Court of Appeal File Numbers: C56118 / C56115 / C56125
Superior Court File No. CV-12-9667-00CL

**COURT OF APPEAL FOR ONTARIO**

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

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# BRIEF OF AUTHORITIES OF THE RESPONDENT, SINO-FOREST CORPORATION

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**BENNETT JONES LLP**
One First Canadian Place
Suite 3400, P.O. Box 130
Toronto, Ontario
M5X 1A4

**Robert Staley** (LSUC #27115J)
**Kevin Zych** (LSUC #33129T)
**Derek J. Bell** (LSUC #43420J)
**Raj Sahni** (LSUC #42942U)
**Jonathan Bell** (LSUC #55457P)

Tel: 416-863-1200
Fax: 416-863-1716

Lawyers for Sino-Forest Corporation

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*Case Name:*

# Nolan v. Ontario (Superintendent of Financial Services)

**Between**
**Kerry (Canada) Inc., Appellant/Respondent by way of cross-appeal, and**
**Elaine Nolan, George Phillips, Elisabeth Ruccia, Kenneth R. Fuller, Paul Carter, R.A. Varney and Bill Fitz, being members of the DCA Employees Pension Committee representing certain of the members of the Pension Plan for the Employees of Kerry (Canada) Inc., Respondents/Appellants by way of cross-appeal, and**
**Superintendent of Financial Services, Respondent/Respondent by way of cross-appeal**

[2007] O.J. No. 2176

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2007 CarswellOnt 3493

Docket: C45720

Ontario Court of Appeal
Toronto, Ontario

**J.I. Laskin, E.E. Gillese and P.S. Rouleau JJ.A.**

Heard: January 10 and 11, 2007.
Judgment: June 5, 2007.

(198 paras.)

*Pensions and benefits law -- Pensions -- Administration of pensions -- Administration costs -- Appeals and judicial review of decisions -- Appeal by employer from successful appeals by its former employees and beneficiaries under its pension plan from two decisions of the Financial Services Tribunal allowed, judgment set aside, and decisions of Tribunal restored -- Pension plan amended to allow employer to pay plan expenses from pension fund and to take contribution holidays in respect of its funding obligations -- Standard of review of Tribunal's decisions was reasonableness -- In applying correctness standard, the Divisional Court erred -- Tribunal's decision with respect to contribution holidays was reasonable and was to stand -- Tribunal's decision to refuse to order Superintendent to refuse registration of the plan amendment was reasonable and was not to be disturbed.*

*Administrative law -- Judicial review and statutory appeal -- Standard of review -- Correctness -- Reasonableness -- Appeal by employer from successful appeals by its former employees and beneficiaries under its pension plan from two decisions of the Financial Services Tribunal allowed, judgment set aside, and decisions of Tribunal restored -- Pension plan amended to allow employer to pay plan expenses from pension fund and to take contribution holidays in respect of its funding obligations -- Standard of review of Tribunal's decisions was reasonableness -- In applying correctness standard, the Divisional Court erred -- Tribunal's decision with respect to contribution holidays was reasonable and was to stand -- Tribunal's decision to refuse to order Superintendent to refuse registration of the plan amendment was reasonable and was not to be disturbed.*

Appeal by Kerry (Canada) Inc. from successful appeals by its former employees and beneficiaries under its pension plan from two decisions of the Financial Services Tribunal. The plan was amended in 1975, 1987 and 2000 to give Kerry the power to pay plan expenses from the pension fund. In 2000, the plan was amended in order to introduce a defined contribution component. Existing plan members were given the option of remaining in the defined benefit component of the plan or converting to the defined contribution component. All new employees were required to participate in the defined contribution component of the plan. Starting in 1985, Kerry took contribution holidays in respect of its funding obligations. By 2001, it had taken contribution holidays of approximately $1.5 million. From the plan's inception through to the end of 1984, the employer paid all plan expenses. Beginning in 1985, however, third party plan expenses were paid from the fund. Money from the fund was used to pay for approximately $850,000 of Plan expenses from 1985 to 2002. After the 2000 Plan amendments were introduced, the Committee asked the Superintendent of Financial Services to investigate alleged irregularities in the administration of the plan, including the payment of plan expenses from the fund and Kerry's contribution holidays. After investigation, the Superintendent issued a Notice of Proposal to make an order requiring Kerry to reimburse the fund for expenses paid from the fund after January 1, 1985, that were not incurred for the exclusive benefit of Plan members. The Superintendent also issued a second Notice of Proposal in which he proposed to refuse to order Kerry to pay the amounts to the fund that had been taken by way of contri-

bution holidays. Kerry sought a hearing before the Financial Services Tribunal on the Superintendent's proposed order in respect of plan expenses. The Committee sought a hearing on the Superintendent's proposed order in respect of contribution holidays. The Superintendent was a party to both hearings. The Tribunal held that all but a very few plan expenses could be paid from the pension fund and that Kerry was entitled to take contribution holidays. The Committee appealed both decisions to the Divisional Court, which largely overturned the Tribunal decisions. The Divisional Court also made a costs award requiring Kerry to pay the Committee's costs, on a partial indemnity basis, of the second Tribunal hearing and the appeals to the Divisional Court. That award also required Kerry, as administrator of the Plan, to cause the Fund to pay the balance of the Committee's costs of the appeals to the Divisional Court. Kerry appealed the judgment of the Divisional Court and the Committee cross-appealed. At issue was whether Plan expenses were properly paid from the Fund or was Kerry required to reimburse the Fund for them; could surplus pension funds be used to satisfy Kerry's contribution obligations in respect of the defined contribution component of the Plan; and, did Kerry give proper notice to Plan members of the conversion option? If the notice was not sufficient, was Kerry required to issue a new notice and was the Superintendent required to refuse to register the 2000 Plan; and, did the Divisional Court err in its costs award? The cross-appeal issues included whether Kerry was required to remit contributions in respect of the defined benefit component of the Plan, and did the Tribunal have the power to order costs payable from a pension fund?

HELD: Appeal allowed and cross-appeal dismissed. The judgment of the Divisional Court in respect of Plan expenses, contribution holidays and costs were set aside, and decisions of the Tribunal were restored. The standard of review of the Tribunal's decisions was reasonableness. In applying a correctness standard, the Divisional Court erred. A review of the Tribunal's decision on a reasonableness standard led to the conclusion that there was no basis for interference with that decision. The Tribunal considered the trust agreement and plan text separately, recognizing the differences between those documents. It focused on the relevant provisions in both and construed those provisions reasonably. Accordingly, the Tribunal's decision was reasonable and was to be restored. The Divisional Court erred in determining that to permit Kerry to pay the plan expenses from the fund amounted to a revocation of trust. Payment of expenses to a third party did not fall within the definition of revocation as no money was returned to the company. The Tribunal's decision with respect to contribution holidays was reasonable and was to stand. The Tribunal approached the matter with caution and was clearly alive to the potential for misuse of surplus funds. The Tribunal's reasons made it clear why it was satisfied that no misuse occurred. The Divisional Court and the Tribunal correctly concluded that Kerry was entitled to take contribution holidays, as its defined benefit pension plan enjoyed an actuarial surplus, and the plan documentation did not explicitly provide that it was not entitled to do so. Kerry, as administrator of the pension plan, had a statutory obligation pursuant to s. 26(1) of the Pension Benefits Act to give notice of the plan amendment that created the conversion option. However, the notice related only to the conversion option, which was a single, discrete aspect of but one of the many amendments made in 2000. Accordingly, the Tribunal's determination that the inadequacies in the notice did not cause the amended plan text to cease to comply with the Act was reasonable. The Tribunal's decision to refuse to order the Superintendent to refuse registration of the amendment or the 2000 Plan was reasonable and was not to be disturbed. There was nothing in the Tribunal's costs decision that warranted interference by the Divisional Court.

