC's position on settlement privilege can be shortly put. The Commissioner submits that since the Public Government for Private People: The Report of the Commission on Freedom of Information and Individual Privacy 1980 (the "Williams Commission Report") did not specifically mention settlement privilege and since settlement privilege is not specifically referred to in s. 19 of FIPPA, settlement privilege is of no consequence in this matter. At p. 17 of Order PO-2538-R:

> In my view, the issue of negotiations was canvassed by the Williams Commission and

> addressed in sections 17(1)(a) and 18(1)(e), and if the Legislature had intended to include settlement privilege in branch 1 of section 19, it would have said so.

[62] What may have been true in 1980 is not necessarily true in 2009. Almost 30 years have passed. From Rush to Kelvin, above, the common law has expanded settlement privilege from a rule of evidence to an overriding public interest in favour of settlement.

[63] In General Accident Assurance Co. v. Chrusz (1999), 45 O.R. (3d) 321, [1999] O.J. No. 3291 (C.A.), the court dealt with litigation privilege. Carthy J.A., writing for the majority, at p. 332 O.R., found that litigation privilege had been narrowed in scope by succeeding amendments to the Rules:

> In a very real sense, litigation privilege is being defined by the rules as they are amended from time to time. Judicial decisions should be consonant with those changes and should be driven more by the modern realities of the conduct of litigation and perceptions of discoverability than by historic precedents born in a very different context.

[64] To paraphrase, in a very real sense, settlement privilege is being defined by the Rules as they are amended from time to time. Settlement privilege has expanded in scope through changes to the Rules. These changes provide for various settlement mechanisms, such as pretrial conferences, settlement conferences, case management and mediation, both voluntary and mandatory.

[65] What follows from the IPC's view of the law regarding settlement negotiations? First, the details of negotiations and settlement of any dispute between a government institution and a third party will be available to the world at large, following a request. Apparently, a Requester need but ask anonymously and the IPC will undertake the heavy lifting, as in this case. There is [page682] a delicious irony in this matter whereby the IPC, in the name of transparency, labours for an anonymous Requester. Second, and perhaps more important, no third party would willingly entertain settlement discussions with a government institution, particularly where admissions are made and concessions offered that would enure to the detriment of the third party, if publicly disclosed. As this court said in Rudd, above, at para. 38:

> Parties may also reveal information to a mediator which they wish to keep confidential even after a settlement is reached, perhaps because the information is private, or because it may injure a relationship with others.

[66] Government institutions are not strangers to litigation. They are entitled to have disclosure of their settlements considered on a case-by-case analysis of their common-law entitlement to settlement privilege.

Section 1 of FIPPA Viewed in the Light of Statutory Interpretation

[67] The purposes of FIPPA are set out in s. 1:

> 1. The purposes of this Act are,
>
> (a) to provide a right of access to information under the control of institutions in accordance with the principles that,
>
> (i) information should be available to the public,
> (ii) necessary exemptions from the right of access should be limited and specific, and
> (iii) decisions on the disclosure of government information should be reviewed independently of government . . .

[68] As noted earlier, the IPC views the meaning of "exemption" in s. 1(a)(ii) as those exceptions specifically set out in FIPPA. Our Court of Appeal has found with respect to FIPPA "[t]he broad intention of the Act is to offer transparency to government functioning with exceptions where the interests of public knowledge are overbalanced by other concerns": Ontario (Attorney General) v. Ontario (Information and Privacy Commission, Inquiry Officer) (2002), 62 O.R. (3d) 167, [2002] O.J. No. 4596 (C.A.), at para. 14 ("Big Canoe (C.A.)").

[69] This view of our Court of Appeal is consistent with the modern approach to statutory interpretation, which requires that all relevant and admissible indicators of legislative meaning must be considered.

[70] In 2747-3174 Quebec Inc. v. Quebec (Regis des permis d'alcool), [1996] 3 S.C.R. 919, [1996] S.C.J. No. 112, at para. 164, L'Heureux-Dubé J. spoke in favour of what she termed the "modern approach" to the interpretation of statutes, citing a [page683] passage from Ruth Sullivan, Driedger on the Construction of Statutes, 3rd ed. (Toronto: Butterworths, 1994) at p. 131. The same passage from this text of Professor Sullivan was cited with approval in Big Canoe (C.A.) and in Ontario (Children's Lawyer) v. Ontario (Information and Privacy Commissioner) (2003), 66 O.R. (3d) 692, [2003] O.J. No. 3522 (Div. Ct.), affd (2005), 75 O.R. (3d) 309, [2005] O.J. No. 1426 (C.A.) ("Children's Lawyer").

[71] In Children's Lawyer, the Divisional Court noted the Court of Appeal's decision in Big Canoe, at paras. 75-76:

> Under the modern approach to statutory interpretation, the language of the statute must be addressed in its context. In referring to the context, the Court of Appeal said (p. 173 O.R.):

Finally, the "modern" interpretation method was reformulated in Canada by Professor R. Sullivan: Driedger on the Construction of Statutes (3d ed. 1994) at p. 131:

> There is only one rule in modern interpretation, namely, courts are obliged to determine the meaning of legislation in its total context, having regard to the purpose of the legislation, the consequences of proposed interpretations, the presumptions and special rules of interpretation, as well as admissible external aids. In other words, the courts must consider and take into account all relevant and admissible indicators of legislative meaning. After taking these into account, the court must then adopt an interpretation that is appropriate. An appropriate interpretation is one that can be justified in terms of (a) its plausibility, that is, its compliance with the legislative text; (b) its efficacy, that is, its promotion of the legislative purpose; and (c) its acceptability, that is, the outcome is reasonable and just.
>
> (Emphasis added)

Applying that test supports the plain meaning test. The broad intention of the Act is to offer transparency to government functioning with exceptions where the interests of public knowledge are overbalanced by other concerns. In the present case, the requester seeks assistance in a civil proceeding following a criminal prosecution concerning the same incident. The purpose and function of the Act is not impinged upon by this request. However, to open prosecution files to all requests which are not blocked by other exemptions could potentially enable criminals to educate themselves on police and prosecution tactics by simply requesting old files. Among other concerns that come to mind are that witnesses might be less willing to co-operate or the police might be less frank with prosecutors. It should be kept in mind that this is the Freedom of Information Act and does not in any way diminish the power of subpoena to obtain documents, such as those in issue here, where appropriate and releva nt in litigation. I can therefore see no countervailing purpose or justification for an interpretation that would render the Crown brief available upon simple request.

This passage is very important. It illustrates the concerns to be addressed. They include balancing the objective of transparency of government functioning and the interests of public knowledge against other concerns; and considering whether the

> purpose and function of FIPPA are impinged upon [page684] by one interpretation or the other. Having performed this analysis, the court found many disadvantages and no countervailing purpose or justification for an interpretation that would render the Crown brief in a criminal case available to the public upon simple request. In our view, this is the sort of analysis which we must perform.

(Emphasis added)

[72] In considering the purposes of FIPPA, as set out in s. 1(a), the language of the statute must be addressed in its total context, having regard to the purpose of the legislation, the consequences of proposed interpretations, the presumptions and special rules of interpretation, as well as admissible external aids. After considering all these indicators of legislative meaning, the court must adopt an interpretation of s. 1(a) that is appropriate. An appropriate interpretation is one that can be justified in terms of (a) its plausibility, that is, its compliance with the legislative text; (b) its efficacy, that is, its promotion of the legislative purpose; and (c) its acceptability, that is, the outcome is reasonable and just (see Ruth Sullivan, Sullivan on the Construction of Statutes, 5th ed. (Markham, Ont.: LexisNexis, 2008) at pp. 1, 3-4 ("Sullivan, Sullivan on the Construction of Statutes")).

A statutory interpretation of s. 1(a) of FIPPA

[73] I conclude that the public policy interest in encouraging settlement as embodied in the common-law concept of settlement privilege trumps the public policy interest in transparency of government action, in the circumstances of this case. I turn, then, to analyze this conclusion within the context of the indicators of legislative meaning proposed by Professor Sullivan.

[74] This interpretation is plausible because it complies with the legislated text (s. 1(a) of FIPPA) which provides for "necessary exemptions" that are "specific and limited". The exemption is "necessary" to maintain confidentiality of negotiated settlements. The exemption is "specific" and "limited" in that it is specific to and limited by the circumstances of this case. A case-by-case analysis ensures settlement privilege will always be specific to and be limited by particular fact situations.

[75] This interpretation is efficacious because it promotes the legislative purpose of creating exemptions where necessary, provided the exemptions are limited and specific.

[76] This interpretation is acceptable because it leads to a conclusion that is both reasonable and just. As noted earlier in these reasons, no party would willingly entertain settlement discussions with a government institution if it knew its confidential settlement discussions would be made public. This is particularly so where admissions would be made and concessions [page685] offered that would be detrimental to that party. If required to discuss settlement by the Rules, those discussions would not, I suggest, be meaningful.

[77] The disputed records must remain confidential according to the terms of the agreement and

minutes of settlement and may not be released to the Requester.

(b) Are records prepared by or for Crown counsel in respect of the mediation and settlement of ongoing litigation exempt from disclosure under s. 19 of FIPPA?

[78] It will be recalled that Branch 2 of s. 19 of FIPPA exempts from disclosure records that were prepared by or for Crown counsel for use in giving legal advice or in contemplation of or for use in litigation.

[79] The IPC found the disputed records were not exempt because they were not prepared in contemplation of or for use in litigation. With respect, the IPC is wrong in law in its analysis of Branch 2 of s. 19 of FIPPA. The Rules have incorporated mediation into the litigation process by requiring parties in case-managed actions (and in all actions commenced in Toronto after January 4, 1999) to participate in a mandatory mediation.

[80] The Ontario Court of Appeal has recognized that mediation is an integral part of the litigation process, particularly in actions which are subject to the mandatory mediation rules (as were two of the matters mediated in the present case). In Rogacki v. Belz (2003), 67 O.R. (3d) 330, [2003] O.J. No. 3809 (C.A.), Abella J.A. (in concurring reasons) described the role of mediation as part of the litigation process, at paras. 44, 47:

> It is true that the purpose of mandatory mediation is to settle disputes outside of the court's process, and, as in discovery, it is not conducted by a judge. But it is also true that aspects of mandatory mediation directly engage the court's process. First and foremost, the fact that mediation is mandated by the commencement of a proceeding under the rules, directly implicates the mediation in the court's process . . . .
>
> . . . . .
>
> Mandatory mediation is a compulsory part of the court's process for resolving disputes in civil litigation. Wilful breaches of the confidentiality it relies on for its legitimacy, in my view, represent conduct that can create a serious risk to the full and frank disclosures the mandatory mediation process requires. It can significantly prejudice the administration of justice and, in particular, the laudable goal reflected in Rule 24.1 of attempting to resolve disputes effectively and fairly without the expense of trial.

(See, also, Warren K. Winkler, C.J.O., "Access to Justice, Mediation: Panacea or Pariah?" (2007), 16 Canadian Arbitration and Mediation Journal 5.) [page686]

[81] Various alternative dispute resolution ("ADR") methods (such as, for example, pre-trial conferences) have been incorporated into the litigation process for many years. There is no valid

reason for distinguishing among different forms of ADR based on where they occur in ongoing court proceedings. It makes no sense to treat some forms of ADR as part of the litigation process and others as not. All forms of ADR, including both mandatory and consensual mediation, are part of the litigation process and are equally deserving of confidentiality and the protection of the Branch 2 exemption under s. 19 of FIPPA. As explained by Power J., in Bard, above, at para. 31:

> In recent years, there has been a significant emphasis on the desirability of encouraging settlement of disputes whether in the courts or before administrative and other tribunals. This has resulted in the use of various forms of alternative dispute resolutions and, as well, changes to our rules of practice which encourage case management, mediation, and court supervised settlement conferences (or pre-trial conferences). In my opinion, the logic for treating settlement discussions as privileged is, therefore, more pressing than ever. It follows, therefore, that this privilege should not be limited except where there are strong and compelling reasons for doing so. I include in the term "settlement discussions", pre-trials and settlement conferences as well as mediations. As aforesaid, I see no valid reason for distinguishing between pre-trials and settlement conferences. The privilege applies even in the absence of rule 50.03.

[82] The LCBO asserted before the IPC that the mediation materials were intended for use in litigation should the mediation fail. The IPC refused to consider this because of a finding that there was no evidence to this effect. It is unnecessary for me to resolve this dispute, other than to say it is obvious that some materials used in any mediation will subsequently be used by counsel to prepare for trial and at the trial itself.

A statutory interpretation of the Branch 2 exemption

[83] Earlier in these reasons, an analysis of s. 1 of FIPPA used the so-called "modern approach" to statutory interpretation (see above, at paras. 67-77). To repeat, in interpreting Branch 2 of s. 19 of FIPPA, all relevant and admissible indicators of legislative meaning must be considered. The language of the statute must be addressed in its total context, having regard to the purpose of the legislation, the consequences of proposed interpretations, the presumptions and special rules of interpretation, as well as admissible external aids (see Sullivan, Sullivan on the Construction of Statutes, above).

[84] Following consideration of these indicators of legislative intention, the court must choose an interpretation of the Branch 2 exemption that is "appropriate". To repeat the earlier analysis, [page687] an appropriate interpretation is one that can be justified in terms of its (a) plausibility; (b) efficacy; and (c) acceptability, that is, the outcome is reasonable and just (see Sullivan, Sullivan on the Construction of Statutes, at pp. 1, 3-4). In Ontario (Attorney General) v. Big Canoe, [2001] O.J. No. 4876, 208 D.L.R. (4th) 327 (Div. Ct.) ("Big Canoe (Div. Ct.)"), this court held that the language of the Branch 2 exemption is "clear and unambiguous". The wording of Branch 2 imposes no

temporal limits on the protection provided nor limits it to particular types of litigation documents, nor specifies specific steps in the litigation. Nothing in the legislative text suggests that the term "litigation" should be given a different meaning than that adopted by the courts and reflected in the Rules. Such an interpretation complies with the legislative text.

[85] Such an interpretation of Branch 2 also promotes the purpose of FIPPA to provide transparency of government functioning "with exceptions where the interests of public knowledge are overbalanced by other concerns" (see Big Canoe (C.A.), above). To interpret Branch 2 in this manner recognizes that in the case of records prepared by or for Crown counsel for use in any aspect of litigation, the interests of the public in transparency are trumped by a more compelling public interest in encouraging settlement of litigation.

[86] The proposed interpretation of Branch 2 is acceptable because it arrives at an outcome that is reasonable and just. The IPC's narrow interpretation of Branch 2 would result in an unreasonable and unjust outcome, since it would deprive government institutions of the privilege attached to settlement discussions otherwise available to all other litigants. Moreover, the IPC's interpretation would discourage third parties from engaging in meaningful settlement negotiations with government institutions. In Children's Lawyer, above, at para. 94, this court said:

> We should not adopt an interpretation of legislation that places a public servant in such a position of conflict of interest if there is a reasonable alternative. It would be absurd to suppose that the Legislature intended such a result. The respondent put it succinctly in para. 63 of its factum.
>
> > To read Branch 2 so as to exclude the child from access would lead to absurd consequences. The presumption that legislation is not intended to produce absurd consequences is a fundamental rule of interpretation. Moreover, "[a] bsurdity is not limited to logical contradictions and internal incoherence; it includes violations of justice, reasonableness, common sense, and other public standards . . . " The primary 'absurd' results of reading Branch 2 in such a manner would be to put the Children's Lawyer in violation of its fundamental duties to the client/ requester.
> >
> > R. Sullivan, Driedger on the Construction of Statutes (Markham: Butterworths, 1994), at 85-86. [page688]

[87] To summarize, the following outcomes contribute to my conclusion that the IPC interpretation of Branch 2 of s. 19 would lead to an absurd result:

(a) where given a choice, private parties will avoid settlement discussions and mediation with government institutions;

(b) when faced with mandatory mediation, private parties will be inhibited from engaging in "full and frank" disclosure upon which the requirement for a successful resolution depends;
(c) the chances of a successful mediation will be remote;
(d) the legislative intentions in the Rules regarding mandatory mediation will be frustrated;
(e) confidentiality clauses negotiated between private parties and government institutions will be meaningless; and
(f) the costs of litigation between private parties and government institutions will, by necessity, be greater than otherwise.

[88] For the foregoing reasons, I conclude that the disputed records are exempted from production by Branch 2 of s. 19 of FIPPA.

The "Asymmetrical Protection" Submission

[89] The IPC refused to apply the Branch 2 exemption to protect the LCBO's mediation materials because (in the IPC's view) it would result in material prepared by or for Crown counsel having more extensive protection than the mediation materials of private parties. The IPC described this "asymmetrical protection" issue as follows:

> [I]t would only protect materials prepared by or for Crown counsel. This would mean that only the government party's settlement-oriented records would be protected, not those of the private litigant engaged in settlement discussions with the Crown.

[90] I reject this interpretation for three reasons. First, the mediation and settlement materials of private parties are always subject to settlement privilege where the settlement privilege is granted pursuant to a case-by-case analysis as discussed above. It is only the introduction of a government institution into the equation that attracts the application of the second Branch of s. 19 to the settlement. The IPC appears to assume that if Branch 2 of s. 19 protects the Crown, nevertheless, a Requester would have access to the private party's documents used in the mediation and settlement process. Such [page689] is not the case. It would be open to the private party to establish settlement privilege on a case-by-case analysis.

[91] Second, in the IPC's interpretation of the Branch 2 exemption any "asymmetry" created by the LCBO's interpretation of Branch 2 pales into insignificance in comparison with the asymmetry created by the IPC's interpretation of Branch 2. It denies to all government institutions the privilege available to private litigants otherwise found to be applicable to mediation and settlement materials. All private litigants can engage in settlement discussions confident that settlement materials will remain confidential. The IPC would have it that the Crown can not. That is true asymmetry.

[92] Third, the IPC's interpretation is directly contrary to the interpretation given to the Branch 2 exemption by this court in Big Canoe (Div. Ct.), above, at para. 32, where it was held that:

> A head may refuse to disclose a record that was prepared by or for Crown counsel for use in giving legal advice or in contemplation of, or for use in, litigation. The language is clear and unambiguous. . . . Thus, if it was not the intention of Branch 2 of s. 19 to enable government lawyers to assert a privilege more expansive or durable than that available at common law to solicitor-client relationships (the Inquiry Officer found it was not), it was open to the Legislature to say so.

[93] For the foregoing reasons, I conclude that the disputed records are exempted from production by Branch 2 of s. 19 of FIPPA.

[94] Whether by application of the common-law doctrine of settlement privilege or by the application of Branch 2 of s. 19 of FIPPA, the disputed records are exempt from disclosure.

[95] An order will go setting aside the portions of the IPC's Order P0-2405 (as amended by Reconsideration Order PO-2538-R), which holds that Records 1, 6, 7, 8, 16 and certain pages of Records 54-58, specified in numbered para. 1 of those orders, are not exempt from release.

[96] A further order shall go upholding the LCBO's decision to withhold disclosure of those records.

[97] As agreed upon by the parties, there shall be no order as to costs.

Application granted.

[page690]

Tab 10

Case Name:

Rudd v. Trossacs Investments Inc.

Between
Martin Rudd, Jack Schwartz, Loys Ligate, Gordon Sawa, William Crysdale, Violet Dicecco, Sam Kotzer, Peter Edwards and Ian C. Grayson, plaintiffs (respondents),
and
Trossacs Investments Inc., Fanlon Services Inc., Trossacs Associates, Kaimor Management Ltd., Trossa Holdings Inc., Tangueray Computers Inc., Stacey Mitchell, Morris Kaiser, Shlomo Sharon, David Sugarman, Hattin, Moses, Sugarman & Company and 645262 Ontario Limited, defendants (appellants), and
Ontario Bar Association, intervenor

[2006] O.J. No. 922

79 O.R. (3d) 687

265 D.L.R. (4th) 718

208 O.A.C. 95

27 C.P.C. (6th) 147

146 A.C.W.S. (3d) 224

2006 CarswellBC 1417

Court File No. 544/04

Ontario Superior Court of Justice
Divisional Court - Toronto, Ontario

K.E. Swinton, E.F. Then, and J.D. Carnwath JJ.

Heard: December 8, 2005.
Judgment: March 9, 2006.

(44 paras.)

Administrative law -- Mediation -- The appeal was allowed and the order of the motions judge was set aside -- The motions judge's order permitting the examination of the mediator as a witness to testify about communications at the mediation was set aside -- The judge had erred by focusing solely on without prejudice settlement privilege and failing to conduct an analysis on the Wigmore conditions -- There was an important public interest in maintaining the confidentiality of the mediation process that in all the circumstances of the case outweighed the interest in compelling the evidence of the mediator.

Civil evidence -- Witnesses -- Compellability -- Tribunal members -- The appeal was allowed and the order of the motions judge was set aside -- The motions judge's order permitting the examination of the mediator as a witness to testify about communications at the mediation was set aside -- The judge had erred by focusing solely on without prejudice settlement privilege and failing to conduct an analysis on the Wigmore conditions -- There was an important public interest in maintaining the confidentiality of the mediation process that in all the circumstances of the case outweighed the interest in compelling the evidence of the mediator.

Statutes, Regulations and Rules Cited:

Ontario Rules of Civil Procedure, Rule 24.1

Counsel:

Harvin D. Pitch and Matthew Sokolsky, for the Plaintiffs (Respondents)

Paul Dollak, for the Defendants (Appellants)

Ian D. Kirby, for the Intervenor

The judgment of the Court was delivered by

1 **K.E. SWINTON J.**:-- This appeal raises the important issue whether a mediator who conducted a mediation pursuant to rule 24.1 of the Rules of Civil Procedure can be compelled to give evidence as to events which took place during the course of such mediation.

Background Facts

2 The Appellants (Trossacs Investments Inc., Fanlon Services Inc., Trossacs Associates, Kaimor Management Limited, Trossa Holdings Inc., Morris Kaiser and 645262 Ontario Limited) are

defendants in this action.

3 The Respondents (Martin Rudd, Gordon Sawa, William Crysdale, Violet DiCecco and Peter Edwards) were investors in a limited partnership. They were represented by counsel Garth Low in this action, in which they sued the general partner and various related or associated companies and their principal Morris Kaiser, as well as the investors' accountants.

4 In 2003, Morris Kaiser brought a motion for summary judgment to dismiss all the claims against him personally. The motion was not opposed when brought before Himel J., and on September 23, 2004, she dismissed the action against Mr. Kaiser and ordered the plaintiffs to pay him costs of over $39,000.

5 After receiving correspondence from Mr. Low suggesting that she had made a clerical error in calculating costs, Himel J. invited further submissions. While she considered those submissions, the litigation continued between the other parties.

6 The parties commenced mandatory mediation on January 12, 2004 and continued on January 28, 2004. A mediation agreement was executed prior to the start of the mediation. It contained a confidentiality clause in the following terms:

> 2. Confidentiality
>
> The parties agree that all communications and documents shared, which are not otherwise discoverable, shall be without prejudice and shall be kept confidential as against the outside world, and shall not be used in discovery, cross examination, at trial, in this or any other proceeding, or in any other way.
>
> The mediator's notes and recollections cannot be soepenaed (sic) in this or any other proceeding.

7 Mr. Kaiser was present at the first mediation session. The Appellants claim that he was there in his capacity as an officer, director, or signing officer of the remaining defendants.

8 A settlement was reached on January 28, 2004, a date on which Mr. Kaiser was in attendance by telephone. The terms of the settlement were drafted by the mediator with input from counsel. The terms are set out in Minutes of Settlement that are largely handwritten. However, they are headed by the typed style of cause of the action, cut from another document and attached to the Minutes of Settlement. Mr. Kaiser's name is included, as he is one of the named defendants in the action.

9 The terms of the settlement are handwritten and state:

> The Plaintiffs William Crysdale, Peter Edwards, Martin Rudd & Gordon Sawa (the "Plaintiffs") and the Defendants signing below agree to settle the within action and counterclaim on the following terms:
>
> 1.) Each of the Plaintiffs shall pay to the Defendants the amount of $32,000.00 all inclusive of all claims, interest, costs, GST & disbursements payable to Paul Dollak in trust.
> 2.) The Plaintiffs & the Defendants shall execute mutual releases in a form satisfactory to counsel.
> 3.) The action & counterclaim respecting the Plaintiffs herein shall be dismissed without costs.

This was dated January 28, 2004, and the names of the plaintiffs were written in, and they signed.

10 The names of the following defendants were in typed form, cut from another document by counsel for the defendants, Mr. Dollak, and inserted: Trossacs Investments Inc., Fanlon Services Inc., Trossacs Associates, Kaimor Management Ltd., Trossa Holdings Inc. and 645262 Ontario Limited. Mr. Dollak then signed as counsel on their behalf. Mr. Kaiser's name is not included among the signatories.

11 A "Settlement and Mutual Release" was executed separately by each of Mr. Low's clients, including Ms. DiCecco. For example, Mr. Rudd signed on February 12, 2004, while Mr. Crysdale signed on February 16, 2004. Both signatures were witnessed by Mr. Low. The parties of the second part were the defendants named in the Minutes of Settlement. Mr. Kaiser's name does not appear, although he signed each Settlement and Mutual Release on behalf of the named defendants.

12 An order was obtained from the Superior Court of Justice dismissing the action against these same named defendants on February 19, 2004.

13 On March 5, 2004, Himel J. released her amended costs order from the summary judgment motion. In it, she reduced the costs payable to Mr. Kaiser to just over $21,000.

14 When counsel for Mr. Kaiser sought to enforce the revised costs order, Mr. Low alleged that he had made a mistake and never noticed that Mr. Kaiser had not signed the settlement documents in his personal capacity. Mr. Low then brought a motion seeking an order to compel the mediator to testify about communications at the mediation, for rectification of the Minutes of Settlement and for enforcement of the settlement.

15 The motions judge, Lederman J., gave his decision on July 8, 2004, ordering that the mediator could be examined as a witness on the pending motion. At para. 23 of his reasons, he stated:

> Accordingly, an order will go permitting the examination of the mediator as a

> witness on the pending motion with the questions being limited to his knowledge and understanding, if any, as to whether Kaiser was or was not a party to the settlement agreement that was arrived at in the mediation.

16 The motions judge discussed the common law principle that settlement discussions are privileged. He also made reference to the parties' confidentiality agreement. He then went on to say that once a settlement has been reached and its interpretation is in question, it may be necessary to disclose mediation discussions to ensure substantive justice. However, he stated that privilege and confidentiality should not be lightly disturbed and continued at paras. 20 to 22:

> Some evidence must be adduced on the motion to demonstrate that the mediator's evidence is likely to be probative to the issue and that the benefit to be gained by the disclosure for the correct disposal of the litigation will be greater than any injury to the mediation process by the disclosure of discussions that took place.
>
> In the instant case, there is evidence that the mediator himself drafted the minutes of settlement in his own handwriting with input from counsel and, therefore, is in a position to provide important information as to whether the minutes of settlement as executed are inconsistent with any prior oral agreement of settlement among the parties.
>
> If, indeed, the omission of Kaiser's name from the minutes of settlement was mere inadvertence, as the plaintiffs contend, it would be of benefit to the court to have the evidence of the mediator on this issue in order to prevent a possible miscarriage of justice. Any impairment to the mediation process would be minimal in this case.

17 Leave to appeal this decision was granted by Howden J. on March 7, 2005. He also made an order granting intervenor status to the Ontario Bar Association.

The Issues

18 The Appellants argued that the motions judge erred by dealing only with settlement privilege and failing to consider whether there is a general mediation privilege or a privilege protecting mediators from testifying based on the Wigmore principles. In addition, they argued that the confidentiality agreement between the parties bars the testimony of the mediator. Finally, they argued that the evidence was neither relevant nor admissible, because of the parol evidence rule and because a settlement at mediation is enforceable only if in writing.

19 The Intervenor supported the Appellants' position that discussions with the mediator are privileged at common law, and the motions judge was in error in ordering the mediator to testify.

20 The Respondents took the position that the motions judge correctly concluded that the mediator's evidence was necessary to prevent a miscarriage of justice.

Analysis

21 Rule 24.1 of the Rules of Civil Procedure deals with mandatory mediation in civil matters. The purpose of the rule is set out in rule 24.1.01:

> This Rule provides for mandatory mediation in case managed actions, in order to reduce the cost and delay in litigation and facilitate the early and fair resolution of disputes.

The nature of mediation is described in rule 24.1.02 as a situation in which "a neutral third party facilitates communication among the parties to a dispute, to assist them in reaching a mutually acceptable solution."

22 Rule 24.1.14 of the Rules of Civil Procedure states that all communications at a mediation session and the mediator's notes and records are deemed to be without prejudice settlement discussions. In Rogacki v. Belz (2003), 67 O.R. (3d) 330 (C.A.), Borins J.A. (Armstrong J.A. concurring) concluded that the rule codified the common law principle that communications made in an attempt to settle a dispute are inadmissible in evidence "unless they result in a concluded resolution of the dispute" (at para. 18).

23 The issue in that case was the availability of a contempt order against a party who had published the content of confidential discussions during mediation. The Court of Appeal held that such an order was not available.

24 The motions judge interpreted the words of Borins J.A. to mean that mediation privilege is not absolute. He then went on to say that if settlement discussions result in an agreement, communications are admissible evidence if the existence or interpretation of the agreement is in issue (at para. 14).

25 The Court of Appeal in Rogacki did not deal exhaustively with the issue of privilege for communications in mediation, as the issue before it was the availability of a contempt order. While the majority discussed rule 24.1.14, they never addressed the common law principles relating to privilege.

26 Common law principles have recognized a privilege for confidential communications in certain important societal relationships. In Slavutych v. Baker (1975), 55 D.L.R. (3d) 224, the Supreme Court of Canada held that the four conditions from Wigmore on Evidence should be applied to determine whether communications are privileged (at 228):

> (1) The communications must originate in a confidence that they will not be

disclosed.

(2) The element of confidentiality must be essential to the maintenance of the relationship in which the communications arose.

(3) The relationship must be one which, in the opinion, of the community ought to be "sedulously fostered".

(4) The injury caused to the relationship by disclosure of the communications must be greater than the benefit gained for the correct disposal of the litigation.

27 In Slavutych, the Court held that a document submitted in a university tenure process was privileged -- in part because the document was labelled "confidential", and in part because of the importance of confidentiality in the tenure process, where individuals are asked to give their frank opinion of colleagues.

28 In M.(A.) v. Ryan (1997), 143 D.L.R. (4th) 1 (S.C.C.), the Supreme Court reaffirmed the approach in Slavutych, making it clear that privilege is to be determined on a case by case basis (at para. 20). In addition, McLachlin C.J.C., writing for the majority, stated that there could be circumstances of partial privilege (at para. 37):

> My conclusion is that it is open to a judge to conclude that psychiatrist-patient records are privileged in certain circumstances. Once the first three requirements are met and a compelling prima facie case for protection is established, the focus will be on the balancing under the fourth head. A document relevant to a defence or claim may be required to be disclosed, notwithstanding the high interest of the plaintiff in keeping it confidential. On the other hand, documents of questionable relevance or which contain information available from other sources may be declared privileged. The result depends on the balance of the competing interests of disclosure and privacy in each case.

29 A number of courts have applied the Wigmore conditions to determine whether communications during mediation are privileged: Porter v. Porter (1983), 40 O.R. (2d) 417 (U.F.C.C.) at p. 421; Sinclair v. Roy (1985), 20 D.L.R. (4th) 748 (B.C.S.C.) at p. 755; Pearson v. Pearson, [1992] Y.J. No. 106 (S.C.Y.T.) at p. 2 (Quicklaw); Sambasivam v. Sambasivam (1988), 73 Sask. R. 230 (C.A.) at p. 231; A.H. v. J.T.H., [2005] B.C.J. No. 321 (B.C.S.C.) at paras. 31-33. The communications at mediation have been held to be privileged unless there were overarching interests in disclosure -- for example, to protect children at risk from criminal activity (Pearson, supra).

30 In this case, the motions judge failed to conduct an analysis based on the Wigmore conditions. Instead, he focussed solely on without prejudice settlement privilege. In so doing, he erred.