**Statutes, Regulations and Rules Cited:**

Courts of Justice Act, R.S.O. 1990, c. C.43, s. 134(1)

Financial Services Commission of Ontario Act, 1997, S.O. 1997, c. 28, s. 24, s. 24(1)

Pension Benefits Act, R.S.O. 1990, c. P.8, s. 6, s. 9, s. 10, s. 12, s. 18, s. 18(1), s. 18(1)(d), s. 22, s. 22(1), s. 26, s. 26(1), s. 26(2), s. 26(4), s. 70(6), s. 87, s. 91, s. 91(1)

Pension Benefits Regulations, R.R.O. 1990, Reg. 909, s. 9

Statutory Powers Procedure Act, R.S.O. 1990, c. S.22, s. 17.1, s. 17.1(6)

Trustee Act, R.S.O. 1990, c. T.23, s. 13(1), s. 23.1

**Appeal From:**

On appeal from the judgment dated March 15, 2006, with reasons reported at (2006), 209 O.A.C. 21, and order dated May 31, 2006, with reasons reported at (2006), 213 O.A.C. 271, of the Divisional Court (Justice John G.J. O'Driscoll, Justice Peter G. Jarvis and Justice Anne M. Molloy).

**Counsel:**

Ronald J. Walker and Christine P. Tabbert for the appellant/respondent by way of cross-appeal.

Ari N. Kaplan and Clio Godkewitsch for the respondents/appellants by way of cross-appeal.

Deborah McPhail and Mark Bailey for the respondent/respondent by way.

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The judgment of the Court was delivered by

**1** E.E. GILLESE J.A.:-- The Supreme Court of Canada has heard a number of major pension cases in the past decade. In its decisions, the Supreme Court has provided much needed guidance in this new and emerging area of law. As this case shows, however, a number of significant questions remain to be decided.

**2** This appeal addresses a number of those difficult questions, including the following. When is it acceptable for pension plan expenses to be paid from the pension fund? After a plan conversion, is it permissible to use surplus assets in the defined benefit part of the pension plan to pay current service costs in respect of the defined contribution part of the plan? What constitutes proper notice of an adverse amendment? When and how are the courts entitled to interfere with a costs order of the Financial Services Tribunal? Does that Tribunal have the power to order costs payable from a pension fund?

**1. OVERVIEW**

**3** In 1954, the Canadian Doughnut Company Limited[1] established a defined benefit pension plan for its employees (the "Plan"). The terms of the Plan were contained in a pension plan text dated December 31, 1954 (the "original Plan text"). Funding for the pension was through company and employee contributions to a pension fund constituted as a trust (the "Fund").

**4** A separate trust agreement, dated December 31, 1954, was entered into in relation to the Fund. The parties to the trust agreement were the Canadian Doughnut Company Ltd. and the National Trust Company Limited (the "original Trust agreement"). Subsequent trust agreements were entered into from time to time, beginning in 1958.

**5** The Canadian Doughnut Company Ltd. later became DCA Canada Inc. Kerry (Canada) Inc., the appellant, is the successor to DCA. The words "company," "employer" and "Kerry" are used interchangeably hereafter to refer to Kerry and its predecessors.

**6** From inception, the role of trustee has been separate and distinct from that of the administration of the Plan. The trustee's role, and its rights and obligations, are contained in the various trust agreements executed by the trustee and the company. Administration of the Plan, however, has been by means of a Retirement Committee established by s. 4 of the original Plan text.

**7** There are approximately eighty members of the Plan. The respondents are former employees of Kerry (or its predecessor companies) and members of the Plan (the "Committee"). Certain of the Committee members are former executives of the company who took the decisions with respect to expenses and contribution holidays about which they now complain.

**8** The Plan is governed by the *Pension Benefits Act*, R.S.O. 1990, c. P.8, as amended (the "Act").

**9** The Fund has been in a surplus position for a great many years that is, there are more assets in the Fund than are needed to cover fully all of the Plan obligations. The Plan members have always received their full pension benefits and continue to do so.

**10** The Plan text has been amended and restated, from time to time. Of significance on this appeal are the amendments made in 1975, 1987 and 2000 which purported, among other things, to give the employer the power to pay Plan expenses from the Fund.

**11** In 2000, the Plan text was amended in order to introduce a defined contribution component. Existing Plan members were given the option of remaining in the defined benefit component of the Plan or converting to the defined contribution component. All new employees were required to participate in the defined contribution component of the Plan.

**12** Starting in 1985, the employer took contribution holidays in respect of its funding obligations. By 2001, it had taken contribution holidays of approximately $1.5 million.

**13** From the Plan's inception through to the end of 1984, the employer paid all Plan expenses. Beginning in 1985, however, third party Plan expenses were paid from the Fund. These expenses were primarily the cost of actuarial, investment management and audit services provided to the Plan. It is agreed that money from the Fund was used to pay for approximately $850,000 of Plan expenses from 1985 to 2002.

**14** After the 2000 Plan amendments were introduced, the Committee asked the Superintendent of Financial Services to investigate alleged irregularities in the administration of the Plan, including the payment of Plan expenses from the Fund and the employer's contribution holidays.

**15** After investigation, the Superintendent[2] issued a Notice of Proposal to make an order requiring Kerry to reimburse the Fund for expenses paid from the Fund after January 1, 1985, that were not incurred for the exclusive benefit of Plan members. The Superintendent also issued a second Notice of Proposal in which he proposed to refuse to order Kerry to pay the amounts to the Fund that had been taken by way of contribution holidays.

**16** Kerry sought a hearing before the Financial Services Tribunal (the "Tribunal") on the Superintendent's proposed order in respect of Plan expenses (the "first Tribunal hearing"). The Committee sought a hearing on the Superintendent's proposed order in respect of contribution holidays (the "second Tribunal hearing"). The Superintendent was a party to both hearings.

**17** Kerry was largely successful at both Tribunal hearings. In a decision rendered after the first Tribunal hearing, the Tribunal held that all but a very few Plan expenses could be paid from the Fund. In a second decision, the Tribunal held that Kerry was entitled to take contribution holidays.

**18** The Committee appealed both decisions to the Divisional Court. The Divisional Court heard the appeals together and issued a judgment which largely overturned the Tribunal decisions. It made a costs award requiring Kerry to pay the Committee's costs, on a partial indemnity basis, of the second Tribunal hearing and the appeals to the Divisional Court. That award also required Kerry, as administrator of the Plan, to cause the Fund to pay the balance of the Committee's costs of the appeals to the Divisional Court.

**19** Kerry appeals the judgment of the Divisional Court. The Committee cross-appeals.

**20** For the reasons that follow, I would allow the appeal and dismiss the cross-appeal.

## 2. THE ISSUES

**21** The appeal raises the following four issues.

(1) Were Plan expenses properly paid from the Fund or must Kerry reimburse the Fund for them?
(2) Could surplus pension funds be used to satisfy Kerry's contribution obligations in respect of the defined contribution component of the Plan?
(3) Did Kerry give proper notice to Plan members of the conversion option? If the notice was not sufficient, must Kerry issue a new notice and must the Superintendent refuse to register the 2000 Plan? and
(4) Did the Divisional Court err in its costs award?

**22** The cross-appeal raises two additional issues.

(5) Must Kerry remit contributions in respect of the defined benefit component of the Plan? and
(6) Does the Tribunal have the power to order costs payable from a pension fund?

**23** Before turning to these issues, however, the matter of the standard of review to be applied to the Tribunal decisions must be addressed.

## 3. STANDARD OF REVIEW OF TRIBUNAL DECISIONS - GEN-

## ERAL CONSIDERATIONS

**24** Following the Supreme Court of Canada's decision in *Monsanto Canada Inc. v. Ontario (Superintendent of Financial Services)*, [2004] 3 S.C.R. 152, there can be no question that when hearing appeals from Tribunal decisions that involve pure questions of law, the court is to apply a standard of review of correctness.

**25** In *Monsanto*, the issue to be decided was the interpretation of s. 70(6) of the Act - a matter of pure law. Unlike *Monsanto*, however, most of the questions raised by this appeal and cross-appeal are not matters of pure statutory interpretation - they are polycentric questions of mixed fact and law, many of which are highly technical and others which involve the exercise of discretion.

**26** In the recent case of *Lévis (City) v. Fraternité des policiers de Lévis Inc.*, 2007 SCC 14, the Supreme Court of Canada made it clear that multiple standards of review can apply to different matters decided by a tribunal in the course of a single proceeding[3]. This is so because the reviewing court must apply the pragmatic and functional approach to determine the appropriate standard of review for each issue under appeal.

**27** Under the pragmatic and functional approach, in order to determine the standard of review, the reviewing court must consider (1) the presence or absence of a privative clause, (2) the expertise of the decision maker relative to that of the court, (3) the purpose of any relevant legislative provisions, and (4) the nature of the question under review: *Pushpanathan v. Canada (Minister of Citizenship and Immigration)*, [1998] 1 S.C.R. 982 at paras. 29-38.

**28** In this appeal, the first factor remains unchanged regardless of the issue under consideration - there is a full statutory right of appeal to the Divisional Court pursuant to s. 91 of the Act and there is no privative clause. However, the other three factors -"relative expertise," "legislative provisions" and "nature of the question" - are not static. As the issues on this appeal raise questions of a different nature that engage the Tribunal's expertise and the legislation in different ways, it is necessary to determine the standard of review for each such decision by the Tribunal. That will be done at the outset of the analysis on each issue. However, the following general comments on the *Pushpanathan* factors apply to all and I set them out now to minimize repetition.

**29** **Relative expertise** - This factor requires the court to consider the expertise that the Tribunal brings to bear when deciding a particular matter compared to that of the courts. As Deschamps J. stated in *Monsanto*, "relative expertise must be evaluated in context and in relation to the specific questions under review" (para. 9).

**30** In my view, the Tribunal has a greater relative expertise on questions concerning pension plan documents. In that regard, I would echo the comments of Goudge J.A. in *Monsanto Canada Inc. v. Ontario (Superintendent of Financial Services)* (2002), 62 O.R. (3d) 305 (C.A.) at para. 29:

> The Act gives the Tribunal the central adjudicative role in the specialized administrative structure set up to regulate pensions in Ontario. While the Tribunal deals with other regulated sectors in addition to pensions, the *Financial Services Commission of Ontario Act* requires that, to the extent practicable, members are appointed with experience and expertise in the regulated sectors and that they are assigned to cases which draw on that experience and expertise. Hence the Tribu-

nal must be seen as having a relative expertise in adjudicating questions relating to pensions. This points to a more deferential standard of review.

**31** Although Deschamps J. took a different view of the Tribunal's expertise in *Monsanto*, that view related to the Tribunal's expertise to decide a question of pure law. In my view, the opinion expressed by Goudge J.A., set out above, remains relevant to questions of mixed fact and law involving pensions[4].

**32** **Legislative provisions** - For several of the issues on appeal, there are no legislative provisions that apply. On these matters, the provisions of the pension plan documentation dictate the result. In such circumstances, greater deference is owed to the Tribunal decision than in situations such as *Monsanto* where a question of pure law was in issue.

**33** **Nature of the Question** - Many of the issues to be decided on this appeal involve questions of mixed fact and law, which require the decision maker to apply a legal standard to a set of facts: *Housen v. Nikolaisen*, [2002] 2 S.C.R. 235 at para. 26. A less searching standard of review is appropriate on questions of mixed fact and law than for matters of pure statutory interpretation. Similarly, greater deference is warranted for decisions involving the exercise of discretion: *Suresh v. Canada (Minister of Citizenship & Immigration)*, [2002] 1 S.C.R. 3 at paras. 29-30.

**34** Accordingly, as will be seen, most of the Tribunal decisions under consideration in this appeal are subject to review on a reasonableness standard.

## 4. PAYMENT OF PLAN EXPENSES

### *Overview*

**35** From the Plan's inception through to the end of 1984, the company paid all of the expenses incurred in administering the Plan and Fund. Beginning in 1985, however, all third-party Plan expenses were paid from the Fund. These expenses included fees for trustee, investment, accounting and actuarial services. Trustee fees are not in dispute in this appeal because, in 1994, the company accepted that it was responsible for all such expenses and repaid the Fund approximately $235,000. Hereafter, I will refer to the expenses paid from the Fund, which exclude trustee fees and expenses, as the "Plan Expenses."

**36** The Tribunal held that, with one exception, it was permissible for the Plan Expenses to be paid from the Fund. The exception was for consulting fees of $6,455 paid for advice on the introduction of a defined contribution option to the Plan ("conversion option expenses"). Fees relating to the implementation of the conversion option, however, were held to be valid Plan Expenses.

**37** On appeal, the Divisional Court reviewed the Tribunal's decision on a correctness standard. It reversed the Tribunal. The Divisional Court held that the Plan provisions did not permit the Plan Expenses to be paid from the Fund and that the Plan could not be validly amended to so provide. It stated that payment of the Plan Expenses from the Fund constituted a partial revocation of the trust and that it was irrelevant whether the Plan Expenses were paid to the company or to a third party.

**38** With respect, I am of the opinion that the Divisional Court erred in the standard of review that it applied. A review of the Tribunal's decision on a reasonableness standard leads to the conclusion that there is no basis for interference with that decision. Moreover, I would not disturb the Tribunal's decision on this issue, even if it were subject to review on a correctness standard.

### *Standard of Review*

**39** The Divisional Court held that the Plan expenses issue was a question of law to which the correctness standard applied. I disagree. Based on a consideration of the *Pushpanathan* factors, I conclude that the Tribunal decision on this matter ought to have been reviewed on a reasonableness standard.

**40** **Relative expertise** - Unlike *Monsanto* which decided a question of statutory interpretation without reference to the terms of particular pension plan documentation, in this case the Plan documents are the basis on which this issue must be decided. In construing those documents, the Tribunal members were required to draw on their knowledge and understanding of pensions. Although the Tribunal has no expertise relative to the courts in applying legal principles, it does have relative expertise in interpreting pension documentation.

**41** **Legislative provisions** - There are no provisions in the Act relevant to the payment of pension plan expenses.

**42** **Nature of the question** - To determine whether the company was entitled to pay the Plan Expenses from the Fund, the Tribunal had to interpret the Plan documents applying legal principles. Although the Plan documents are not facts, they are specific to this Plan and these parties. A less searching standard of review is appropriate for this type of question than for matters of pure statutory interpretation.

**43** These three *Pushpanathan* factors[5] support treating the Tribunal decision with deference. Hence my view that the appropriate standard of review of the Tribunal decision on Plan expenses is reasonableness.

***Analysis***

**a. The Tribunal decision is reasonable**

**44** The Tribunal began by considering the provisions of the Trust agreements. It viewed the relevant provisions of the original Trust agreement as being no different than those in the 1958 Trust agreement and thereafter referred to the provisions of the latter.

**45** The Tribunal noted that the Trust agreement served two purposes. The first is to establish a trust over funds contributed to the pension plan. The second is to set out the respective rights and obligations of the parties to the Trust agreement which, in the first instance, were the company, as Plan sponsor, and National Trust, as trustee.

**46** The Tribunal interpreted ss. 5 and 19 of the 1958 Trust agreement as requiring the company to pay the trustee's fees and any expenses that the trustee incurred in performance of the trust. Those sections read as follows:

> 5. *The expenses incurred by the Trustee in the performance of its duties*, including fees for expert assistants employed by the Trustee with the consent of the Company and fees of legal counsel, *and such compensation to the Trustee* as may be agreed upon in writing from time to time between the Company and the Trustee, and all other proper *charges and disbursements of the Trustee shall be paid by the Company*, and until paid shall constitute a charge upon the Fund. ...
> 19. The Trustee shall be entitled to compensation in accordance with the Schedule of Fees on pension and profit-sharing trusts of National Trust Company, Limited now in effect, which compensation may be adjusted from time to time based up-

on experience hereunder, as and when agreeable to the Company and the Trustee. Compensation payable to any successor trustee shall be agreed to by the Company and such successor trustee at the time of its designation. Such compensation shall constitute a charge upon the Fund unless it shall be paid by the Company. The Company expressly agrees to pay all expenses incurred by it or by any Trustee in the execution of this Trust and to pay all compensation which may become due to any Trustee under the provisions of this Agreement. [emphasis added]

**47** The Tribunal noted that s. 1 of the 1958 Trust agreement stipulates that "[n]o part of the *corpus* or income of the Fund shall ever revert to the Company or be used for or diverted to purposes other than for the exclusive benefit of" the beneficiaries. The Tribunal also observed that nothing in the later trust agreements purported to modify the intent expressed in s. 1 that the Fund could be used only for the exclusive benefit of Plan beneficiaries.