31 In this case, it is clear that the communications to the mediator originated in confidence and, therefore, the first Wigmore condition has been satisfied. The parties to this mediation signed a confidentiality agreement, which expressly stated that the communications at the mediation were to

be confidential. More importantly, the parties agreed that the mediator's notes and recollections could not be subpoenaed in this litigation.

32 The second condition requires a determination that confidentiality of communications during the mediation is essential to the functioning of the mediation process in which the parties were engaged. In order for mediation to succeed, parties must be assured of confidentiality, so that discussions can be free and frank. The following quotation from Owen v. Gray provides a useful summary of the reasons that confidentiality is vital to the operation of the mediation process (from "Protecting the Confidentiality of Communications in Mediation" (1998), 36 Osgoode Hall L.J. 667 at 671):

> The mediator encourages the parties to be candid with the mediator and each other, not just about their willingness to compromise, but also and especially about the needs and interests that underlie their positions. As those needs and interests surface, the possibility of finding a satisfactory resolution increases. The parties will be wary and guarded in their communications if they think that the information they reveal may later be used outside of the mediation process to their possible disadvantage. When they have resorted to mediation in an attempt to settle pending or threatened litigation, they will be particularly alert to the possibility that information they reveal to others in mediation may later be used against them by those others in that, or other, litigation. The parties may also be concerned that their communications might be used by other adversaries or potential adversaries, including public authorities, in other present or future conflicts. The possibility of prejudice to legal rights, or of exposure to legal liability or prosecution, may not be a party's only concern. Parties may also be concerned that disclosure of information they reveal in the mediation process may prejudice them in commercial dealings or embarrass them in their personal lives. Accordingly, mediation works best if the parties are assured that their discussions with each other and with the mediator will be kept confidential.

33 The third Wigmore condition requires a determination whether the relationship in which the communication is given is one which should be "sedulously fostered". The Rules of Civil Procedure require mandatory mediation of many civil disputes in order to assist the parties in arriving at settlement and thus reduce the costs of litigation. There is clearly a significant public interest in protecting the confidentiality of discussions at mediation in order to make the process as effective as possible.

34 That brings me to the fourth stage of the Wigmore test, where it is necessary to balance the public interest in disclosure against the interest in preserving the confidentiality of communications during the mediation process. In this case, the Respondents seek to examine the mediator as a witness on a pending motion in which they seek rectification of the written settlement agreement. The remedy of rectification rests on proof of a common intention to agree to terms different from

those in the signed document (Stephen Waddams, The Law of Contract, 5th ed. (Aurora: Canada Law Book Ltd., 2005) at pp. 232-4). While evidence relevant to the issue of mistake and the parties' intention is available from the parties themselves, the mediator is being asked to give evidence as, in effect, a tiebreaker.

35 The motions judge was of the view that the disclosure of the settlement discussions would not undermine the mediation process, since the disclosure is "sought not as an admission against a party's interest, but solely for the purpose of determining the specific terms of an agreement that both parties have arrived at" (at para. 19).

36 It is true that the mediator's evidence might be of some assistance in determining the terms of the settlement. However, it is not the only evidence available on the scope of the parties' agreement. Both the parties and their counsel can give evidence of what the agreement was. Indeed, it is the intention of the parties that is key to the resolution of the motion for rectification.

37 Weighing against disclosure is the fact that the parties entered into a confidentiality agreement in which they agreed not to make the mediator a witness. This is not a case where the parties, by their confidentiality agreement, seek to block a third party's access to information that is important for the resolution of a case. Here, the parties agreed on the rules for the mediation, which included confidentiality and non-compellability of the mediator. Absent an overriding public interest in disclosure, their agreement should be respected.

38 The motions judge concluded that the potential harm from disclosure was minimal because the parties had reached a settlement. In doing so, he assumed that the reason for the privilege was to protect parties from disclosure of admissions against interest during the mediation process. However, as set out in the earlier quotation from Mr. Gray's article, confidentiality is important not only because parties may make admissions against interest. Parties may also reveal information to a mediator which they wish to keep confidential even after a settlement is reached, perhaps because the information is private, or because it may injure a relationship with others.

39 The ability of parties to engage in full and frank disclosure is fundamental to the mediation process and to the likelihood that it will lead to resolution of a dispute. There is a danger that they will be less candid if the parties are not assured that their discussions will remain confidential, absent overarching considerations such as the revelation of criminal activity.

40 Moreover, there is a danger that a mediator will lose the appearance of neutrality if required to testify in proceedings between the parties. In her concurring judgment in Rogacki, supra, at para. 37, Abella J.A. discussed the importance of confidentiality, quoting from Jonnette Watson Hamilton, "Protecting Confidentiality in Mandatory Mediation: Lessons from Ontario and Saskatchewan" (1999), 24 Queen's L.J. 561 at 574:

> In any process forced upon parties, they must have confidence in the integrity of the process and those who have a major role in it. One of the results of requiring

> mediators to testify or produce documents may be a perception that the mediator, the program or the process itself does not keep confidences. While such a perception might normally cause parties to avoid mediation, they cannot do so where it is mandatory. They might, however, treat mediation as a mere formality.

41 The motions judge found that any impairment to the mediation process would be minimal since the mediator would only be asked about the terms of the agreement. However, it is unlikely that the questions to the mediator could be restricted to a narrow question of who the parties were meant to be in the Minutes of Settlement. Indeed, it is likely that the questions to the mediator would open up discussion of the course of negotiations in order to determine the scope of Mr. Kaiser's role.

42 The fourth condition of the Wigmore test requires a balancing of the public interest in disclosure against the public interest in preserving the confidentiality of the relationship at issue. In this case, there is an important public interest in maintaining the confidentiality of the mediation process that, in all the circumstances of this case, outweighs the interest in compelling the evidence of the mediator.

Conclusion

43 The appeal is allowed, and the order of the motions judge is set aside. If the parties cannot agree on costs of the appeal and leave to appeal motion, the Appellants may make written submissions within 21 days of the release of this decision, with the Respondents making submissions within 14 days thereafter.

44 At the end of the hearing, the Intervenor indicated that it would not be seeking costs and asked that costs not be awarded against it. Given the assistance provided to the Court by the Intervenor, no costs are awarded against it.

K.E. SWINTON J.

cp/e/qw/qlyxh

Tab 11

Case Name:

Bot Construction (Ontario) Ltd. v. Dumoulin

Between
Bot Construction (Ontario) Limited, Plaintiff, and
Marcel Rene Dumoulin, also known as Marcel Joseph Dumoulin, Laila Dumoulin, 2022539 Ontario Inc. o/a Lad Consulting, David Jaggard, Jeffrey David Trembath, Northern Fencing & Guardrail Contracting, 1621730 Ontario Inc. o/a Northern Construction & Maintenance and Towanda Timber Limited, Kristi Lin Trembath, Paula H. Jaggard, Maray Construction, Dawson Road Mini Storage Inc., Lisa I. Dumoulin, Dylan Byrnes, Defendants

[2011] O.J. No. 590

2011 ONSC 492

6 C.L.R. (4th) 99

2011 CarswellOnt 778

Court File No. CV-06-0180

Ontario Superior Court of Justice

D.C. Shaw J.

Heard: By written submissions.
Judgment: January 25, 2011.

(14 paras.)

Civil litigation -- Civil procedure -- Discovery -- Examination for discovery -- Range of examination -- Objections and compelling answers -- Production and inspection of documents -- Privileged documents -- Documents prepared for the purpose of settlement -- Motion by defendant to claim by Bot for order compelling Bot's representative to answer question refused on examination for discovery dismissed -- Question related to payment by Bot of outstanding sum to previous gravel supplier to Towanda -- Claim of previous supplier settled by Bot, terms of settlement which were confidential -- Interest in protecting confidentiality of settlement discussions

paramount to defendant's interest -- Suggestion lack of disclosure would irreparably harm defendant was mere speculation.

Motion by Towanda to compel Bot to answer questions refused on examination for discovery. Towanda sought to examine Bot's representative with respect to whether or not Bot had paid its former gravel supplier Hacquoil anything toward an outstanding invoice for gravel supplied that Bot considered rejectable. Bot's representative refused to answer because Bot had settled a claim by Hacquoil in relation to the outstanding invoice, the settlement agreement containing a confidentiality provision. The lawyer for Bot stated the terms of the settlement were not related to the subsequent re-employment of Hacquoil by Bot and were not relevant to Towanda's claim. Towanda had been retained to haul granular material in relation to the same project giving rise to the Hacquoil claim. It pleaded fraud, conspiracy and breach of fiduciary duty by Bot, relied on allegations made by Hacquoil against Bot, and took the position it replace Hacquoil as the main supplier for granular material to the project, a focal point of the present litigation.

HELD: Motion dismissed. The communications and settlement agreement between Bot and Hacquoil originated in confidence and were subject to a confidentiality agreement. Confidentiality was essential to meaningful, frank and candid settlement discussions. There was a significant public interest in protecting the confidentiality of settlement discussions. Towanda's interest in disclosure did not trump the interest in preserving the confidentiality of the settlement agreement and negotiations. It was nothing more than speculation that non-disclosure of the settlement agreement would cause Towanda irreparable harm.

Counsel:

William Shanks, for the Plaintiff.

Nick Melchiorre, for the Defendants, David Jaggard, Towanda Timber Limited, Paula H. Jaggard and Dawson Road Mini Storage Inc., (the "Towanda Defendants").

Decision Regarding Refusal -
Item No 8, Q. 1050-1052

1 **D.C. SHAW J.**:-- On December 8, 2010, I released Reasons on motions by the plaintiffs and the defendants to compel answers to refusals and to compel compliance with undertakings, given on examinations for discovery.

2 In my Reasons, I reserved my decision with respect to a refusal on the examination for discovery of Mr. Bot by the Towanda defendants, namely Item No. 8, Q. 1050 - 1052, at p. 26 of

my Reasons. (*Note:* Q. 1050 - 1052 were incorrectly shown as Q. 150 - 152.) Mr. Bot was asked questions in connection with issues between Bot Construction (Ontario) Limited and Hacquoil Construction Limited over the supply of gravel by Hacquoil to Bot Construction that Bot Construction described as "rejectable". Bot Construction wrote to Hacquoil stating that Hacquoil owed Bot Construction over $89,000.00, based on deducting the amount of the Hacquoil invoices from Bot Construction backcharges of $305,713.06. Mr. Bot testified that Hacquoil placed a lien on the job and that Bot Construction settled the matter in the following year.

3 Mr. Bot refused to answer the following question:

> "I would like to know whether Bot made a payment to Hacquoil with respect to the outstanding invoice. If so, the amount, when payment was made and whether or not the terms and consideration for that agreement to pay were in any way related to the re-employment of Hacquoil to provide services at a later date."

4 Mr. Bot refused to answer on the following basis:

> "Bot Construction has settled Hacquoil's claim against it pursuant to minutes of settlement dated April 20, 2006, which contain a confidentiality provision, pursuant to which Bot may not disclose the terms of the settlement in the absence of express consent of Hacquoil or as otherwise required by law. The terms of the settlement were not related to the re-employment of Hacquoil and are not relevant to any of the issues raised by the pleadings."

5 The defendant, Towanda Timber Limited, submits that this information is relevant because:

(1) The litigation between Bot and HCL arises directly from the same construction project that is the subject matter of this litigation;
(2) At one point during the construction project, HCL had a contract with Towanda to haul granular material;
(3) The settlement between HCL and Bot is completed and final;
(4) Bot pleads fraud, conspiracy and breach of fiduciary duty against Defendants;
(5) Bot relies on allegations made by HCL to support its claim against the Defendants; and
(6) Towanda, for all intents and purposes, replaced HCL as the main supplier of granular material to the project. That supply of granular materials to the project is a focal point of the litigation.

6 The Divisional Court dealt with the issue of disclosure of settlement documents to a third party in *Ontario (Liquor Control Board) v. Magnotta Winery Corp.* (2009), 97 O.R. (3d) 665 (Div. Ct.). At paras. 37 to 46, Carnwath J., delivering the judgment of the court, stated:

"**37** When parties share information in furtherance of settling disputes, that information is generally subject to privilege from disclosure. The documents containing the information are often, but not always, marked as being "without prejudice".

38 In Ontario, as early as 1968, Fraser J. analyzed the public policy considerations which supported non-disclosure of information shared during the course of settlement discussions and negotiations. He concluded:

> In my opinion the privilege as so often stated, is intended to encourage amicable settlements and to protect parties to negotiations for that purpose. It is in the public interest that it not be given a restrictive application.
>
> (I. Waxman & Sons Ltd. v. Texaco Canada Ltd. et al., [1968] 1 O.R. 642 at 656 (H.C.J.).)

39 The Ontario Court of Appeal confirmed Fraser. J.'s judgment:

> We find ourselves in agreement with the conclusions reached by Fraser J., and also with his analysis, in the main, of the very numerous decisions referred to in his reasons for judgment. ...
>
> (I. Waxman & Sons Ltd v. Texaco Canada Ltd. et al, [1968] 2 O.R. 452 at 453 (C.A.).)

40 In 1988, the House of Lords concluded:

> In my view, this advantage does not outweigh the damage that would be done to the conduct of settlement negotiations if solicitors thought that what was said and written between them would become common currency available to all other parties to the litigation. In my view the general public policy that applies to protect genuine negotiations from being admissible in evidence should also be extended to protect those negotiations from being discoverable to third parties.

> (Rush & Tompkins Ltd. v. Greater London Council, [1988] 3 All E.R. 737 at 744 (H.L.) [Rush].)

41 In British Columbia, the Court of Appeal endorsed the public policy basis for nondisclosure of settlement discussions. McEachern C.J.B.C. said:

> ... I find myself in agreement with the House of Lords that the public interest in the settlement of disputes generally requires "without prejudice" documents or communications created for, or communicated in the course of, settlement negotiations to be privileged. I would classify this as a "blanket", prima facie common law, or "class" privilege because it arises from settlement negotiations and protects the class of communications exchanged in the course of that worthwhile endeavour.

> (Middelkamp v. Fraser Valley Real Estate Board (1992), 96 D.L.R. (4th) 227 at 232-33 (B.C.C.A.) [Middelkamp].)

42 Chief Justice McEachern went on to say:

> In my judgment this privilege protects documents and communications created for such purposes both from production to other parties to the negotiations and to strangers, and extends as well to admissibility, and whether or not a settlement is reached. This is because, as I have said, a party communicating a proposal related to settlement, or responding to one, usually has no control over what the other side may do with such documents. Without such protection, the public interest in encouraging settlements will not be served.

(Middelkamp at 233.)

43 Also in Middelkamp Locke J.A. agreed, although he concluded the issue had to be determined on a "case-by-case" analysis rather than the class privilege proposed by Chief Justice McEachern. At 250-51, he stated:

> With all respect I cannot in law see one reason why this province, alone in

> the Commonwealth, should not recognize the overriding importance of this protection from the eyes of a third party. To refuse is to inhibit and penalize one who wishes to settle. It is easy to envisage a building owner loath to compromise the minor claim of a small sub-contractor because of concern an admission of fact would be held against him in another major subcontractors proceeding.
>
> All the cases emphasize that no bars should be placed in the way of one who wishes to compromise, and to allow the production is by definition to inhibit. Such barriers to settlement should only be permitted if the other competing interest absolutely demands it.

44 In 1992, the Supreme Court of Canada also stressed the public policy aspect of settlement negotiations in Kelvin Energy Ltd. v. Lee (1992), 97 D.L.R. (4th) 616 at 634 (S.C.C.) [Kelvin]. The Court quoted with approval the following statement from Sparling v. Southam Inc. (1988), 66 O.R. (2d) 225 at 230 (H.C.J.) [Sparling]:

> ... The Courts consistently favour the settlement of lawsuits in general. To put it another way, there is an overriding public interest in favour of settlement. This policy promotes the interest of litigants generally by saving them the expense of trial of disputed issues, and it reduces the strain upon an already overburdened provincial Court system.

45 There is strong support for a public-policy based class privilege for settlement privilege. However, that support comes from cases where the court analyzes each claim in the context of its particular facts.

46 The case-by-case analysis is preferable. It is particularly important in the following instances:

(a) where discussions have led to a settlement, the litigation has resolved, but an argument arises over the terms of the settlement;
(b) where the interests of third parties in other litigation might be affected; and,
(c) where there is a dispute over whether litigation was "in contemplation".