**48** Section 11, the amendment provision in the 1958 Trust agreement, was subject to the same limitation. The relevant part of s. 11 reads as follows:

> 11. This Agreement may be amended in whole or in part or be terminated any time and from time to time by an instrument in writing executed by the Company and the then Trustee; provided however that unless approved by the Minister of National Revenue *no such amendment shall authorize or permit any part of the Fund to be used for, or diverted to, purposes other than for the exclusive benefit of such employees, or their beneficiaries or personal representatives* as from time to time may be included under the Plan, and for the payment of taxes, assessments, or other charges as provided in Section 5 and Section 19 herein, provided, it being understood that this proviso is not to be construed to enlarge the obligations of the Company beyond those assumed by it under the Plan. [emphasis added]

**49** The Tribunal then considered the Plan texts. It noted that the original Plan text contained no provision dealing with payment of Plan or Fund expenses. It considered the Plan amendments in 1975, 1987 and 2000, all of which were directed at providing that reasonable Plan expenses would be paid from the Fund, and concluded that the amendments were permissible so long as such expenses were, in accordance with the terms of the Trust agreement, for the "exclusive benefit" of Plan members.

**50** The Tribunal heard expert evidence that the words "exclusive benefit" had no special meaning in the pension field. It also heard expert evidence that the Plan Expenses were for the exclusive benefit of Plan members because they were routine expenses essential to the continued operation of the Plan.

**51** The Tribunal considered the amendments made in respect of expenses in 1975, 1987 and 2000 to be consonant with the Plan and trust documents. It concluded that the amendments did not authorize the use of the Fund other than for the exclusive benefit of Plan members. In so concluding, the Tribunal construed the words "exclusive benefit" as meaning "primary benefit." It explained that on a strict interpretation of those words, even payment of pension benefits to a member could be said to be other than for the exclusive benefit of Plan members as the payment benefited the company by virtue of discharging its obligation. The Tribunal concluded that the Plan Expenses, apart from $6,455 spent to obtain advice on the addition of the defined contribution option, were

incurred for the primary benefit of the Plan beneficiaries. It ordered Kerry to repay only the sum of $6,455.

**52** The Tribunal considered the Trust agreement and Plan text separately, recognizing the differences between those types of documents. It focused on the relevant provisions in both and construed those provisions reasonably. Accordingly, in my view, the Tribunal's decision was reasonable and it ought to be restored.

### b. Plan expenses are properly payable from the Fund

**53** Even if the Tribunal were required to be correct on this issue, I would not interfere with the result.

**54** I approach a determination of this issue in the following way.

**55** First, I looked to the Act to determine whether it contains any provisions that govern the payment of pension plan expenses. There are none.

**56** Next, I considered whether there are any principles of law, trust or otherwise, that would require the company to pay the Plan Expenses. I know of none. I understand trusts to operate on the basis that expenses of the trust are paid from the *corpus* of the trust unless the trust agreement provides otherwise. This understanding is reinforced by s. 23.1 of the *Trustee Act*, R.S.O. 1990, c. T.23, as am. by S.O. 2001, c. 9, Sch. B, s. 13(1), which permits a trustee to pay expenses properly incurred in carrying out the trust from the trust property or to seek indemnification from the trust for any such expenses.

**57** The Plan documentation (Trust agreement and Plan text) was then reviewed to determine whether the matter of expenses had been addressed. If, in the documentation, the company undertook to pay the Plan Expenses, it must do so, unless that undertaking was validly amended. Absent such an undertaking, the company was under no legal obligation to pay such expenses.

**58** Pursuant to ss. 5 and 19 of the Trust agreement, set out above, the company undertook to pay the trustee's fees and expenses. Thus, as the company acknowledges, it is obliged to pay the trustee's fees and expenses.

**59** However, a properly administered pension plan requires a number of services in addition to those of a trustee, including actuarial, accounting and investment functions. The Plan text vests responsibility for ensuring that such functions are fulfilled in the Retirement Committee. The relevant parts of s. 4 of the original Plan text read as follows:

> 4. ADMINISTRATION OF THE PLAN
>
> The Plan shall be administered by a Retirement Committee consisting of at least three members appointed by the Company. ...
>
> The Committee shall have the right and power, among other rights and powers,
>
> (a) to authorize payments of the benefits provided by the Plan;
> (b) to make and enforce uniform and non-discriminatory rules for the efficient administration of the Plan, to interpret the Plan and to decide finally and

conclusively any questions that may arise in connection with the Plan subject to the provisions of the Text of the Plan and of the Trust Agreement;

(c) *to employ or appoint Actuaries, Accountants, Counsel (who may be Counsel for the Company) and such other services as it may require from time to time in the administration of the Plan* ... [emphasis added]

**60** The Plan text is silent in respect of payment of the Plan Expenses. Silence does not create a legal obligation on the company to pay.

**61** Neither the Trust agreement nor the Plan text placed an obligation on the company to pay the Plan Expenses. Based on those documents, the company is obliged to pay only the trustee fees and its expenses incurred in the execution of the trust. As it did not undertake to pay the Plan Expenses, it had no legal obligation to pay for them. The fact that the company voluntarily chose to pay the Plan Expenses for a period of time does not create a legal obligation on it to continue to pay such expenses.

**62** It will be apparent from the foregoing that I disagree with the Divisional Court's view that because the 1958 Trust agreement specified that taxes, interest and penalties were to be paid by the Fund but did not specify that the Plan Expenses were to be paid also from the Fund, it was reasonable to infer that the expenses were not payable from the Fund and to place the obligation to pay such expenses on the company. The company is responsible for the obligations that it undertook; the failure of the original Plan documentation to directly address payment of the Plan Expenses does not lead to the conclusion that the company is obliged to pay for them. In accordance with general trust practice and principles, the trust fund would bear such expenses.

**63** I make two responses to the argument that s. 11 of the Trust agreement precluded any amendment permitting payment of the Plan Expenses from the Fund. This argument is based on the limitation in s. 11 that no amendment can be made that would permit the Fund to be used other than for the exclusive benefit of the employees (the "limitation").

**64** First, in my view, the limitation is directed at "true" amendments - that is, amendments which change a party's rights or obligations. As I have explained, the company was under no obligation to pay the Plan Expenses - they could have been paid from the Fund from the outset. Amending the Plan text to reflect this made no change to the rights or obligations of any person so the limitation was not engaged. As a procedural matter, an amendment was required in order to change the Plan text to make it clear how the Plan Expenses were to be paid but that was an amendment in form, not substance.

**65** Second, s.11 expressly provides that it "is not to be construed to enlarge the obligations of the Company beyond those assumed by it under the Plan." The company was under no obligation to pay for the Plan Expenses. If the limitation in s. 11 is held to preclude an amendment that permits the Fund to be used to pay the Plan Expenses, the company will be forced to pay such expenses in order to ensure that the Plan continues. That means that s. 11 will have been used to enlarge the company's obligations beyond those that it had assumed under the Plan. Such a result is directly prohibited by that part of s. 11 which provides that it is not to be construed so as to enlarge the company's obligations.

**66** In light of this conclusion, it is unnecessary to decide whether the Tribunal was correct in construing "exclusive benefit" to mean "primary benefit."

**67** Finally, I am of the view that the Tribunal was correct in requiring the company to repay the Fund the sum of $6,455. It will be recalled that the money was paid for advice about the addition of the defined contribution option. In my view, the company obtained that advice for its own benefit, in order to determine whether it wished to alter the structure of the Plan. Even if the advice was obtained by the company in its role as the Plan sponsor, that does not mean that it was obtained on behalf of the Plan. It remains information that the Plan sponsor sought in order to determine how it wished to proceed in terms of the Plan structure. As the expense was that of the company, it is obliged to pay for it.

**c. No partial revocation of trust**

**68** I disagree also with the Divisional Court's view that to permit the company to pay the Plan Expenses from the Fund amounted to a revocation of trust. Revocation is the return of (some or all of) the trust funds to the person who placed the funds in trust. So, for example, revocation occurs when an employer withdraws surplus monies from a pension fund. Payment of expenses to a third party does not fall within that definition as no money was returned to the company.

**69** The Divisional Court relied on this court's recent decision in *Markle v. Toronto (City)* (2003), 63 O.R. (3d) 321 in concluding that payment of the Plan Expenses amounted to a partial revocation. In that case, this court held that the right to amend a pension plan did not entitle the City of Toronto to recover contributions that it had made, even where the recovery was for services that the City had provided to the Plan.

**70** *Markle*, however, is very different factually from the present case. As will be seen, the result and reasoning in *Markle* are consistent with the notion of revocation articulated above and with my conclusion that causing the Fund to pay for third party expenses incurred by the Plan does not amount to revocation.

**71** In *Markle*, the City enacted a by-law to provide pension benefits for its permanent employees. The by-law created a contributory, defined benefit plan. Contributions were held in a trust fund. Administration of the plan was vested in a board of trustees. The board of trustees was responsible for all aspects of administering the plan and fund. Thus, the board was responsible not only for holding the plan funds but also for investing the funds, paying benefits and appointing the plan actuary and accountant.

**72** The by-law stipulated that the City would bear all expenses incurred by the board. It also provided that the City had the right to amend the by-law "provided always that no such amendment shall entitle [the City] to recover any contribution whatever made by it into the [f]und."

**73** The City provided administrative services to the plan. In 2001, it enacted a by-law (the "later by-law") which purported to have the cost of those services paid from the fund. The City then sent the board an invoice for $181,333.40.

**74** The board applied for a determination of the legality of the later by-law. At first instance and on appeal, it was held that the later by-law was invalid, in part because it amounted to a partial revocation of trust.

**75** There are three critical differences between *Markle* and the present case.

(1) In *Markle*, the by-law specified that no amendment could permit the City to recover "any contribution whatever" that it made to the pension fund.

The later by-law purported to allow the City to recover contributions, albeit as compensation for services rendered. That is, the later by-law purported to do that which was directly prohibited in the original by-law.

In the present case, there was no provision making the company responsible for the Plan Expenses, so later amendments permitting such expenses to be paid from the Fund are not in conflict with original plan documents. The only obligation placed on the company, which came from the original Trust agreement, was to pay for trustee fees and expenses incurred in the execution of the trust; the company acknowledges that obligation and continues to meet it.

(2) In *Markle*, if the later by-law had been held valid, the City would have been returned part of its contributions to the trust fund. I recognize that the character of the money changed in that the City made payments to the fund by way of contribution but it would have received money from the fund as compensation for the administrative services it had rendered. Nonetheless, the return of money to the City falls within the definition of revocation, namely, the return of trust funds to a person who has placed funds in the trust. In the present case, Kerry is not asking that money from the trust fund be returned to it. It is asking that the Plan pay for expenses it incurred on behalf of Plan members.

(3) The expenses at issue in the present appeal were not in issue in *Markle*. It is clear from the trial decision in *Markle*[6] that the board was not challenging the provision in the by-law that provided that third party services were to be paid from the pension fund; it questioned payment for services rendered by the Plan sponsor. Here, the company asks for no funds - payments are only for third party services.

## 5. APPEAL AND CROSS-APPEAL IN RESPECT OF CONTRIBUTION HOLIDAYS

### *Overview*

**76** It will be recalled that the company established a defined benefit pension plan for its employees in 1954 and that the Plan was funded through employer and employee contributions which were held in a trust fund. The initial beneficiaries of the Fund were employees and retired employees, their beneficiaries or estates, and their contingent annuitants (s. 22 of the original Plan text).

**77** In 2000, the Plan was amended to add a defined contribution component. The effect of the 2000 amendments was to create two categories of Plan members - those in the defined benefit component and those in the defined contribution component.

**78** In 1999, existing Plan members who would be active members of the Plan on January 1, 2000, were given a one-time option to convert their defined benefit entitlement to a defined contribution entitlement. Those who did not elect to convert remained as members of the defined benefit component of the Plan ("Part 1 members"). After January 1, 2000, all new employees were required to participate in the defined contribution component of the Plan. The pre-2000 Plan members who

exercised the conversion option together with the new Plan members who were in the defined contribution component of the Plan are termed "Part 2 members."

**79** Funds contributed to the defined contribution component of the Plan were held by the Standard Life Assurance Company pursuant to an insurance contract. When a Part 2 member retires, the accumulated contributions held by Standard Life to that member's benefit are used to purchase a life annuity for the member. The payments from the life annuity are the member's pension.

**80** The employer began taking contribution holidays in 1985. It continued to do so after the Plan was amended in 2000 for both Part 1 and Part 2 members. The contribution holidays were taken through use of the actuarial surplus in the Fund which had accrued when the Plan was a defined benefit plan only.

**81** The Committee asked the Superintendent to refuse to register the 2000 Plan on the basis that, among other things, the provisions in the 2000 Plan text that permitted the company to take contribution holidays in respect of Part 2 members were contrary to the Trust agreement ("cross-subsidization"). It also challenged the right of the company to take contribution holidays in respect of the defined benefit component of the Plan.

**82** The Tribunal held that the provisions in the 2000 Plan permitting cross-subsidization were inconsistent with the terms of the Trust agreement. It concluded, however, that the conflict could be resolved by amending the 2000 Plan to designate Part 2 members as Fund beneficiaries. It would have permitted registration of the 2000 Plan so long as it had been amended to make the Part 2 members beneficiaries of the Fund.

**83** The Tribunal also held that the company was entitled to take contribution holidays in respect of the Part 1 members.

**84** The Divisional Court set aside the Tribunal's decision in respect of the cross-subsidization. It viewed the 2000 amendments as having created two pension plans and funds and held that cross-subsidization was impermissible - that is, Kerry could not use surplus money in the Fund to satisfy its contribution obligations in respect of the Part 2 members. Consequently, the Divisional Court ordered the Superintendent to refuse registration of the 2000 Plan.

**85** Like the Tribunal, however, the Divisional Court held that the contribution holidays taken in respect of the defined benefit component of the Plan were acceptable.

**86** Kerry appeals and asks that the cross-subsidization decision of the Tribunal be restored.

**87** The Committee cross-appeals; it seeks an order requiring Kerry to remit the amounts that it has taken by way of contribution holidays in respect of the defined benefit component of the Plan.

**88** The appeal and cross-appeal are dealt with in separate sections, below.

**89** Before turning to that analysis, I will consider the standard of review on the issue of contribution holidays; this reasoning applies to both the appeal and cross-appeal. As will be seen, unlike the Divisional Court which applied a standard of correctness to the Tribunal's decisions on contribution holidays, in my view, those decisions are subject to review on a reasonableness standard. As the Tribunal's decisions are reasonable, they should be permitted to stand. Moreover, as I explain, even if those decisions must be correct, I would not interfere with them.

***Standard of Review***

**90** Again, the *Pushpanathan* factors must be considered to determine the standard of review applicable to the question of whether the employer was permitted to take contribution holidays.

**91** For the same reasons as those given in respect of the standard of review on the issue of Plan expenses, in my view, the standard of review on the question of the permissibility of the contribution holidays is reasonableness. This issue, like that of Plan expenses, required the Tribunal to interpret the Plan documents, a matter on which they have relative expertise. This issue, like that of Plan expenses, is specific to this Plan and these parties and warrants a higher degree of deference than do matters of pure law; it is not a matter of pure statutory interpretation, a matter on which the Tribunal is required to be correct. And, again like the situation in respect of Plan expenses, there are no statutory provisions governing this issue.

**92** Accordingly, the Tribunal's decisions on contribution holidays are to be reviewed on a reasonableness standard.

## 6. CONTRIBUTION HOLIDAYS IN RESPECT OF THE DEFINED CONTRIBUTION COMPONENT OF THE PLAN (APPEAL)

**93** The Tribunal accepted the Committee's argument that permitting cross-subsidization was inconsistent with the provisions of the Trust agreement. It explained this conclusion as follows. The trust provisions permitted the Fund to be used or diverted only for the "exclusive benefit of" Fund beneficiaries. The 2000 Plan confined the Fund beneficiaries to Part 1 members. That is, it did not make Part 2 members beneficiaries of the Fund. Thus, use of the Fund by means of a contribution holiday in respect of Part 2 members was inconsistent with the Trust agreement requirement that the Fund be used only for the exclusive benefit of Fund beneficiaries.

**94** However, the Trust agreement also provided that beneficiaries of the Fund were those persons designated under the Plan (s. 1). Under the terms of the Plan, it was possible to designate Part 2 members as beneficiaries of the Fund. Thus, the Tribunal held that the contribution holidays in respect of Part 2 members were permissible so long as the Plan was amended to designate Part 2 members as beneficiaries of the Fund, with effect from January 1, 2000.

**95** The Tribunal rejected the argument that *Aegon Canada Inc. v. ING Canada Inc.* (2003), 179 O.A.C. 196 (C.A.) precluded this result. In *Aegon*, two separate pre-existing plans - one in a surplus position and the other in deficit - were merged as a result of the amalgamation of NN Life Insurance Company of Canada and Halifax Life Insurance Company of Canada. The plans were merged subject to the condition, imposed by the Pension Commission of Ontario, that the assets and liabilities of each plan were to be accounted for separately in the merged plan. The pension plan that was in surplus was subject to a trust in favour of the plan members. This court held that no part of the assets of the fund in surplus could be applied to meet the liabilities associated with the other fund without breaching the trust in favour of the beneficiaries of the fund in surplus.