I conclude that any analysis undertaken to establish common law settlement privilege must be done on a case-by-case analysis."

7 Carnwath J. further stated that the existence of settlement privilege must be established on a case-by-case analysis, applying the "Wigmore" test as described in *Slavutych v. Baker*, [1976] 1 S.C.R. 254 at 260:

> (1) The communications must originate in a confidence that they will not be disclosed.
> (2) The element of confidentiality must be essential to the maintenance of the relationship in which the communications arose.
> (3) The relationship must be one which, in the opinion of the community, ought to be 'sedulously fostered'.
> (4) The injury caused to the relationship by disclosure of the communications must be greater than the benefit gained for the correct disposal of the litigation.

8 Carnwath J. noted, at para. 52, that the Supreme Court of Canada has re-affirmed the approach in *Slavutych* in *M.(A.) v. Ryan*, [1997] 1 S.C.R. 157, at para. 20.

9 In the instant case, the communications and settlement agreement between Bot Construction and Hacquoil originated in confidence. They were the subject of a confidentiality agreement. The first Wigmore condition is therefore satisfied.

10 Confidentiality is essential to meaningful, frank and candid settlement discussions. The second Wigmore condition is satisfied.

11 It is well settled that there is a significant public interest in protecting the confidentiality of settlement discussions in order to make the process as effective as possible. As noted by Carnwath J. at para. 58, confidentiality of settlement discussions should be "sedulously fostered". The third Wigmore condition is satisfied.

12 The fourth Wigmore condition requires a balancing of the interest of the Towanda and Dumoulin defendants in disclosure against the public interest in preserving the confidentiality of settlement negotiations.

13 I am not persuaded that the interest of the defendants in disclosure trumps the interest in preserving the confidentiality of the settlement agreement and negotiations leading up to the settlement agreement. In his submissions, counsel for Towanda sought production of the settlement documents on the basis that disclosure of the terms of the settlement agreement may relate to the re-engagement of Hacquoil's services by Bot Construction. However, counsel for Bot Construction states, as an officer of the court, that the terms of the settlement were not related to the re-employment of Hacquoil. The fact that Hacquoil supplied material to the same construction

project and may be a witness in the action does not meant that the terms of a settlement agreement dated April 2006, well after Towanda left the project, are relevant. Mr. Bot testified that Hacquoil had placed a lien on the job arising out of the fact that Bot had offset backcharges of $305,713.06 against Hacquoil's invoices. The backcharges related to material supplied by Hacquoil that Mr. Bot said was rejectable. I see nothing in the pleadings or in the transcript of the discovery of Mr. Bot which leads me to conclude that there is relevance to the settlement agreement that outweighs the public interest in protecting the confidentiality of settlement negotiations. Towanda submits that it would suffer "irreparable prejudice" if the settlement document is not produced, but this is a bald submission. Something more is required to succeed on the fourth Wigmore condition. Even if the suggested relevance of the settlement document is an attempt to show a weak cause of action on the part of Bot Construction (and there is nothing before me to show that this is, in fact, the case), this would be insufficient. The settlement agreement would have to have potential relevance apart from any force it might have as an admission against interest. An example of such relevance would be if the contractual relationship between Bot Construction and Hacquoil, as established by the settlement agreement, was itself in issue.

14 I therefore find that Mr. Bot is not required to answer questions 1050 to 1052.

D.C. SHAW J.

cp/e/qlafr/qlvxw/qljyw/qlhcs

Tab 12

Ainslie et al. v. CV Technologies Inc. et al.*
[Indexed as: Ainslie v. CV Technologies Inc.]

93 O.R. (3d) 200

Ontario Superior Court of Justice,

Lax J.

December 3, 2008
* A corrigendum to these reasons for decision was released on December 4, 2008. See p. 210 for text of the corrigendum.

Securities regulation -- Misrepresentation -- Statutory cause of action -- Leave of court -- Section 138.8 (2) of Securities Act not requiring every proposed defendant to file affidavit on application for leave to commence action -- Proposed defendant only required to file affidavit where it intends to lead evidence of material facts in response to motion for leave -- Plaintiffs not entitled to resort to rule 39.03 of Rules of Civil Procedure to examine proposed defendant for purposes of motion for leave under s. 138.8 of Securities Act -- Securities Act, R.S.O. 1990, c. S.5, s. 138.8 -- Rules of Civil Procedure, R.R.O. 1990, Reg. 194, rule 39.03.

The plaintiffs brought a motion under s. 138.8(2) of the Securities Act for leave to bring an action for misrepresentation under Part XXIII.1 of the Act. Section 138.8(2) of the Act provides that upon an application under s. 138.8, the plaintiff and each defendant shall serve and file one or more affidavits setting forth the material facts upon which each intends to rely. It was the plaintiffs' position that a proper interpretation of s. 138.8(2) required each of the proposed defendants to file an affidavit upon which they could be cross-examined. They brought a motion to compel each defendant to file and serve an affidavit setting forth the material facts upon which each intended to rely in response to the motion for leave. Alternatively, they sought an order requiring each defendant to be examined under rule 39.03 of the Rules of Civil Procedure.

Held, the motion should be dismissed.

Section 138.8 was not enacted to benefit plaintiffs. Rather, it was enacted to protect defendants from coercive litigation and to reduce their exposure to costly proceedings. Proposed defendants are not required to assist plaintiffs in securing evidence upon which to base an action under Part XXIII.1. The ordinary meaning of s. 138.8(2) is that a proposed defendant must file an affidavit only where it intends to lead evidence of material facts in response to the motion for leave. The plaintiffs were not entitled to resort to rule 39.03 of the Rules to examine the proposed defendants. Subsection 138.8(3) of the Act specifically provides that "the maker of such affidavit may be examined". That provision would be redundant and unnecessary if the Rules applied to permit the plaintiffs to examine any witnesses they chose. The plaintiffs had yet to meet their onus under s. 138.8(1). Their proposed reliance on rule 39.03 was not contemplated by the Act or by the principles governing examinations under that rule. To permit the plaintiffs to accomplish indirectly what they were prevented from doing directly would amount to an abuse of process.

Cases referred to

Silver v. IMAX Corp., [2008] O.J. No. 1844, 167 A.C.W.S. (3d) 881 (S.C.J.) [Leave to appeal refused [2008] O.J. No. 2751, 169 A.C.W.S. (3d) 64 (Div. Ct.)], consd [page201]

Other cases referred to

Beck v. Bradstock (1976), 14 O.R. (2d) 333, [1976] O.J. No. 2320, 2 C.P.C. 90 (H.C.J.); Canada Post Corp. v. Key Mail Canada Inc. (2005), 77 O.R. (3d) 294, [2005] O.J. No. 3653, 259 D.L.R. (4th) 309, 202 O.A.C. 158, 142 A.C.W.S. (3d) 70 (C.A.); CanWest MediaWorks Inc. v. Canada (Attorney General), [2007] O.J. No. 3119, 2007 ONCA 567, 227 O.A.C. 116, 48 C.P.C. (6th) 281, 159 A.C.W.S. (3d) 778; Epstein v. First Marathon Inc., [2000] O.J. No. 452, [2000] O.T.C. 109, 2 B.L.R. (3d) 30, 41 C.P.C. (4th) 159, 94 A.C.W.S. (3d) 1062 (S.C.J.); Fehringer v. Sun Media Corp. (2001), 54 O.R. (3d) 31, [2001] O.J. No. 5783 (S.C.J.); Kaighin Capital Inc. v. Canadian National Sportsmen's Shows (1987), 58 O.R. (2d) 790, [1987] O.J. No. 2172, 17 C.P.C. (2d) 59, 4 A.C.W.S. (3d) 5 (H.C.J.); Lang v. Kligerman, [1998] O.J. No. 3708, 82 A.C.W.S. (3d) 811 (C.A.); Meditrust Healthcare Inc. v. Shoppers Drug Mart, a Division of Imasco Retail Inc., [2000] O.J. No. 3762, 100 A.C.W.S. (3d) 226 (S.C.J.); Royal Bank v. Société Générale (Canada), [2006] O.J. No. 5081, 219 O.A.C. 83, 31 B.L.R. (4th) 63, 154 A.C.W.S. (3d) 72 (C.A.); Schreiber v. Mulroney (2007), 87 O.R. (3d) 643, [2007] O.J. No. 3901, 160 A.C.W.S. (3d) 1010 (S.C.J.); Sun-Times Media Group Inc. v. Black, 2007 CarswellOnt 1186 (S.C.J., Comm. List); Transamerica Life Insurance Co. of Canada v. Canada Life Assurance Co. (1995), 27 O.R. (3d) 291, [1995] O.J. No. 3886, 46 C.P.C. (3d) 110, 59 A.C.W.S. (3d) 864 (Gen. Div.)

Statutes referred to

Securities Act, R.S.O. 1990, c. S.5, Part XXIII.1, s. 138.3 [as am.], 138.8 [as am.]

Rules and regulations referred to

Rules of Civil Procedure, R.R.O. 1990, Reg. 194, rules 20, 20.04 [as am.], 39.03

Authorities referred to

Driedger, E., and Ruth Sullivan, Driedger on the Construction of Statutes, 3d ed. (Toronto: Butterworths, 1994)

Proposal for a Statutory Civil Remedy for Investors in the Secondary Market and Response to the Proposed Change to the Definitions of "Material Fact" and "Material Change", Canadian Securities Administrators, CSA Notice 53-302, 2000 O.S.C.B. 7383

Toronto Stock Exchange, Interim Report of the Committee on Corporate Disclosure, Toward Improved Disclosure -- A Search for Balance in Corporate Disclosure (Allen Committee Interim Report) (Toronto Stock Exchange, December 1995)

Toronto Stock Exchange, Final Report of the Committee on Corporate Disclosure, Toward Improved Disclosure -- A Search for Balance in Corporate Disclosure (Allen Committee Final Report) (Toronto Stock Exchange, March 1997)

MOTION for an order compelling the defendants to file and serve an affidavit under s. 138.8(2) of Securities Act or, alternatively, for an order for examination of the defendants under rule 39.03 of Rules of Civil Procedure.

W.V. Sasso, J. Strosberg and M.G. Robb, for plaintiffs.

A.L.W. D'Silva and P. O'Kelly, for defendants CV Technologies Inc., Harry Buddle, Gordon Tallman and Jacqueline J. Shan.

R. Heintzman and M. Fleming, for defendant Grant Thornton LLP. [page202]

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[1] **LAX J.**: -- This is one of the first actions to be brought under Part XXIII.1 of the Ontario Securities Act, R.S.O. 1990, c. S.5 as amended ("OSA"). The amendments (familiarly known as Bill 198) permit a statutory cause of action for misrepresentation in the secondary market if the plaintiffs obtain leave from the court pursuant to s. 138.8 of the Act. At issue on this motion is the interpretation of s. 138.8(2), which has not previously been interpreted.

[2] Section 138.8 provides:

> 138.8(1) No action may be commenced under section 138.3 without leave of the court granted upon motion with notice to each defendant. The court shall grant leave only where it is satisfied that,
>
> (a) the action is being brought in good faith; and
>
> (b) there is a reasonable possibility that the action will be resolved at trial in favour of the plaintiff.
>
> (2) Upon an application under this section, the plaintiff and each defendant shall serve and file one or more affidavits setting forth the material facts upon which each intends to rely.
>
> (3) The maker of such an affidavit may be examined on it in accordance with the rules of court.
>
> (4) A copy of the application for leave to proceed and any affidavits filed with the court shall be sent to the Commission when filed.

(Emphasis added)

[3] The plaintiffs' action is against CV Technologies Inc. and three of its former or present officers and directors ("CV") and against CV's former auditors, Grant Thornton LLP ("GT"). The Statement of Claim alleges that CV in its 2006 fiscal year and in the first quarter of its 2007 fiscal year falsely represented that CV's financial statements were prepared and reported in accordance with GAAP. The plaintiffs allege that the statements improperly recognized sales of its Cold-FX products to customers in the United States as revenue earned in those periods and that this did not fairly present CV's financial results. The plaintiffs therefore assert that CV's public filings contained misrepresentations and that CV and certain of its officers and directors are liable to the plaintiffs for damages. The plaintiffs also allege that GT is liable to the plaintiffs based on claims of negligence and negligent misrepresentation in connection with the audit performed by GT of CV's financial statements for its 2006 fiscal year.

[4] The leave motion and the certification motion are scheduled to be heard together in June 2009.

The plaintiffs have delivered affidavits in support of both motions and have confirmed that [page203] they have put before the court all material facts and the evidentiary basis necessary for the court to decide the leave motion. The CV defendants have filed the affidavits of two expert witnesses on which they intend to rely in opposing the leave and certification motions. GT has filed no affidavit material in response to the plaintiffs' leave motion and intends to rely on the facts disclosed in the plaintiffs' motion materials upon which they propose to cross-examine.

[5] It is the plaintiffs' position that a proper interpretation of s. 138.8(2) requires each of the proposed defendants to file an affidavit sworn in their name upon which they can be cross-examined. They bring this motion to compel each defendant to forthwith file and serve an affidavit setting forth the material facts upon which each intends to rely in response to the plaintiffs' motion for leave to plead the causes of action in s. 138.3 of the Act and to attend to be cross-examined on their affidavits. Alternatively, the plaintiffs seek an order requiring each defendant to be examined under rule 39.03 of the Rules of Civil Procedure, R.R.O. 1990, Reg. 194.

[6] The defendants submit that the plaintiffs' position is an improper attempt to dictate the evidence on which the defendants can rely in opposition to the leave motion and that it affords the plaintiffs greater rights than in an action where it is unnecessary to obtain leave. They argue that this is inconsistent with the plain meaning of the section and improperly shifts the onus from the plaintiffs to the defendants contrary to its legislative intent.

Legislative Background to Bill 198

[7] The genesis of the secondary market liability provisions including s. 138.8 can be found in the 1997 interim and final reports of the Toronto Stock Exchange Committee on Corporate Disclosure (more commonly referred to as the "Allen Committee").[1] The mandate of the Allen Committee was to examine the adequacy of continuous disclosure by public companies in Canada and to consider whether additional remedies should be made available to investors or regulators for breaches by companies of their continuous disclosure obligations. [page204]

[8] The Allen Committee recommended the adoption of a statutory civil liability regime for the secondary securities market as a means of deterring misleading continuous disclosure by issuers. In doing so, it emphasized that deterrence, rather than investor compensation, was the focus of its recommendations.[2]

[9] In response to the Allen Committee's recommendations, the Canadian Securities Administrators (the "CSA") proposed draft legislation to amend the Act and implement a secondary market liability regime. It recognized and endorsed the Allen Committee's objective which was to create a system of statutory liability that would contain enough checks and balances through, for example, the availability of due diligence defences and limitations on liability by means of damage caps so that issuers and their directors would be deterred from inadequate or untimely disclosure without, at the same time, creating a regime that would favour short-term over long-term investors. The focus on deterrence was in part a recognition that while compensation of a prospectus investor would generally involve the culpable issuer returning subscription money it received from aggrieved investors, by contrast, compensation of aggrieved secondary market investors would come at the expense of other innocent investors, particularly the issuer's continuing shareholders.[3]

[10] Initially, neither the Allen Committee, nor the CSA, proposed a gatekeeper mechanism such as that now found in s. 138.8(1) of the Act. However, in response to comments received by the CSA during the public consultation process, the CSA recommended this as a means to dissuade plaintiffs from bringing "strike suits" -- that is, coercive and unmeritorious claims which are aimed at pressuring a defendant into a settlement in order to avoid costly litigation.[4] These had become increasingly frequent

in securities class action litigation in the United States and ultimately led to legislative reforms there.

[11] The Allen Committee had concluded that the litigation environment in Canada was sufficiently different to the United States to make it unlikely that meritless class actions would be brought, but after the release in 1997 of the Allen Committee Final Report, a "strike suit" showed up in an Ontario courtroom.[5] The issuer [page205] community, which had opposed the introduction of secondary market liability provisions, was successful in persuading the CSA of the need to introduce measures to deter the potential for them.

[12] In recommending that the Act include a screening mechanism, the CSA concluded that, irrespective of whether it was believed that the proposed legislation would result in strike suits, a screening mechanism was necessary in order to prevent corporate defendants from being exposed to proceedings "that cause real harm to long-term shareholders and resulting damage to our capital markets".[6] The 2000 Draft Legislation proposed by the CSA retained the "loser pay" costs, proportionate liability and damage cap provisions recommended by the Allen Committee, but added the screening mechanism now found in s. 138.8(1). The CSA described its purpose as follows:

> This screening mechanism is designed not only to minimize the prospects of an adverse court award in the absence of a meritorious claim but, more importantly, to try to ensure that unmeritorious litigation and the time and expense it imposes on defendants, is avoided or brought to an end early in the litigation process.[7]

(Emphasis added)

[13] In the result, the CSA revised its proposed legislation to incorporate a provision requiring plaintiffs to obtain leave from the court in order to bring an action for secondary market liability. The CSA's proposed legislation for secondary market liability was ultimately adopted, with some modifications in Bill 198 which was introduced for first reading in the legislature on October 30, 2002 and was given royal assent on December 9, 2002. Following technical amendments to certain sections of the secondary market liability provisions, Part XXIII.1 of the Act was proclaimed into force on December 31, 2005.

The Interpretation of Section 138.8(2)

[14] Section 138.8(1) sets out a two-part test for obtaining leave to bring an action under Part XXIII.1 of the OSA and places the onus on the plaintiffs to demonstrate that (1) their proposed action is brought in good faith and (2) has a reasonable prospect for success at trial. As s. 138.8(1) requires an examination of the merits, the plaintiffs submit that the section is supplemented with s. 138.8(2) and (3). They rely on the mandatory language in s. 138.8(2) ("and each defendant shall" [emphasis added]) and [page206] submit that without the benefit of this requirement and the ability to cross-examine, a plaintiff would be deprived of the tools necessary to meet the standard the legislature created in s. 138.8(1).

[15] This submission ignores the legislative purpose of s. 138.8. The section was not enacted to benefit plaintiffs or to level the playing field for them in prosecuting an action under Part XXIII.1 of the Act. Rather, it was enacted to protect defendants from coercive litigation and to reduce their exposure to costly proceedings. No onus is placed upon proposed defendants by s. 138.8. Nor are they required to assist plaintiffs in securing evidence upon which to base an action under Part XXIII.1. The essence of the leave motion is that putative plaintiffs are required to demonstrate the propriety of their proposed secondary market liability claim before a defendant is required to respond. Section 138.8(2) must be interpreted to reflect this underlying policy rationale and the legislature's intention in imposing a "gatekeeper mechanism".

[16] The plaintiffs appear to be interpreting s. 138.8(2) as if it read: "Upon an application under this section, the plaintiff and each defendant shall serve and file one or more affidavits." But, the subsection continues: "setting forth the material facts upon which each intends to rely". If there are no material facts upon which a defendant intends to rely in responding to a leave motion, how can it be that a defendant is required to file an affidavit? Similarly, if a defendant files one or more affidavits, how can a plaintiff require that defendant to file other affidavits? By discounting this language, the plaintiffs are proposing an interpretation which relieves them of their obligation to demonstrate that their proposed action meets the pre-conditions for granting leave under the Act.

[17] The plaintiffs' interpretation also fails to address the language used in subsections (3) and (4). Section 138.8(3) reads: "The maker of such an affidavit may be examined on it in accordance with the rules of court." Section 138.8(4) reads: "A copy of the application for leave to proceed and any affidavits filed with the court shall be sent to the Commission when filed" (emphasis added). Had it been the intention of the legislature to require the parties to file affidavits, irrespective of the onus placed upon the moving party, the legislature would have substituted the word "the" for "any" in s. 138.8(4) and the words "the plaintiff and each defendant" for "maker" in s. 138.8(3). I also note that the legislature attached no consequences to the failure of "each defendant" to file an affidavit.

[18] In terms of onus, a useful analogy can be found in the summary judgment rule, Rule 20, of the Rules of Civil Procedure. Rule 20.04 provides: [page207]

> 20.04(1) In response to affidavit material or other evidence supporting a motion for summary judgment, a responding party may not rest on the mere allegations or denials of the party's pleadings but must set out, in affidavit material or other evidence, specific facts showing that there is a genuine issue for trial.

(Emphasis added)

[19] Similar to s. 138.8(2), rule 20.04 utilizes language suggesting that a responding party "must" or "shall" file affidavit material. Notwithstanding the use of such language, under Rule 20, a responding party retains the option to counter the motion by simply cross-examining the moving party, rather than by leading any direct evidence on the motion. In this regard, rule 20.04 has been interpreted as requiring the respondent to a summary judgment motion to "lead trump or risk losing". Notably, however, the onus to establish that there is no genuine issue for trial remains with the moving party. The onus does not shift to the respondent to show that a genuine issue for trial does in fact exist.[8]

[20] Similarly, in a motion under s. 138.8 of the Act, the onus to demonstrate that the proposed claim meets the required threshold remains with the plaintiffs. The onus does not shift to the defendants. A defendant that does not "lead trump" by filing affidavit evidence in response to a motion under s. 138.8 may well take the risk that leave will be granted to the plaintiffs. It does not follow, however, that a defendant is obligated to file evidence or produce an affidavit from each named defendant. It is a well-established principle that, as a general proposition, it is counsel who decides on the witnesses whose evidence will be put forward.[9]

[21] The plaintiffs submit that their interpretation of s. 138.8(2) and (3) is consistent with the only judicial interpretation of Part XXIII.1 of the OSA, referring to the decision in Silver v. IMAX Corp.[10] In that case, the proposed defendants (the corporation and certain directors) chose to file affidavits setting out the statutory defences upon which they intended to rely in response to a [page208] motion for leave pursuant to s. 138.8(1). The issue in IMAX was the permissible scope of the examination on those affidavits authorized by s. 138.8(3).

[22] In concluding that the defendants were required to answer questions that met the "semblance of relevance" test, van Rensburg J. appears to have been influenced by the unfairness that would result if the defendants were able to file evidence asserting statutory defences but were immune to having that evidence fully tested by cross-examination. Her comments must be considered in this context: As she stated [at paras. 17, 19]:

> The Securities Act provides its own procedure in respect of the statutory remedy, that specifically requires proposed defendants to put forward information (presumably otherwise confidential and non-compellable information to the extent it may be relevant to their defence) . . .
>
> . . . . .
>
> There is no indication in the statute that evidence put forward or examined upon must be restricted to what is in the public record. Indeed the facts to support a due diligence defence are generally in the possession and control of the party asserting such a defence.

(Emphasis added)

[23] In IMAX, van Rensburg J. considered [at para. 19] s. 138.8(2) to prescribe a "mandatory requirement for each plaintiff and each proposed defendant to set out the facts by affidavit, with the right to cross-examine". I respectfully suggest that these comments should be confined to the facts and circumstances at issue in IMAX. These comments were made in obiter in resolving a refusals motion in circumstances where the defendants had filed affidavit material. It is important to recognize that in IMAX, the court was not addressing the interpretation of s. 138.8(2). The reasons make no reference to the Allen Committee Reports or CSA Notice 53-302, which are admissible as evidence of the purpose of legislation and the intention of the legislature. I regard these documents as essential interpretive tools, but it would appear that they were not provided to the court in IMAX.

[24] In my view, the "gatekeeper provision" was intended to set a bar. That bar would be considerably lowered if the plaintiffs' view is correct. As I have already indicated, a defendant who does not file affidavit material accepts the risk that it may be impairing its ability to successfully defeat the motion for leave and is probably foregoing the right to assert the statutory defences under Part XXIII.1 of the Act. However, parties are entitled to present their case as they see fit and this includes the right to oppose the leave motion on the basis of the record put forward by the plaintiffs as GT intends, or on the basis of the affidavits of experts as CV intends. [page209]

[25] To accept the plaintiffs' submissions would require each defendant to produce evidence that may not be necessary for the leave motion and would serve no purpose other than to expose those defendants to a time-consuming and costly discovery process. It would sanction "fishing expeditions" prior to the plaintiffs obtaining leave to proceed with their proposed action. This is an unreasonable interpretation of s. 138.8(2). It is inconsistent with the scheme and object of the Act. Properly interpreted, the ordinary meaning of s. 138.8(2) is that a proposed defendant must file an affidavit only where it intends to lead evidence of material facts in response to the motion for leave.

Rule 39.03

[26] It is well-established that a proposed examination under rule 39.03 will not be permitted if it is being used for an ulterior or improper purpose or is nothing more than a "fishing expedition".[11] In Beck v. Bradstock, for example, the court refused to permit an examination under rule 39.03 -- notwithstanding that the information from the proposed examination would be relevant to the motion at

issue -- because the plaintiff intended to use the proposed examination for the improper purpose of obtaining information to commence an action against the witness. The court held that such an examination would constitute an abuse of process.[12]

[27] In addition, an examination under rule 39.03 is improper if the purpose of the examination is to prematurely inquire into a party's defences or otherwise commence the discovery process before the close of pleadings.[13] For instance, in Fehringer v. Sun Media Corp., the plaintiff sought to examine the defendants under rule 39.03 in relation to a motion for certification. The court held that the proposed examinations under rule 39.03 constitute an abuse of process insofar as those examinations would (i) allow the plaintiffs to conduct a general examination of the defendants before the close of pleadings and (ii) impose a significant cost [page210] burden on those defendants before it was [known] if the action was certifiable.[14]

[28] The Securities Act provides its own procedure in respect of the statutory remedy and it should not be presumed that all of the rights and procedures under the Rules apply.[15] Section 138.8(3) of the OSA specifically provides that "the maker of such affidavit may be examined". This provision would be redundant and unnecessary if the Rules applied to permit the plaintiffs to examine any witnesses they chose.

[29] The plaintiffs have yet to meet their onus under s. 138.8(1). Their proposed reliance on rule 39.03 is neither contemplated by the statute nor by the principles governing examinations under this rule. To permit the plaintiffs to accomplish indirectly what they are prevented from doing directly would amount to an abuse of process.

[30] For these reasons, the plaintiffs' motion is dismissed.

[31] If the parties are unable to agree on costs, they may submit costs outlines and brief submissions within 30 days.

Motion dismissed.

CORRIGENDUM

December 4, 2008

[1] LAX J.: -- In Reasons for Decision in an interlocutory motion in this proposed class proceeding, released December 3, 2008, I said, at para. 23, that it appeared that the court in Silver v. IMAX, [2008] O.J. No. 1844 (S.C.J.) had not been provided with the Allen Committee Reports and CSA Notice 53-302 on the hearing of a motion in that case. It has since been brought to my attention that these references were provided to the court.

[2] I was also in error in stating that the court in IMAX had made no reference to these documents. I regret that I overlooked a reference to CSA 53-302 in para. 14 of the IMAX reasons.

[3] This information does not change my conclusion or my analysis.

Notes

1 Interim Report of the Committee on Corporate Disclosure, Toward Improved Disclosure - A Search for Balance in Corporate Disclosure (Allen Committee Interim Report), Toronto Stock Exchange (December 1995) at p. iii; Final Report of the Committee on Corporate Disclosure, Toward Improved Disclosure - A Search for Balance in Corporate Disclosure (Allen Committee Final Report), Toronto Stock Exchange (March 1997); Canadian Securities Administrators Notice 53-302 ("CSA Notice 53-302"), 2000 O.S.C.B. 7383, at 7385.

2 Allen Committee Interim Report, at p. 58; Allen Committee Final Report, at pp. 41-42; CSA Notice 53-302, at p. 7386.

3 CSA Notice 53-302, at p. 7387.

4 Ibid., at pp. 7389-90.

5 Epstein v. First Marathon Inc., [2000] O.J. No. 452, 2 B.L.R. (3d) 30 (S.C.J.).

6 CSA Notice 53-302, at p. 7389.

7 Ibid., at p. 7390.

8 Royal Bank v. Société Générale (Canada), [2006] O.J. No. 5081, 31 B.L.R. (4th) 63 (C.A.), at paras. 35-37; Lang v. Kligerman, [1998] O.J. No. 3708, 82 A.C.W.S. (3d) 811 (C.A.), at para. 9; Meditrust Healthcare Inc. v. Shoppers Drug Mart, a Division of Imasco Retail Inc., [2000] O.J. No. 3762, 100 A.C.W.S. (3d) 226 (S.C.J.), at para. 11; Kaighin Capital Inc. v. Canadian National Sportsmen's Shows (1987), 58 O.R. (2d) 790, [1987] O.J. No. 2172 (H.C.J.), at p. 792.

9 CanWest MediaWorks Inc. v. Canada (Attorney General), [2007] O.J. No. 3119, 48 C.P.C. (6th) 281 (C.A.), at p. 285 C.P.C.

10 [2008] O.J. No. 1844, 167 A.C.W.S. (3d) 881 (S.C.J.), leave to appeal refused [2008] O.J. No. 2751, 169 A.C.W.S. (3d) 64 (Div. Ct.).

11 Transamerica Life Insurance Co. of Canada v. Canada Life Assurance Co. (1995), 27 O.R. (3d) 291, [1995] O.J. No. 3886 (Gen. Div.), at p. 299 O.R.; Schreiber v. Mulroney (2007), 87 O.R. (3d) 643, [2007] O.J. No. 3901 (S.C.J.), at p. 648 O.R.

12 (1976), 14 O.R. (2d) 333, [1976] O.J. No. 2320 (H.C.J.), at p. 337 O.R., per Cory J.

13 Fehringer v. Sun Media Corp. (2001), 54 O.R. (3d) 31, [2001] O.J. No. 5783 (S.C.J.), at p. 35 O.R.; See also, Sun-Times Media Group Inc. v. Black, 2007 CarswellOnt 1186 (S.C.J., Comm. List), at paras. 46-47.

14 Fehringer v. Sun Media Corp., supra, at p. 35 O.R.

15 Elmer Driedger and Ruth Sullivan, Driedger on the Construction of Statutes, 3d ed. (Toronto: Butterworths, 1994) at p. 168; Canada Post Corp. v. Key Mail Canada Inc. (2005), 77 O.R. (3d) 294, [2005] O.J. No. 3653 (C.A.).

Tab 13

The Trustees of the Labourers' Pension Fund of Central and Eastern Canada et al. v. Sino-Forest Corporation et al. [Indexed as: Labourers' Pension Fund of Central and Eastern Canada v. Sino-Forest Corp.]

110 O.R. (3d) 173

2012 ONSC 1924

Ontario Superior Court of Justice,

Perell J.

March 26, 2012

Civil procedure -- Class proceedings -- Certification -- Plaintiffs bringing proposed class action and moving for leave to assert causes of action pursuant to ss. 138.3 and 138.8 of Securities Act -- Leave motion and certification motion ordered to be heard together -- Securities Act, R.S.O. 1990, c. S.5, ss. 138.3, 138.8.

Civil procedure -- Class proceedings -- Pleadings -- Plaintiffs bringing proposed class action and moving for leave to assert causes of action pursuant to ss. 138.3 and 138.8 of Securities Act -- Defendants objecting to delivering statement of defence before leave motion and certification motion were heard -- Pleadings should generally be completed before certification motion -- Defendants who delivered affidavit pursuant to s. 138.8(2) of Securities Act ordered to deliver statement of defence -- Delivery of statement of defence not precluding defendant from bringing Rule 21 motion at leave and certification motion or from contesting that plaintiffs had shown cause of action -- Securities Act, R.S.O. 1990, c. S.5, ss. 138.3, 138.8.

The plaintiffs brought a proposed class action against the defendants, alleging that the defendants made misrepresentations in the primary and secondary markets. They also claimed against some of the defendants for a corporate oppression remedy, negligence, negligent misrepresentation, conspiracy and unjust enrichment. They had moved for leave to assert causes of action pursuant to ss. 138.3 and 138.8 under Part XXIII.1 of the Securities Act. The plaintiffs brought a motion for an order requiring the defendants to deliver a statement of defence. The defendants objected to filing a statement of defence before the certification motion and before leave was granted pursuant to s. 138.8 of the Securities Act. The plaintiffs also sought to have the certification motion and the leave motion under s. 138.8 of the Securities Act heard together. The defendants submitted that a series of motions should be scheduled, beginning with the leave motion, followed by Rule 21 (of the Rules of Civil Procedure, R.R.O. 1990, Reg. 194) motions, followed by the certification motion.

Held, the motion should be granted in part.