**96** The Tribunal distinguished *Aegon* on the basis that in the present case, there was a single plan formed with the intention of benefiting all of the company's employees, present and future.

**97** In my view, the Tribunal's decision is reasonable and ought to stand. In reaching this conclusion, it is important to note the caution with which the Tribunal approached this matter. The Tri-

bunal was clearly alive to the potential for misuse of surplus funds and its reasons make it clear why it was satisfied that no misuse was occasioned in the present case.

**98** However, even if the Tribunal must be correct on this matter, I see no basis on which to interfere with its decision.

**99** This conclusion flows from the following five points.

**100** First, nothing in the original Plan and Trust documents prohibited the taking of contribution holidays. Consequently, as I explain more fully in the following section, *Schmidt v. Air Products of Canada Ltd.*, [1994] 2 S.C.R. 611 provides that the company has the right to use the actuarial surplus to fund its contributions while the Plan is ongoing. It is significant to note that *Schmidt* establishes that right even where, as here, the trust agreement provides that the fund is to be used exclusively for the benefit of plan members.

**101** Consequently, to the extent that the Divisional Court's decision is premised on the notion that the Plan members were entitled to surplus while the Plan was ongoing, I respectfully disagree. *Schmidt* makes it clear that members of a pension plan have no entitlement to the actuarial surplus in an ongoing pension plan. Justice Cory explained in *Schmidt* that members in plans with exclusive benefit language or the equivalent are entitled to "two distinct types" of benefits: the benefits promised under the pension plan and the right to share in surplus remaining on plan termination (654-5).

**102** Second, s. 9 of the *Pension Benefits Regulations*, R.R.O. 1990, Reg. 909, provides that after a plan conversion, surplus can be used to fund employer contributions. Section 9 reads as follows:

> 9. If an amendment to a pension plan with defined benefits converts the defined benefits to defined contribution benefits, the employer may offset the employer's contributions for normal costs against the amount of surplus, if any, in the pension fund after conversion.

**103** Although the Plan has introduced a defined contribution component, rather than been fully converted, this provision confirms that an employer is entitled to use the actuarial surplus to fund contributions where a defined benefit arrangement is not maintained.

**104** Third, the company was at liberty to introduce a new category of Plan member: there is nothing in law or the Plan documentation to prevent such an action. The Plan text expressly permits the company to unilaterally amend the plan (s. 22). Thus, the company could amend the Plan to introduce a new category of member. So, for example, if there were part-time employees for whom the company wished to provide a pension, it could create a new category of members and permit the part-time employees to become Plan members in that category.

**105** Fourth, if the company introduced a new category of Plan member, it would be entitled to take contribution holidays in respect of that new category (*Schmidt*). The fact that overall Plan membership was expanded through inclusion of a new category of member would not alter the company's right to take contribution holidays.

**106** Fifth, cross-subsidization is not prohibited by the Trust agreement. What is prohibited is the use of the Fund for other than the exclusive benefit of Fund beneficiaries. Once the Part 2 members are designated Fund beneficiaries,[7] use of the Fund's surplus by way of contribution holi-

days in respect of them meets the requirement that the Fund be used exclusively for the benefit of Fund beneficiaries.

**107** Once the 2000 Plan is amended to designate the Part 2 members as beneficiaries of the Fund, the entitlement of members would be as follows:

- Part 1 members - pension benefits are paid from the Fund.
- Part 2 members - pension benefits are paid from the funds in the member's account, at the time of retirement, with Standard Life (through the purchase of an annuity).
- On Plan termination - both Part 1 and Part 2 members are entitled to lay claim to the Fund's surplus.

**108** In short, Part 2 members would receive their pension benefits from their accounts with Standard Life but would have the same right as Part 1 members to make a claim to any surplus in the Fund, on Plan termination.

**109** I recognize that the present case was not simply the introduction of a new category of Plan member - it also created a new funding arrangement for the payment of pension benefits for the Part 2 members. Thus, it must be asked, does that change the foregoing analysis? The answer to that question is "no," so long as the Part 2 members are made Fund beneficiaries.

**110** Why is that? Why can the Fund be used for the benefit of Part 2 members when the surplus in the Fund accrued prior to some of them becoming Plan members?[8] The answer lies in the Plan documentation. Read as a whole, it is apparent that: (1) the Plan and Fund were created to benefit all full-time employees; and (2) it was intended that all full-time employees would become members of the Plan and beneficiaries of the Fund. The Plan documents created an "open" pension plan in the sense that it was designed for employees, an ever-changing class with some employees leaving before retirement and new employees joining. Because employment is not static so neither is membership in the Plan. It does not matter whether new members arrive one at a time or as a group, the Plan was designed to permit them to become Plan members and Fund beneficiaries.

**111** Finally, I do not see the introduction of the defined contribution component to the Plan as creating a second plan. In this regard, I disagree with the Divisional Court. In my view, a single plan remained after the introduction of the defined contribution component. The fact that the Plan consisted of two components does not mean that a new plan was created for Part 2 members. Control, management and administration of the Plan remained with the Retirement Committee and the company, as Plan administrator. The fact that pension benefits were payable from the Fund in the case of Part 1 members and from annuities in the case of Part 2 members does not lead to the conclusion that there were two different plans, particularly as both Part 1 and Part 2 members have a claim to any Fund surplus remaining on Plan termination.

**112** On this view, I do not see *Aegon* as relevant to the instant case. *Aegon* was about the merger of two existing independent pension plans. This is not a plan merger case: the same Plan continued to exist although it had two components and two categories of members. Put another way, it was the unexpected liabilities presented by merger with a second plan that led to the need for segregation in *Aegon*. Absent segregation, the Halifax Plan members' rights would have been diminished by the addition of a new category of beneficiaries whose membership was not contemplated at

the time the Halifax Plan was created. In the instant case, however, the new category of member was contemplated from the outset as the Plan was designed for all full-time employees.

**113** Accordingly, while my reasoning differs from that of the Tribunal, I arrive at the same result. Consequently, even if the Tribunal had to be correct on this matter, its decision should be reinstated.

## 7. CONTRIBUTION HOLIDAYS IN RESPECT OF THE DEFINED BENEFIT COMPONENT OF THE PLAN (CROSS-APPEAL)

**114** On cross-appeal, the Committee argues that the Divisional Court erred in concluding that Kerry was entitled to take contribution holidays in respect of the defined benefit component of the Plan. The Committee submits that the terms of the original Trust agreement prohibit contribution holidays and that amendments made in 1965 explicitly permitting contribution holidays are invalid because they constitute a partial revocation of the Fund.

**115** Kerry submits that the Divisional Court and the Tribunal correctly concluded that the Supreme Court of Canada's decision in *Schmidt, supra,* establishes that it was entitled to take contribution holidays. I agree.

**116** In my view, there is no question but that Kerry's contribution holidays in respect of the defined benefit component of the Plan were permissible. *Schmidt* establishes that an employer may take contribution holidays when a defined benefit pension plan enjoys an actuarial surplus, unless the plan documentation explicitly provides otherwise. A specific formula for calculating the employer's annual contribution is an example of such a provision. However, if an employer's contribution is to be determined by an actuarial calculation of the amount necessary to fund promised benefits, a contribution holiday is permissible. Thus, the Plan documentation must be examined to determine whether Kerry was entitled to take contribution holidays.

**117** Kerry's funding obligation, as set out in s. 14(b) of the original Plan text, requires Kerry to contribute the amount necessary to fund current and future benefits. Section 14(b) reads as follows:

> (b) Contributions by the Company
>
> In addition to contributing the full cost of providing the Past Service retirement incomes referred to in Section 13(a) of this Plan, the Company shall also contribute, in respect of Future Service benefits, such amounts as will provide, when added to the Member's own required contributions, the Future Service retirement incomes referred to in Section 13(b) of the Plan.

**118** Section 14(b) does not contain a formula by which Kerry's contributions are determined. Although no explicit reference is made to actuarial calculations, there is no other means by which Kerry's contributions could reasonably be determined. Section 14(b), therefore, implicitly permits Kerry to take contribution holidays by limiting its contribution obligation to the additional amount needed to pay current and future benefits, if any. When no such amount is needed, Kerry is not obligated to contribute.