It was the clear intention of the legislature that the pleadings be closed before certification. It would not be contrary to law or a denial of due process to order the pre-certification delivery of a statement of defence. While it would be inappropriate to order all the defendants to deliver a statement of defence to

a secondary market claim under the Securities Act, it would be proper to order any defendant who delivered an affidavit pursuant to s. 138.8(2) of the Act to also deliver a statement of defence. Any other defendant may, if so advised, deliver a statement of defence. The delivery of the statement of defence was not a fresh step, and any defendant who did so was not precluded from bringing a Rule 21 motion at the leave and certification motion or from contesting that the plaintiffs [page174] had shown a cause of action under s. 5(1)(a) of the Class Proceedings Act, 1992, S.O. 1992, c. 6.

It would be fair and efficient to hear the certification motion and the leave motion together. If a sequential approach were adopted, there would be appeals at each stage, leading to increased delay.

Cases referred to

Pennyfeather v. Timminco Ltd. (2011), 107 O.R. (3d) 201, [2011] O.J. No. 3286, 2011 ONSC 4257; Sharma v. Timminco Ltd., [2012] O.J. No. 719, 2012 ONCA 107; Sharma v. Timminco Ltd., [2010] O.J. No. 469, 2010 ONSC 790, consd

Other cases referred to

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Statutes referred to

Class Proceedings Act, 1992, S.O. 1992, c. 6, ss. 5(1)(a), 12, 28, 35

Securities Act, R.S.O. 1990, c. S.5, ss. 130 [as am.], (3), (4), (5), Part XXIII.1 [as am.], ss. 138.3 [as am.], 138.8 [as am.], (2)

Rules and regulations referred to

Rules of Civil Procedure, R.R.O. 1990, Reg. 194, rules 1.04, 20, 21, 25.06(1), 25.07

MOTION for an order requiring the defendants to deliver a statement of defence.

Kirk M. Baert and Michael Robb, for plaintiffs. [page175]

Michael Eizenga, for Sino-Forest Corporation, Simon Murray, Edmund Mak, W. Judson Martin, Kai Kit Poon and Peter Wang.

Emily Cole and Megan Mackey, for Allan T.Y. Chan.

Peter Wardle and Simon Bieber, for David J. Horsley.

Laura Fric and Geoffrey Grove, for William E. Ardell, James P. Bowland, James M.E. Hyde and Garry J. West.

John Fabello and Andrew Gray, for Credit Suisse Securities (Canada) Inc., TD Securities Inc., Dundee Securities Corporation, RBC Dominion Securities Inc., Scotia Capital Inc., CIBC World Markets Inc., Merrill Lynch Canada Inc., Canaccord Financial Ltd., Maison Placements Canada Inc., Credit Suisse Securities (USA) LLC and Banc of America Securities LLC.

Peter H. Griffin and Shara Roy, for Ernst & Young LLP.

Kenneth Dekker and Michelle Booth, for BDO Limited.

John Pirie and David Gadsden, for Pöyry (Beijing) Consulting Company Limited.

PERELL J.: --

A. Introduction

[1] A motion for an order requiring a defendant to deliver a statement of defence or for an order setting a timetable for a motion should not be a momentous matter. But scheduling is a very big deal in this very big case under the Class Proceedings Act, 1992, S.O. 1992, c. 6.

[2] The defendants strenuously resist delivering a statement of defence before the certification motion, and they submit that it would [be] both contrary to law and a denial of due process to require them to plead in the normal course of an action.

[3] The defendants submit that having to plead their statement of defence is contrary to law because the plaintiffs' statement of claim can be commenced only with leave pursuant to s. 138.8 of the Securities Act, R.S.O. 1990, c. S.5 and in Sharma v. Timminco Ltd., [2012] O.J. No. 719, 2012 ONCA 107 the Court of Appeal ruled that the statement of claim does not exist until leave is granted. The defendants submit that having to plead their statement of defence is a denial of due process because the plaintiffs' statement of claim includes causes of action that might not survive a challenge under Rule 21 of the Rules of Civil Procedure, R.R.O. 1990, Reg. 194. One of the defendants, BDO Limited, also argues that claims against it are statute-barred, and, therefore, it should not be required to deliver a statement of defence but should be permitted to bring a Rule 21 motion before the certification hearing.

[page176]

[4] The position of the defendants is set out in para. 2 of the defendant Sino-Forest Corporation's factum as follows:

> 2. The Responding Parties oppose the relief relating to the delivery of a statement of defence because, as a result of the Ontario Court of Appeal's decision in Sharma v. Timminco, the secondary market action has yet to be commenced and will not have been commenced unless and until leave has been granted by this Honourable Court. Accordingly, the Defendants cannot be required to deliver a statement of defence to a proceeding that has yet to be commenced. Moreover, the secondary market claims are intertwined with the balance of the allegations in the statement of claim, such that it would not be realistic to provide a partial or bifurcated defence. In addition, the Responding Parties expect to be bringing a motion to strike the Statement of claim, at least in respect of the portion of the claim that purports to be brought on behalf of Noteholders, who are prohibited from commencing such a claim by virtue of the no suits by holder clause.

[5] In response, the plaintiffs submit that just as defendants are entitled to know the case they must meet, plaintiffs are entitled to know the defence they confront. The plaintiffs submit that the law and the dictates of due process do not preclude ordering the delivery of a statement of defence in accordance with the Rules of Civil Procedure, and the plaintiffs' rely on the court's power under s. 12 of the Class Proceedings Act, 1992 and on what I said in Pennyfeather v. Timminco Ltd. (2011), 107 O.R. (3d) 201, [2011] O.J. No. 3286, 2011 ONSC 4257 about the desirability of the pleadings being closed before the certification motion.

[6] In the immediate case, the defendants also strenuously resist the plaintiffs' request that the leave motion under s. 138.8 the Securities Act and the certification motion under the Class Proceedings Act, 1992 be heard together. Instead of a combined leave and certification motion, the defendants submit that a series of motions be scheduled, beginning with the leave motion, followed by Rule 21 motions, followed by the certification motion. Some defendants would begin with the Rule 21 motions before the leave motion, but all wish a sequence of separate motions.

[7] The defendants submit that a combined leave and certification motion would be both inappropriate and also unfair, and particularly so if they are also required to plead their defences. The defendants submit that fairness dictates that leave be determined in advance of certification and that their right to attack all or part of whatever pleading emerges from the leave motion be preserved. They submit that it would be inefficient to deliver a statement of defence when the statement of claim is likely to be amended in a substantial manner depending on the outcome of the plaintiffs' leave motion and the Rule 21 motions. [page177]

[8] The plaintiffs regard the defendants' proposal of a sequence of motions as something akin to having their action being sentenced to a life of imprisonment on Devil's Island.

[9] For the reasons that follow, I adjourn the motion as it concerns BDO Limited, and I order that there shall be a combined leave and certification motion on November 21-30, 2012 (ten days).

[10] I order that the "Proposed Fresh as Amended Statement of Claim" be the statement of claim for the purposes of the leave and certification motion and that this pleading shall not be amended without leave of the court. Further, I order that with the exception of the plaintiffs' funding motion, there shall be no other motions before the leave and certification motion without leave of the court first being obtained.

[11] I do not agree that it would be contrary to law or a denial of due process to order the pre-certification delivery of a statement of defence; nevertheless, I shall not order all the defendants to deliver their statements of defence before the combined leave and certification.

[12] Rather, I shall order that a statement of defence be delivered by any defendant that delivers an affidavit pursuant to s. 138.8(2) of the Securities Act. I order that any other defendant may, if so advised, deliver a statement of defence. Further, I order that if a defendant delivers a statement of defence, then the delivery of the statement of defence is not a fresh step and the defendant is not precluded from bringing a Rule 21 motion at the leave and certification motion or from contesting that the plaintiffs have shown a cause of action under s. 5(1)(a) of the Class Proceedings Act, 1992.

[13] In my reasons, I will explain why it may be advantageous to a defendant to deliver a statement of defence although it may not be obliged to do so.

[14] Finally, in my reasons, I will establish a timetable for the funding motion and for the leave and certification motion, which timetable may be adjusted, if necessary, by directions made at a case conference.

B. Factual and Procedural Background

[15] Sino-Forest is a Canadian public company whose shares formerly traded on the Toronto Stock Exchange. At the moment, trading is suspended because on June 2, 2011, Muddy Waters Research released a research report alleging fraud by Sino-Forest. The release of the report had a catastrophic effect on Sino-Forest's share price. [page178]

[16] On June 20, 2011, the Trustees of the Labourers' Pension Fund of Central and Eastern Canada ("Labourers") retained Koskie Minsky LLP to sue Sino-Forest. Koskie Minsky issued a notice of action in a proposed class action with Labourers as the proposed representative plaintiff.

[17] The June action, however, was not pursued, and in July 2011, Labourers and another pension fund, the Trustees of the International Union of Operating Engineers Local 793 Pension Plan for Operating Engineers in Ontario ("Engineers") retained Koskie Minsky and Siskinds LLP to commence a new action, which followed on July 20, 2011 by notice of action. The statement of claim in Labourers v. Sino-Forest, which is the action now before the court, was served in August 2011.

[18] On November 4, 2011, Labourers served the defendants in Labourers v. Sino-Forest with the notice of motion for an order granting leave to assert the causes of action under Part XXIII.1 of the Ontario Securities Act.

[19] At this time, there were rival class actions. Douglas Smith had retained Rochon Genova, LLP. Rochon Genova issued a notice of action on June 8, 2011. The statement of claim in Smith v. Sino-Forest followed on July 8, 2011. Northwest & Ethical Investments L.P. and Comité Syndical National de Retraite Bâtirente Inc. retained Kim Orr Barristers P.C., and on September 26, 2011, Kim Orr commenced Northwest v. Sino-Forest.

[20] On December 20 and 21, 2011, there was a carriage motion, and on January 6, 2012, I released my judgment awarding carriage to class counsel in Labourers v. Sino-Forest. I granted leave to the plaintiffs to deliver a Fresh as Amended Statement of Claim, which may include the joinder of the plaintiffs and the causes of action set out in Grant v. Sino-Forest, Smith v. Sino-Forest and Northwest v. Sino-Forest, as the plaintiffs may be advised.

[21] On January 26, 2012, the plaintiffs delivered an Amended Statement of Claim.

[22] On March 2, 2012, the plaintiffs initiated a motion seeking leave to assert causes of action pursuant to ss. 138.3 and 138.8 under Part XXIII.1 of the Securities Act.

[23] Plaintiffs' motion materials included a draft Fresh as Amended Statement of Claim for the eventuality that leave is granted ("Proposed Fresh as Amended Statement of Claim"). The Proposed Fresh as Amended Statement of Claim substantially amends and extends the allegations contained in the pleading delivered in January 2012.

[24] In their various pleadings, the plaintiffs allege that Sino-Forest and the other defendants made misrepresentations in the [page179] primary and secondary markets. The plaintiffs claims include US$0.8 billion for primary market claims, US$1.8 billion for noteholders and US$6.5 billion for secondary market claims. There are also claims against some of the defendants for a corporate oppression remedy, negligence, negligent misrepresentation, conspiracy and unjust enrichment. The following chart describes the claims against each defendant:

	S.A. s. 130 (prospectus)	S.A. s. 130.1 (offering memorandum)	S.A. s. 138.3 (secondary market)	Negligent misrepresentation (secondary market)	Negligent misrepresentation (prospectus / o-memo)	Negligence (prospectus, offering memorandum)	Unjust Enrichment	CBCA Oppression	Conspiracy
Sino Forest	X	X	X	X	X	X	X	X	X
Chan	X		X	X	X	X	X	X	X
Horsley	X		X	X	X	X	X	X	X
Poon	X		X	X	X	X	X	X	X
Wang	X		X	X	X	X		X	
Martin	X		X	X	X	X	X	X	
Mak	X		X		X	X	X	X	
Murray	X		X	X	X	X	X	X	
Hyde	X		X	X	X	X		X	
Ardell			X	X				X	
Bowland			X	X				X	
West			X	X				X	
Ernst & Young	X		X	X	X	X			
BDO Ltd.	X		X	X	X	X			
Boyry (Beijing)	X		X			X			
Credit Suisse	X				X	X	X		
TD Securities	X				X	X	X		
Dundee Securities	X				X	X	X		
RBC Dominion	X				X	X	X		
Scotia Capital	X				X	X	X		
CIBC World	X				X	X	X		
Merrill Lynch	X				X	X	X		
Canaccord	X				X	X	X		
Maison	X				X	X	X		
Credit Suisse (USA)						X	X		
Banc of America						X	X		

[25] On March 6, 2012, there was a case conference, and I scheduled ten days of hearings from November 21 to November 30, 2012. Apart from deciding that the leave motion must be [page180] heard, I did not decide what would be the subject matter of those hearing dates.

[26] None of the defendants has served a statement of defence. None has advised which, if any, statutory or common law defences they will advance in response to the plaintiffs' claims. In this regard, it may be noted that the plaintiffs advance claims under s. 130 of the Securities Act with respect to misrepresentations in the primary market. These claims raises at least eight possible statutory defences, which are set out in s. 130(3), (4) and (5) of the Securities Act. If leave is granted, the plaintiffs also advance claims under Part XXIII.1 of the Securities Act. As noted in Sino-Forest's factum for this motion, there are at least 11 defences to secondary market claims.

C. Discussion

1. Introduction

[27] In this introductory section, I will address the one relatively easy issue, i.e., the problem of the "moving target" statement of claim.

[28] In the sections that follow, I will address the more difficult issues of (a) whether the defendants can and should be ordered to deliver statements of defence; (b) whether the leave motion should be combined with the certification motion or instead there should be a sequence of motions; (c) what other motions, if any, should be permitted before the certification motion; and (d) what should the timetable be for the motions.

[29] Beginning with the relatively easy problem, at the argument of this motion, the defendants vociferously complained that the plaintiffs keep changing their statement of claim. The defendants pointed to substantial differences among the statement of claim delivered before the carriage motion, the statement of claim delivered after the carriage motion and the Proposed Fresh as Amended Statement of Claim offered up for the purposes of the leave motion.

[30] This complaint about a "moving target" statement of claim was advanced as part of the defendants' arguments that they cannot legally be ordered to deliver a statement of defence. I, however, do not see how this complaint supports that particular argument.

[31] I rather regard the "moving target" complaint as a proper objection that if the defendants are to be ordered to deliver a statement of defence, the content of the statement of claim needs first to be finalized. [page181]

[32] I agree that for the purposes of a leave or a certification motion, the content of the statement of claim needs to be finalized, and thus the approach should be to order a pleading to be finalized and to order that this pleading not be amended without leave of the court. I so order.

[33] The problem then becomes one of selecting which pleading to finalize for the purposes of the leave and certification motion. It makes common sense to select the pleading for which leave is being sought under the Securities Act, i.e., the Proposed Fresh as Amended Statement of Claim, and that indeed is my selection.

2. The delivery of the statement of defence in class actions

[34] I turn now to the difficult issues of whether the defendants can be ordered to deliver statements of defence, and if they can be ordered to plead, whether they should be ordered to plead.

[35] As will be seen shortly, the defendants submit that they cannot be ordered to plead to a secondary market claim that does not exist unless and until leave is granted under s. 138.8 of the

Securities Act. For present purposes, I will accept the correctness of this submission, but it does not follow that the defendants cannot plead to that portion of the Proposed Fresh as Amended Statement of Claim that is not exclusively referable to the secondary market claims. Assuming that the defendants are correct that there is a portion of the Proposed Fresh as Amended Statement of Claim to which they cannot be obliged to plead does not negate that there are portions of the Proposed Fresh as Amended Statement of Claim that can and should be answered by a statement of defence.

[36] The defendants' submission, rather, means that rule 25.07 of the Rules of Civil Procedure, which provides the rules of pleading applicable to defences, needs to be amended for the purpose of the leave and certification motion so that defendants do not have to plead to a pregnant action under Part XXIII.1 of the Securities Act that may never be born.

[37] Rule 25.07 states:

Admissions

> 25.07(1) In a defence, a party shall admit every allegation of fact in the opposite party's pleading that the party does not dispute.
>
> Denials
>
> (2) Subject to subrule (6), all allegations of fact that are not denied in a party's defence shall be deemed to be admitted unless the party pleads having no knowledge in respect of the fact. [page182]
>
> Different Version of Facts
>
> (3) Where a party intends to prove a version of the facts different from that pleaded by the opposite party, a denial of the version so pleaded is not sufficient, but the party shall plead the party's own version of the facts in the defence.
>
> Affirmative Defences
>
> (4) In a defence, a party shall plead any matter on which the party intends to rely to defeat the claim of the opposite party and which, if not specifically pleaded, might take the opposite party by surprise or raise an issue that has not been raised in the opposite party's pleading.
>
> Effect of Denial of Agreement
>
> (5) Where an agreement is alleged in a pleading, a denial of the agreement by the opposite party shall be construed only as a denial of the making of the agreement or of the facts from which the agreement may be implied by law, and not as a denial of the legality or sufficiency in law of the agreement.
>
> Damages
>
> (6) In an action for damages, the amount of damages shall be deemed to be in issue unless specifically admitted.

[38] To repeat, for the purposes of the leave motion where a party cannot be obliged to plead and for

the combined certification motion, rule 25.07 needs to be revised to accommodate s. 138.8 of the Securities Act.

[39] Pursuant to the authority provided by s. 12 of the Class Proceedings Act, 1992, which authorizes the court to make any order it considers appropriate respecting the conduct of a class proceeding to ensure its fair and expeditious determination, I have the jurisdiction to revise the procedure for a class proceeding to accommodate s. 138.8 of the Securities Act, and I do so by notionally adding a new subrule 25.07(7) as follows:

> (7) In an action under the Class Proceedings Act, 1992 for which leave is also being sought to commence an action under section 138.3 of the Securities Act (liability for secondary market disclosure), in a defence, a party who does not file an affidavit pursuant to rule 138.8(2) and who delivers a statement of defence shall decline to either admit or deny the allegations of fact referable solely to his or her liability for secondary market disclosure and not referable to any other pleaded cause of action.

[40] Practically speaking, notional subrule 25.07(7) divides the defendants into three classes.

[41] First, there are those defendants who deliver a s. 138.8(2) affidavit under the Securities Act. These defendants must deliver a statement of defence for the reasons expressed below.

[42] Second, there are those defendants against whom there are no allegations of fact referable to liability for secondary market disclosure, who thus have no right or need to deliver a s. 138.8(2) affidavit under the Securities Act and who choose to deliver a [page183] statement of defence. These plaintiffs may, if so advised, simply plead in the normal course.

[43] Third, there are those defendants against whom there are allegations of fact referable to liability for secondary market disclosure and who do not deliver a s. 138.8(2) affidavit but who deliver a statement of defence.

[44] Under notional rule 25.07(7), these defendants shall decline to either admit or deny the allegations of fact referable solely to his or her liability for secondary market liability and not referable to any other pleaded cause of action. These defendants must state that they neither admit nor deny the allegations contained in those paragraphs (identify paragraph numbers) of the statement of claim referable solely to liability for secondary market liability and not referable to any other pleaded cause of action. As will become clearer after the discussion below, by being required to neither admit nor deny allegations referable solely to secondary market liability, these defendants cannot circumvent the requirements of s. 138.8(2) of the Securities Act that they must file an affidavit in order to set forth the material facts upon which they intend to rely for the leave motion.

[45] This brings the discussion and the analysis to whether there might be other reasons not to order the defendants to deliver a statement of defence. The convention in class actions, which existed from 1996 to 2011, was that a defendant not be required to deliver a statement of defence pre-certification because of the likelihood that the statement of claim would be reformulated as a result of the certification decision and based on the view that the statement of defence had little utility before certification. See Mangan v. Inco Ltd. (1996), 30 O.R. (3d) 90, [1996] O.J. No. 2655 (Gen. Div.), at pp. 94-95 O.R.; Glover v. Toronto (City), [2008] O.J. No. 604 (S.C.J.), at para. 8.

[46] In Pennyfeather, I suggested that the convention should be revisited and that it was desirable that the pleadings be closed before the certification motion. See, also, Kang v. Sun Life Assurance Co. of Canada, [2011] O.J. No. 4792, 2011 ONSC 6335.

[47] In Pennyfeather, at paras. 37-38, 84-92, I stated:

> Class actions are subject to the Rules of Civil Procedure, and there is nothing in the Class Proceedings Act, 1992 that precludes defendants from pleading before the certification motion. It is informative that the convention of not closing the pleadings is not a statutory rule, and if the plaintiff insists on the delivery of a pleading, a defendant may need to seek the permission of the court to delay the delivery of the pleading.
>
> Moreover, the provisions of the Class Proceedings Act, 1992 indicate that it was the Legislature's intention that the general rule is that the statement of defence should be delivered before the certification motion. Section 2(3) of [page184] the Act indicates that the timing of the certification motion is measured by the delivery of the statement of defence[.]
>
> . . . . .
>
> . . . it would be advantageous for the immediate case and for other cases, if the current convention ended and defendants were required in the normal course to deliver a statement of defence before the certification motion. As I will illustrate, there would be several advantages to this approach, and as I mentioned above, the Legislature intended that the general rule should be that the pleadings should be completed before the certification motion.
>
> Before I provide some examples of the advantages of closing the pleadings before certification, it is helpful to recall that under s. 5(1) of the Class Proceedings Act, 1992, a plaintiff must satisfy five interdependent criteria for his or her action or application to be certified as a class proceeding. The Plaintiff must: (1) show a cause of action; (2) identify a class; (3) define common issues; (4) show that a class proceeding would be the preferable procedure; and (5) qualify as a representative plaintiff with a litigation plan and adequate Class Counsel.
>
> A major advantage of closing the pleadings is that controversies about the first of the five criteria for certification might be resolved or at least narrowed or confined before the certification motion.
>
> The delivery of a statement of defence could be a fresh step that could foreclose any subsequent attack by the defendant for any pleadings irregularities and, more to the point, typically defendants do not deliver a statement of defence if there is a substantive challenge to the statement of claim. Rather, they bundle all their challenges to the statement of claim and bring a motion to have the statement of claim or portions of it struck out on both technical and substantive grounds[.]
>
> In other words, the requirement of delivering a statement of defence will call out the defendant to make its challenges to the statement of claim and, thus, the s. 5(1)(a) criterion might be removed as an issue as would any challenge to the pleading for wanting in particulars or for breaching the technical rules for pleading. The s. 5(1)(a) criterion for certification might be decided before the certification motion.
>
> If the defendant brings a comprehensive pleadings challenge before the certification motion, then, the s. 5(1)(a) criterion would be resolved before the certification hearing one

> way or the other. It would be particularly useful to resolve a s. 5(1)(a) challenge before the certification motion when the challenge is based on the court not having subject-matter jurisdiction over the plaintiff's claim. If that challenge is upheld, then the class action would be dismissed or stayed and the enormous costs of a comprehensive certification motion is avoided.
>
> Further, hearing an interlocutory motion about the sufficiency of the pleading might be preferable to having the challenge heard at the certification motion as an aspect of the s. 5 (1)(a) analysis because a common outcome of this analysis is to grant the plaintiff leave to amend his or her statement of claim, which outcome, at a minimum, exacerbates the complexities of determining the certification motion because of the interdependency of the certification criteria. [page185]
>
> In many cases, the technical or substantive adequacy of a plaintiff's statement of claim is not an issue and, therefore, requiring the completion of the pleadings will involve no interlocutory steps and the analysis of the other four certification criteria would be facilitated by a completed set of pleadings.
>
> For instance, having the statement of defence before the certification motion would provide useful information for analyzing the preferable procedure criterion and the plaintiff's litigation plan. Moreover, it may emerge that there are issues worthy of certification in the defendant's statement of defence.

[48] For present purposes, I do not retreat from what I said in Pennyfeather, and I shall emphasize several points and add a few more. In this regard, I emphasize that it was the clear intention of the legislature that the pleadings be closed before certification. I add that this makes sense because the certification criteria of class definition, common issues, preferable procedure and litigation plan are best adjudicated in the context of the parameters of the action and it may emerge that the defendant has pleaded issues that may usefully be added to the list of common issues.

[49] Further, I add that the legislature also indicated by s. 35 of the Class Proceedings Act, 1992 that the Rules of Civil Procedure apply to class proceedings, reserving the courts' authority to make adjustments to that procedure under s. 12 of the Act. Generally speaking, it is desirable to normalize class actions with the procedure under the Rules of Civil Procedure. The Rules are the norm for a fair procedure, and the norm of civil procedure is that both sides must disclose the case that their opponent must meet. Defendants are not like an accused in a criminal proceeding with a right to remain silent. It is not regarded as unfair or abnormal to compel a defendant to plead a statement of defence in response to a statement of claim.

[50] Further still, I add that having a complete set of pleadings recognizes the maturity of the class action jurisprudence. There already have been many Rule 21 and s. 5(1) (a) challenges, and the viability of many causes of action or types of claim as being suitable for class actions has been informed by 20 years of cases. Recognition of the maturity of the case law in and of itself calls for a rethinking of the convention of not delivering a statement of defence, because assisted by precedents of what has been certified in the past, plaintiffs are better able to exit the certification hearing with their pleadings intact.

[51] In other words, in contemporary times the defendants' concern that they will have wasted time and effort pleading to a statement of claim that may be different after certification will not be borne out. In any event, the complaint of a wasted effort [page186] is overblown. Unless pleadings are to be regarded as a work of fictional literature, claims and defences are based on the material facts that existed, and competent counsel will take instructions about all the possible claims and defences that

emerge from those set of facts before the certification motion.

[52] I find it hard to believe that the accomplished lawyers in the case at bar are waiting for the outcome of the leave motion and the certification motion before investigating the material facts and researching the applicable law and advising the defendants about what defences are available to them. The truth of the matter is that the defendants and their lawyers are not concerned about wasted time and effort, but rather they do not wish to plead because they believe it is tactically better to avoid the disclosure of their case that the Rules of Civil Procedure would normally mandate.

[53] I see no unfairness of denying defendants a tactical maneuver that may be inconsistent with general principle of rule 1.04 that the rules "shall be liberally construed to secure the just, most expeditious and least expensive determination of every civil proceeding on its merits".

[54] I also see no unfairness in denying defendants the tactical maneuver of not delivering a statement of defence before certification when the exchange of pleadings may be tactically and substantively beneficial to defendants. The defendants arguments that class membership is overinclusive or under-inclusive, that the proposed common issues want for commonality, that the action is not manageable as a class action, that a class proceeding is not the preferable procedure, and that the litigation plan is deficient are best made when the defendants shows the colour of his or her eyes by pleading a defence and these arguments will be stronger than the "is! -- is not! -- is too!" sandbox arguments of many a certification motion. For whatever it is worth, my own observation from recent certification motions where defendants have pleaded before certification is that both sides and the administration of justice are better for it.

[55] Finally, from a public relations point of view -- and class actions are by their nature of considerable interest to the public -- I would have thought that many defendants would like to seize the opportunity by pleading the material facts of their defence to take the sting out of the plaintiff's argument that the defendants need behaviour management and to level the playing field about the certification criteria.

[56] Thus, generally speaking, I persist in my view that the pleadings issues should be completed before the certification [page187] motion. The defendants' argue, however, that whatever may be the situation for class actions generally, the Court of Appeal's decision in Sharma v. Timminco, supra, has overtaken Pennyfeather, and Sharma means that in a proposed secondary-market class action, a statement of defence cannot be demanded or delivered before leave is granted under s. 138.3 of the Securities Act. A defendant cannot be asked to plead to a pregnant statement of claim.

[57] The defendants take the Sharma decision to be authority that a class proceeding is not an action commenced under s. 138.3 until leave is granted and leave is required to add the s. 138.3 cause of action to the class proceeding. The defendants submit that without leave, a s. 138.3 action cannot be enforced. As Sino-Forest put it in its factum: "Until leave has been granted, the plaintiff has nothing: no limitation periods are tolled, and no steps in the proceeding -- including the filing of a defence -- can be taken."

[58] This hyperbolic submission by Sino-Forest and by the rest of the defendants is not true. Whatever the effect of Sharma, it did not take away s. 138.8 of the Securities Act, under which subsection (2) requires for the leave motion that the plaintiff and each defendant swear under oath the "material facts upon which each intends to rely".

[59] Section 138.8 of the Securities Act, which provides the test for leave and which governs the procedure for the leave motion, states:

Leave to proceed

> 138.8(1) No action may be commenced under section 138.3 without leave of the court granted upon motion with notice to each defendant. The court shall grant leave only where it is satisfied that,
>
> (a) the action is being brought in good faith; and
>
> (b) there is a reasonable possibility that the action will be resolved at trial in favour of the plaintiff.
>
> Same
>
> (2) Upon an application under this section, the plaintiff and each defendant shall serve and file one or more affidavits setting forth the material facts upon which each intends to rely.
>
> Same
>
> (3) The maker of such an affidavit may be examined on it in accordance with the rules of court.

[60] Subsection 138.8(2) may be usefully compared and contrasted with rule 25.06(1) of the Rules of Civil Procedure, [page188] which is the predominant rule about pleading in an action. Rule 25.06(1) states:

> 25.06(1) Every pleading shall contain a concise statement of the material facts on which the party relies for the claim or defence, but not the evidence by which those facts are to be proved.

Both the subsection and the rule require the party to disclose to their opponent the "material facts" on which the party "relies". The pleadings rule, however, does not require that the disclosure of material facts be under oath. Assuming that a defendant does file an affidavit under s. 138.8(2), then the affidavit is, in effect, an under-oath version of 25.06(1)'s requirement that a defendant disclose the material facts upon which he or she relies.

[61] I concede that filing an affidavit under s. 138(8) is not mandatory and that it cannot be assumed that a defendant will deliver an affidavit for a leave motion under the Securities Act, and that he or she cannot be compelled to do so. In Ainslie v. CV Technologies Inc. (2008), 93 O.R. (3d) 200, [2008] O.J. No. 4891 (S.C.J.), at paras. 14-20, 24-25, Justice Lax interpreted s. 138.8(2), and she stated:

> Section 138.8(1) sets out a two-part test for obtaining leave to bring an action under Part XXIII.1 of the OSA and places the onus on the plaintiffs to demonstrate that (1) their proposed action is brought in good faith and (2) has a reasonable prospect for success at trial. As s. 138.8(1) requires an examination of the merits, the plaintiffs submit that the section is supplemented with s. 138.8(2) and (3). They rely on the mandatory language in s. 138.8(2) ("and each defendant shall") and submit that without the benefit of this requirement and the ability to cross-examine, a plaintiff would be deprived of the tools necessary to meet the standard the legislature created in s. 138.8(1).
>
> This submission ignores the legislative purpose of s. 138.8. The section was not enacted to benefit plaintiffs or to level the playing field for them in prosecuting an action under Part

XXIII.1 of the Act. Rather, it was enacted to protect defendants from coercive litigation and to reduce their exposure to costly proceedings. No onus is placed upon proposed defendants by s. 138.8. Nor are they required to assist plaintiffs in securing evidence upon which to base an action under Part XXIII.1. The essence of the leave motion is that putative plaintiffs are required to demonstrate the propriety of their proposed secondary market liability claim before a defendant is required to respond. Subsection 138.8(2) must be interpreted to reflect this underlying policy rationale and the legislature's intention in imposing a "gatekeeper mechanism".

The plaintiffs appear to be interpreting s. 138.8(2) as if it read: "Upon an application under this section, the plaintiff and each defendant shall serve and file one or more affidavits." But, the subsection continues: "setting forth the material facts upon which each intends to rely". If there are no material facts upon which a defendant intends to rely in responding to a leave motion, how can it be that a defendant is required to file an affidavit? Similarly, if a defendant files one or more affidavits, how can a plaintiff require [page189] that defendant to file other affidavits? By discounting this language, the plaintiffs are proposing an interpretation which relieves them of their obligation to demonstrate that their proposed action meets the pre-conditions for granting leave under the Act.

The plaintiffs' interpretation also fails to address the language used in subsections (3) and (4). Section 138.8(3) reads: "The maker of such an affidavit may be examined on it in accordance with the rules of court." Section 138.8(4) reads: "A copy of the application for leave to proceed and any affidavits filed with the court shall be sent to the Commission when filed". Had it been the intention of the Legislature to require the parties to file affidavits, irrespective of the onus placed upon the moving party, the legislature would have substituted the word "the" for "any" in s. 138.8(4) and the words "the plaintiff and each defendant" for "maker" in s. 138.8(3). I also note that the legislature attached no consequences to the failure of "each defendant" to file an affidavit.