**119** As a result of this determination, it is unnecessary to decide the second question raised by the Committee, namely, whether the 1965 amendments permitting contribution holidays were invalid. Because the original Plan text permits the employer to take contribution holidays, the 1965 amendment does nothing but make that right explicit.

**120** The Committee makes several additional arguments against Kerry's right to take contribution holidays.

**121** First, it submits that in other cases, language similar to that in s. 14(b) has been held to amount to a formula for determining an employer's contribution, and thus to preclude the taking of contribution holidays. It points to *C.U.P.E., Local 1000 v. Ontario Hydro* (1989), 68 O.R. (2d) 620 (C.A.); *Trent University Faculty Association v. Trent University* (1997), 35 O.R. (3d) 375 (C.A.); *Hockin v. Bank of British Columbia* (1995), 123 D.L.R. (4th) 538 (B.C.C.A.); and *Chateauneuf v. T.S.C.O. of Canada Ltd.* (1995), 124 D.L.R. (4th) 308 (Que. C.A.), as examples.

**122** Those cases, however, are fundamentally different. In those cases, the pension plan documentation contained a formula by which the employer's annual contribution was calculated: the employer was to pay the difference between the employees' contributions and the benefits either accrued or paid out in a given year. As previously mentioned, s. 14(b) is not such a formula. It requires Kerry to contribute the amount needed to ensure that the Fund will be able to pay the current and future benefits owed to Plan members. This requires a determination of the amount needed to ensure that the Fund remains adequately funded rather than the amount needed to pay benefits in the current year. This distinction was recognized by LeBel J.A. (as he then was) in *Chateauneuf* as integral to determining whether a pension plan permits contribution holidays (401-2).

**123** Second, the Committee argues that contribution holidays are prohibited by the terms of the Plan. It asserts that the Divisional Court failed to appreciate that although contributions do not become part of the *corpus* of the Fund until paid, the requirement that Kerry make ongoing contributions is a separate trust obligation imposed by the Plan. As just explained, the Plan does not create such an obligation. Further, this submission is inconsistent with *Schmidt*. Beneficiaries of a defined benefit pension plan are entitled to the benefits promised by the plan, and may be entitled to any surplus actually remaining on plan termination. They do not have a claim to any notional surplus that exists while the plan is ongoing. (See *Schmidt* at 654-5.) It follows that the Plan members cannot compel the employer to make additional contributions to preserve or increase the actuarial surplus. It would be inconsistent with both the result and the reasoning in *Schmidt* to find that Kerry is obliged to make contributions while the Fund enjoys an actuarial surplus, given the language of s. 14(b).

**124** Third, the Committee submits that contribution holidays constitute an impermissible partial revocation of trust. It argues that Kerry has made a binding promise, which it cannot unilaterally amend or revoke, to alienate certain property to the Fund. Again, this argument runs squarely contrary to the terms of the Plan. Section 14(b) does not contain an unconditional promise that Kerry would alienate property to the Fund. The promise is that Kerry would make contributions when necessary. Further, it is only after money is contributed to the pension trust fund that it becomes trust property and, therefore, subject to the possibility of revocation.

**125** Finally, the Committee argues that clauses permitting contribution holidays should be construed narrowly because there is a strong policy interest in requiring companies to make ongoing contributions to protect employees against the employer's potential future financial hardship.

*Schmidt* is a full answer to this argument. Kerry is required by s. 14(b) to make only those contributions necessary to ensure the Fund can pay all benefits. It is legally entitled to take contribution holidays so long as that obligation is met. I would add that there is nothing in the record to support such an argument in this case. There is no evidence to suggest that Kerry would be unable to make any future contributions that might be required or that the Fund will be unable to pay benefits owed. In fact, given the continuing surplus position of the Fund, the evidence is to the contrary.

## 8. NOTICE OF CONVERSION OPTION

### *Overview*

**126** In November 1999, Kerry gave notice to its employees that they had a one-time option to convert the value of their defined benefit entitlement, as of January 1, 2000, to a defined contribution arrangement. The notice advised that the option had to be exercised by December 15, 1999, and that any such exercise would have the effect of eliminating pension entitlement under the existing defined benefit plan.

**127** For various reasons, including that Kerry had given allegedly inadequate notice about the conversion option, the Committee asked the Superintendent to refuse to register the 2000 Plan.

**128** The Superintendent refused to take the action requested by the Committee; consequently, the Committee asked for a hearing before the Tribunal in relation to this matter.

**129** At the Tribunal hearing, the Committee renewed its complaint in relation to the notice and asked the Tribunal to direct the Superintendent to refuse registration of the 2000 Plan.

**130** The Tribunal found that there were "shortcomings" in the "disclosure" process that raised questions as to whether the employees had been given adequate information about the conversion option. However, it held that any such shortcomings were insufficient to constitute grounds on which the Superintendent could refuse to register the 2000 Plan. The Tribunal found it unnecessary to decide whether Kerry was obliged to give notice of the conversion option.

**131** The Divisional Court held that Kerry, as administrator of the Plan, had a duty to give notice to all affected parties, including former employees who were beneficiaries under the original Plan, of all of the proposed changes that would take place as a result of the 2000 Plan amendments and that it failed to give proper notice. It relied on ss. 22 and 26(1) of the Act in arriving at this conclusion.

**132** The Divisional Court also reasoned that the failure to give proper notice amounted to a failure to administer the Plan in accordance with the Act. Relying on ss. 18 and 87 of the Act, the Divisional Court held that the Superintendent erred in failing to refuse registration of the 2000 Plan and it so ordered.

**133** Kerry argues that the Divisional Court erred in finding that inadequate notice had been given.

**134** The Superintendent argues that the Divisional Court erred in ordering him to refuse registration of the 2000 Plan.

**135** To resolve the matters raised by the parties in respect of this issue, three questions must be addressed. These are:

i. Was Kerry, as administrator of the Plan, required by the Act to give notice of the amendment that created the conversion option?
ii. If so, was adequate notice given? and
iii. Was the Divisional Court correct in ordering the Superintendent to refuse to register the 2000 Plan?

***Standard of Review***

**136** In my view, the appropriate standard of review must be determined for each of the three questions. My intent is not to overly complicate this matter. But, as explained above, *Lévis* makes clear that multiple standards of review can apply to different matters decided in a single proceeding. And, considering these questions on the pragmatic and functional approach established by *Pushpanathan*, it is apparent that the three questions are each of a different nature and may engage the Tribunal's expertise and the Act in different ways.

**137** The first question - whether notice was required - depends on interpreting s. 26(1) of the Act to determine whether it applies to the conversion option amendment. Although this is a question of mixed fact and law, its outcome depends on the proper interpretation of s. 26(1). As *Monsanto* makes clear, the court's expertise exceeds that of the Tribunal in matters of statutory interpretation. In addition, if s. 26(1) applies, the Superintendent must require the administrator to give notice unless the limited circumstances set out in s. 26(4) are found to exist, in which case he can choose to not require transmittal of the notice. Thus, while recognizing that s. 26(4) creates a limited discretion in the Superintendent, in my view, s. 26(1) is better understood as mandatory in nature. A weighing of these factors leads me to conclude that the standard of review for the first question is correctness.

**138** Different considerations apply in respect of the second question, however. Whether the notice that was given was adequate is a question of mixed fact and law: it involves the application of the legal standards for notice to the particular facts of this case to determine whether the legal requirements have been met. For reasons similar to those given in respect of the issues of Plan expenses and contribution holidays, this question is subject to review on a standard of reasonableness.

**139** The third question revolves around a discretionary decision of the Tribunal. As has been noted, where the decision involves the exercise of discretion, greater deference is owed: see *Suresh, supra*. As the Act expressly permits the Superintendent (and the Tribunal, if a hearing is convened) to decide whether it is appropriate to refuse registration, a more deferential standard of review is called for. Consequently, the decision of the Tribunal in respect of the third question is also, in my view, reviewable on a reasonableness standard.

**140** It is unclear what standard of review the Divisional Court applied when reviewing the Tribunal's decision on these matters. While nothing is said explicitly in this regard, it appears that the Divisional Court considered the questions as a single matter and applied a standard of correctness[9].