In terms of onus, a useful analogy can be found in the summary judgment rule, Rule 20, of the Rules of Civil Procedure. Rule 20.04 provides:

> 20.04(1) In response to affidavit material or other evidence supporting a motion for summary judgment, a responding party may not rest on the mere allegations or denials of the party's pleadings but must set out, in affidavit material or other evidence, specific facts showing that there is a genuine issue for trial.

Similar to s. 138.8(2), rule 20.04 utilizes language suggesting that a responding party "must" or "shall" file affidavit material. Notwithstanding the use of such language, under Rule 20, a responding party retains the option to counter the motion by simply cross-examining the moving party, rather than by leading any direct evidence on the motion. In this regard, Rule 20.04 has been interpreted as requiring the respondent to a summary judgment motion to "lead trump or risk losing". Notably, however, the onus to establish that there is no genuine issue for trial remains with the moving party. The onus does not shift to the respondent to show that a genuine issue for trial does in fact exist.

Similarly, in a motion under s. 138.8 of the Act, the onus to demonstrate that the proposed claim meets the required threshold remains with the plaintiffs. The onus does not shift to the defendants. A defendant that does not "lead trump" by filing affidavit evidence in response to a motion under s. 138.8 may well take the risk that leave will be granted to the plaintiffs. It does not follow, however, that a defendant is obligated to file evidence or

> produce an affidavit from each named defendant. It is a well-established principle that, as a general proposition, it is counsel who decides on the witnesses whose evidence will be put forward.
>
> . . . . .
>
> In my view, the "gatekeeper provision" was intended to set a bar. That bar would be considerably lowered if the plaintiffs' view is correct. As I have already indicated, a defendant who does not file affidavit material accepts the risk that it may be impairing its ability to successfully defeat the motion for leave and is probably foregoing the right to assert the statutory defences under Part XXIII.1 of the Act. However, parties are entitled to present their case as they see fit and this includes the right to oppose the leave motion on the basis of the record put forward by the plaintiffs as GT intends, or on the basis of the affidavits of experts as CV intends. [page190]
>
> To accept the plaintiffs' submissions would require each defendant to produce evidence that may not be necessary for the leave motion and would serve no purpose other than to expose those defendants to a time-consuming and costly discovery process. It would sanction "fishing expeditions" prior to the plaintiffs obtaining leave to proceed with their proposed action. This is an unreasonable interpretation of s. 138.8(2). It is inconsistent with the scheme and object of the Act. Properly interpreted, the ordinary meaning of s. 138.8(2) is that a proposed defendant must file an affidavit only where it intends to lead evidence of material facts in response to the motion for leave.

[Emphasis in original]

[62] In Ainslie, leave to appeal was granted ([2009] O.J. No. 730 (Div. Ct.)), but it appears that the appeal was never argued. In Sharma v. Timminco Ltd., [2010] O.J. No. 469, 2010 ONSC 790, at para. 32, I agreed with Justice Lax's interpretation of s. 138.8(2).

[63] In the case at bar, I do not know whether any of the defendants will deliver affidavits under s. 138.8(2), but I do know that if a defendant does deliver an affidavit, then its protest that it would be unfair to require a statement of defence loses its potency as does the urgency of the plaintiffs' request that the defendants be ordered to deliver their statements of defence. Delivering an affidavit under s. 138.8 is essentially the same as delivering a statement of claim or defence. As Justice Lax notes, a defendant who does not file affidavit material accepts the risk that it may be impairing its ability to successfully defeat the motion for leave. Justice Lax also notes that the defendant is probably foregoing the right to assert the statutory defences under Part XXIII.1 of the Act, but I would not necessarily go that far.

[64] Where this analysis takes me is that it while it would be inappropriate to order all the defendants to deliver a statement of defence to a secondary market claim under the Securities Act, it would be proper to order that any defendant who delivers an affidavit pursuant to s. 138.8(2) of the Act shall also deliver a statement of defence. I so order.

[65] Although I am ordering only defendants who deliver s. 138.8(2) affidavits to deliver a statement of defence, I order that any other defendant may, if so advised, deliver a statement of defence. I leave them to make the tactical decision whether or not to deliver a pleading. As I discussed above, there are advantages for a defendant to plead in a class action.

[66] For reasons that I will come to next, if a defendant does deliver a statement of defence, the delivery is without prejudice to the defendant's right to bring a Rule 21 motion or to challenge whether

the plaintiffs have shown a cause of action as required by s. 5(1)(a) of the Class Proceedings Act, 1992. [page191]

[67] Here, it should be noted that the "plain and obvious" test for disclosing a cause of action from Hunt v. Carey Canada Inc., [1990] 2 S.C.R. 959, [1990] S.C.J. No. 93, which is used for a Rule 21 motion, is used to determine whether the proposed class proceedings discloses a cause of action; thus, a claim will be satisfactory under s. 5(1)(a) unless it has a radical defect or it is plain and obvious that it could not succeed: Anderson v. Wilson (1999), 44 O.R. (3d) 673, [1999] O.J. No. 2494 (C.A.), at p. 679 O.R., leave to appeal to S.C.C. refused [1999] S.C.C.A. No. 476; 1176560 Ontario Ltd. v. Great Atlantic & Pacific Co. of Canada Ltd. (2002), 62 O.R. (3d) 535, [2002] O.J. No. 4781 (S.C.J.), at para. 19, leave to appeal granted (2003), 64 O.R. (3d) 42, [2003] O.J. No. 1089 (S.C.J.), affd (2004), 70 O.R. (3d) 182, [2004] O.J. No. 856 (Div. Ct.); Healey v. Lakeridge Health Corp., [2006] O.J. No. 4277, 38 C.P.C. (6th) 145 (S.C.J.), at para. 25.

[68] In this last regard, the defendants submitted that a defendant has a right to challenge whether the plaintiff has pleaded a reasonable cause of action by bringing a Rule 21 motion and a defendant would lose this procedural right if he or she delivered a statement of defence. Pleading over is a fresh step that deprives a defendant of the right to subsequently challenge the substantive adequacy of a pleading: Bell v. Booth Centennial Healthcare Linen Services, [2006] O.J. No. 4646, 153 A.C.W.S. (3d) 828 (S.C.J.), at paras. 5-7; Cetinalp v. Casino, [2009] O.J. No. 5015 (S.C.J.). From this true premise, the defendants submit that since some or all of them wish to bring a Rule 21 motion or some or all will be challenging the reasonableness of the plaintiffs' statement of claim as an aspect of the s. 5(1)(a) criterion of the of test for certification, they should not be required to deliver a statement of defence before the certification motion.

[69] The court's typical but not inevitable response to a defendant's request to bring a Rule 21 motion before certification is to direct the motion to be heard at the certification hearing because the test for granting a Rule 21 motion is the same test that is applied for the s. 5(1)(a) criterion for certification. Typically, when this direction is made the defendant is not required to deliver a statement of defence.

[70] As already noted, in the case at bar, several defendants have indicated that they wish to bring Rule 21 motions on the basis that several of the plaintiffs' claims do not disclose a reasonable cause of action or on the basis that the bonds contain a "no suits" clause, and BDO Limited wishes to bring a Rule 21 motion based on the argument that it is plain and obvious that claims against it are statute-barred. [page192]

[71] I agree that the right of defendants to challenge the reasonableness of the plaintiffs' statement of claim should be preserved and protected, and I also believe that this objective can be accomplished while still permitting defendants to deliver a statement of defence.

[72] Once again, using the authority of s. 12 of the Class Proceedings Act, 1992, I order that if a defendant delivers a statement of defence, then the delivery of the statement of defence is not a fresh step and the defendant is not precluded from bringing a Rule 21 motion at the leave and certification motion or the defendant is not precluded from disputing that the plaintiffs have shown a cause of action under s. 5(1)(a) of the Class Proceedings Act, 1992.

3. Leave and certification

[73] The above discussion addresses the matter of the plaintiffs' request that the defendants be ordered to deliver statements of defence and the discussion also lays the foundation for the discussion of the plaintiffs' request that the leave motion under s. 138.8 [of] the Securities Act and the certification motion under the Class Proceedings Act, 1992 be heard together and the defendants' counter-submission

that the motions should be sequenced leave motion, Rule 21 motion and certification motion.

[74] In the case at bar, there is a general consensus that the leave motion should go first and, in any event, because of the Court of Appeal's ruling in Sharma that s. 28 of the Class Proceedings Act, 1992 is useless in protecting claims under Part XXIII.1 of the Securities Act from limitation periods, the leave motion must go first, and I have scheduled ten days of hearing commencing November 21, 2012.

[75] The question then is whether the certification motion should be combined with the leave motion.

[76] The plaintiffs submit that hearing the two matters together is consistent with the direction from the Ontario Court of Appeal and [the] Supreme Court of Canada that litigation by installments should be avoided wherever possible because "it does little service to the parties or to the efficient administration of justice." Garland v. Consumers' Gas Co. (2001), 57 O.R. (3d) 127, [2001] O.J. No. 4651 (C.A.), at para. 76, revd [2004] 1 S.C.R. 629, [2004] S.C.J. No. 21, at para. 90. The plaintiffs note that leave and certification were dealt with together in Silver v. Imax Corp., [2009] O.J. No. 5585, 86 C.P.C. (6th) 273 (S.C.J.), leave to appeal refused (2011), 105 O.R. (3d) 212, [2011] O.J. No. 656 (Div. Ct.) [page193] and in Dobbie v. Arctic Glacier Income Fund, [2011] O.J. No. 932, 2011 ONSC 25.

[77] An admonition is different from a prohibition, and while the Court of Appeal and the Supreme Court may frown on litigation in installments, they did not prohibit it. Whether to permit motions before the certification motion is a matter of discretion. In exercising its discretion whether to permit a motion before the certification motion, relevant factors include (a) whether the motion will dispose of the entire proceeding or will substantially narrow the issues to be determined; (b) the likelihood of delays and costs associated with the motion; (c) whether the outcome of the motion will promote settlement; (d) whether the motion could give rise to interlocutory appeals and delays that would affect certification; (e) the interests of economy and judicial efficiency; and (f) generally, whether scheduling the motion in advance of certification would promote the fair and efficient determination of the proceeding: Cannon v. Funds for Canada Foundation, [2010] O.J. No. 314, 2010 ONSC 146, at paras. 14-15.

[78] Thus, in my opinion, the question to be decided in the immediate case is whether it is fair (the most important factor) and efficient to hear the certification motion and the leave motion together.

[79] Provided that any defendants who deliver s. 138.8(2) affidavits or any defendants who deliver statements of defence may bring Rule 21 motions or otherwise challenge all of the certification criteria as they may be advised, I see no unfairness in having the certification motion heard along with the leave motion. Because of the orders that I shall make, already discussed above, a defendant may challenge all of the certification criteria regardless of whether the defendant has pleaded or not. Pursuant to notional rule 25.07(7), defendants who do not file a s. 138.8(2) affidavit and who deliver a statement of defence "shall decline to admit or deny the allegations referable solely to liability for secondary market disclosure and not referable to any other pleaded cause of action". I see no unfairness to the defendants who may resist both the certification motion and the leave motion as they may be advised.

[80] In contrast, the sequential approach being advocated by the defendants is unfair to the plaintiffs and to the proposed class and will impede fulfilling the purposes of the class proceedings legislation, which are, first and foremost, access to justice, secondarily, judicial economy and thirdly, behaviour modification, all the while providing due process and fairness to all parties. Unfortunately, the suffocating expense of motions in class actions [page194] along with the excruciating delays and the additional costs of the inevitable leave to appeal motions and appeals that follow class action orders is a serious barrier to achieving the purposes of the legislation for both plaintiffs and defendants and a substantial disincentive to class counsel employing the legislation for other than the huge cases that would justify the litigation risks.

[81] As night follows day, if I agreed to schedule sequentially, there would be a ten-day leave motion, followed by the unsuccessful party launching the appeal process which will take several years to resolve. Whatever the outcome of the appeal, the action will return to the Superior Court for the certification motion of the claims not referable solely to liability for secondary market disclosure.

[82] In the case at bar, if Rule 21 motions were permitted before the certification hearing although work that could be done at the certification hearing will be accomplished, this will come at the cost of another round of appeals that will take several years to resolve only for the action to return again to the Superior Court for the determination of whether the balance of the certification criteria have been satisfied. That determination will also be appealed.

[83] In contrast, if I combine the leave motion, the Rule 21 motions and the certification motion into one hearing, as night follows day, the determination will be appealed but the superior court and the appellate courts, including the Supreme Court of Canada, will be denied the pleasure of three visits from one or two generations of class and defence counsel.

[84] The defendants argue that there will be no efficiencies in a sequential ordering of the motions because the criteria for leave differs from the certification criteria, as does the burden of proof for these motions. However, courts are obliged to have the perspicacity to be able to deal with different criteria and different onuses of proof but, more to the point, the evidentiary footprint for the leave and certification motions are the same, and it makes for little efficiency for the parties and little judicial economy to have the evidence and argument for leave and for certification heard more than once.

[85] Putting aside the somewhat unique circumstances of BDO Limited, I conclude that the certification hearing should be combined with the leave motion and that with the exception of the plaintiffs' funding motion, which has already been scheduled, there shall be no other motions before the leave and certification motion without leave of the court first being obtained. [page195]

4. BDO Limited's request for a Rule 21 motion

[86] As noted at the outset of these reasons, I am adjourning the motion as it concerns BDO Limited, whose circumstances may be unique.

[87] BDO was a party to the Smith v. Sino-Forest and the Northwest v. Sino-Forest rival class actions and it was added to the case at bar after the carriage motion. It submits that all of the statutory claims against it are statute-barred as in one of the main common law misrepresentation claims. It submits that it can diminish its involvement in this expensive litigation by a Rule 21 motion based on the pleadings and without evidence.

[88] The plaintiffs' response was that if BDO wished to assert a limitation period defence it should be a pleaded defence to which the plaintiffs would file a reply demonstrating that it was not plain and obvious that the claims were statute-barred or demonstrating that there were defences to the running of the limitation period, presumably based on fraudulent concealment or estoppel or waiver. The plaintiffs also asserted that there were other common claims against BDO that were not statute-barred and thus there was no utility in permitting a Rule 21 motion that would see BDO only partially out of the action.

[89] BDO's response was that there were no defences that could withstand the ultimate limitation periods of the Securities Act and fairness dictated that it should be permitted to substantially reduce being embroiled in this litigation.

[90] My own assessment was that the plaintiffs were correct in submitting that in the circumstances

of this case, BDO should plead its limitation defence and the plaintiffs should have an opportunity to deliver a reply.

[91] Once BDO has pleaded, I will be in a better position in determining whether to permit a Rule 21 motion or perhaps a Rule 20 partial summary judgment motion.

[92] Accordingly, I am adjourning the motion as it concerns BDO Limited to be brought on again, if at all, after BDO has pleaded its statement of defence and the plaintiffs their reply.

5. The timetable

[93] In light of the discussion above, it is ordered that subject to adjustments, if necessary, made at a case conference, the timetable for the plaintiff's funding approval motion and for the leave and certification motion is as follows:

Funding Approval Motion

March 9, 2012: plaintiffs to deliver motion record (completed)

March 30, 2012: defendants to deliver responding records, if any [page196]

April 6, 2012: plaintiffs to deliver factum

April 13, 2012: defendants to delivery factum

April, 17, 2012: Hearing of the motion

Leave and Certification Motion

April 10, 2012: plaintiffs to deliver motion record

June 11, 2012: defendants to deliver responding records

July 3, 2012: plaintiffs to delivery reply records, if any

September 14, 2012: Cross-examinations to be completed

October 19, 2012: plaintiffs to deliver factum

November 9, 2012: defendants to deliver factum

November 21-30, 2012: Hearing of the motion

D. Conclusion

[94] An order shall issue in accordance with these reasons with costs in the cause.

Motion granted in part.

SINO-FOREST CORPORATION
Applicant

-and-

ERNST & YOUNG LLP
Respondent

Court File No. CV-12-9667-00-CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

PROCEEDING COMMENCED AT TORONTO

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