***Analysis***

**a. Was there a statutory duty to give notice?**

**141** Section 26 of the Act governs adverse amendments. Section 26(1) stipulates that if an administrator applies for registration of an amendment that would reduce benefits or "adversely affect

the rights or obligations of a member or former member," the Superintendent *shall* require the plan administrator to transmit notice to specified persons. Section 26(1) reads as follows:

> 26(1) *If the administrator of a pension plan applies for registration of an amendment to the pension plan that would result in a reduction of pension benefits* accruing subsequent to the effective date of the amendment *or that would otherwise adversely affect the rights or obligations of a member or former member or of any other person* entitled to payment from the pension fund, *the Superintendent shall require the administrator to transmit* to such persons as the Superintendent may specify *a written notice* containing an explanation of the amendment and inviting comments to be submitted to the administrator and the Superintendent, and the administrator shall provide to the Superintendent a copy of the notice and shall certify to the Superintendent the date on which the last such notice was transmitted. [emphasis added]

**142** In my view, Kerry, as administrator of the pension plan, had a statutory obligation pursuant to s. 26(1) of the Act to give notice of the Plan amendment that created the conversion option.

**143** The Act provides that pension plans must be registered (s. 6). To be registered, among other things, the plan administrator must file copies of all plan documentation with the Superintendent (ss. 9 and 10). The obligation to ensure that pension plan documentation is filed for registration is ongoing; the plan administrator must apply to the Superintendent for registration of all plan amendments (s. 12).

**144** In my view, a conversion from a defined benefit plan to a defined contribution plan is an adverse amendment within the meaning of s. 26(1)[10]. Why? Because of the uncertainty and risk for a plan member that such a change brings about. Uncertainty arises because the pension plan changes from one in which a plan member receives a guaranteed, defined pension benefit to one in which the amount that will be received is unknown until retirement. Risk increases because the plan member bears the full risk of loss or diminution if the defined contribution investments do not perform well. Although a conversion to a defined contribution plan does not necessarily result in a reduction in benefits, such a result can occur. Because of that risk and the uncertainty as to the quantum of the pension benefit to be received, it seems to me that an amendment that converts a defined benefit pension plan to a defined contribution plan is within the purview of s. 26(1). The intent of s. 26(1) is to ensure that plan members are apprised of changes to their pension plan that may adversely affect their rights. As the change to a defined contribution plan could have that effect, the Superintendent was obliged to require Kerry, *qua* administrator, to transmit notice.

**145** I recognize that in the present case the Plan was not actually converted. Rather, existing Plan members were given the option to convert. However, in order to meaningfully exercise that option and in light of the potentially adverse consequences that can arise if the option is exercised, the Plan members need proper information. Thus, in my view, notice is required pursuant to s. 26(1).

**146** The Divisional Court linked the obligation to give notice flowing from s. 26(1) of the Act to s. 22 of the Act. With respect, I do not see s. 22 as relevant to the question of whether notice of the conversion option was required. Section 22 specifies the standard of care owed by an administrator in the administration and investment of the pension fund[11].

### b. Was adequate notice given?

**147** When determining whether adequate notice has been given, two questions must be asked: (1) was the content of the notice accurate and sufficient? and (2) were all affected parties given notice? The latter question may be subject to modification in the pension context because s. 26(1) of the Act gives the Superintendent the power to specify the persons to whom notice must be given.

**148** The Divisional Court found that the content of the notice was inadequate because it failed to disclose all of the changes that the 2000 amendments would make to the Plan, including the fact that "cross-subsidization" would occur. With respect, that finding does not correspond to the matter in issue. The question was whether Kerry gave adequate notice of the conversion option; the question was not whether Kerry had given adequate notice of all of the 2000 Plan amendments, including its intended use of surplus assets. The question of adequacy of notice of the latter matters does not arise unless it has first been decided that s. 26(1) requires that notice be given of such matters. Whether notice of the other 2000 Plan amendments is required is beyond the scope of this appeal as the Committee request to both the Superintendent and the Tribunal was based on the specific allegation of inadequate notice of the conversion option.

**149** The Tribunal said only this in respect of the adequacy of notice: the Superintendent found the notice to be adequate. As will be apparent from my determination that a reasonableness standard of review is appropriate on the matter of the adequacy of notice, deference is to be afforded a Tribunal decision on such a matter. However, as the Tribunal gave no meaningful reasons for its decision, no deference is owed to it.

**150** In any event, the Tribunal's decision is not reasonable. The conversion election form specified that if the member elected to transfer to the defined contribution "plan," the member would "have no further rights and entitlements under the defined benefit plan." The quoted phrase encompasses more than simply the value of a member's accrued pension entitlement under the Plan ("pension entitlement"). If it was intended that exercise of the conversion option would extinguish not only a member's pension entitlement but also all other rights in the Plan and Fund, including the right to future Plan enhancements and to claim entitlement to surplus on Plan termination, then the conversion option information was not only misleading, it was incorrect. As explained above in the section on contribution holidays, a single Plan remains after the introduction of the defined contribution component and all Plan members remain beneficiaries of the Fund. Thus, conversion to the defined contribution component could not, of itself, wipe out such rights.

**151** Having found that the notice was misleading or incorrect or both, the Tribunal's determination that notice was adequate is unreasonable. None of the parties have addressed what is to follow from a finding by this court that inadequate notice of the conversion option was given - that matter is beyond the scope of this appeal. It may be that it becomes a matter for investigation by the Superintendent.

### c. Ought the Superintendent to be required to refuse registration of the 2000 Plan?

**152** The Tribunal declined to order the Superintendent to refuse to register the 2000 Plan text for three reasons:

1. the Superintendent found that adequate notice had been given;

2. the Act does not provide that failure to give the required notice of an adverse amendment results in the amendment being void or otherwise non-registerable; and
3. any deficiencies in the notice would not constitute sufficient grounds for the Superintendent to refuse registration of the 2000 Plan text.

**153** The Divisional Court overturned this decision. However, in my view, the Tribunal's decision meets the reasonableness standard of review, so there was no basis on which to overturn it. A review of the Tribunal's reasons explains my conclusion.

**154** At the time the Tribunal made its decision on this matter, the first reason was factually accurate and the Tribunal was entitled to consider it - the Superintendent did find that adequate notice had been given. Although I have found that adequate notice was not given, in light of the Tribunal's second and third reasons, discussed below, such a finding does not derogate from my view that the Tribunal's decision on this ought not to be disturbed.

**155** What of the second reason given by the Tribunal? Does failure to give adequate notice result in an amendment being non-registerable or void? Nothing in the Act so provides.

**156** Section 26(2) of the Act reads as follows:

> *If the Superintendent has required the administrator to transmit notices* under subsection (1), the Superintendent shall not register an amendment mentioned in that subsection before the expiration of forty-five days after the date certified to the Superintendent under that subsection, but *after the expiration of the forty-five day period the Superintendent may register the amendment* with such changes as are requested in writing by the administrator. [emphasis added]

**157** On a plain reading of s. 26(2), where notice of an adverse amendment has been required, the Superintendent has the discretion to register the amendment after the forty-five day period has elapsed. Nothing in this provision limits the Superintendent's power to register the amendment to situations in which adequate notice has been given.

**158** I would add that s. 18(1) (d) of the Act reinforces this plain reading of s. 26(2), namely, that the Superintendent has the power to register an amendment after the expiration of a forty-five day period even if inadequate notice was given.

**159** Section 18(1) (d) concerns void amendments. It reads as follows:

> 18(1) The Superintendent *may*,
>
> ...
>
> (d) refuse to register an amendment to a pension plan if the amendment is void or if the pension plan with the amendment would cease to comply with this Act and the regulations[.] [emphasis added]

**160** The language in this provision is, again, permissive. Although the Superintendent has the discretion to refuse to register a void amendment, he is not required to do so.

**161** Furthermore, in my opinion, there may be good reason for the Superintendent to register an amendment even if he is concerned that it may be invalid. Pension plan members rely on the Super-

intendent for complete information on the terms of their pension plan. The legality of plan provisions is often a difficult question that requires determination by an appropriate adjudicative body. The Superintendent might choose to register an amendment, even if inadequate notice was given or he has received comments that cause him to doubt its validity, because he wishes pension plan members to have access to as much information as possible about the terms of their plan. Based on that information, the pension plan members can take whatever steps they feel are necessary to protect their rights.

**162** In relation to the third reason given by the Tribunal, the Tribunal found that any shortcomings in the notice related only to information that might have affected a member's decision on whether to exercise the conversion option. It is apparent that the Tribunal did not view such shortcomings as sufficiently serious that it would cause the amended 2000 Plan text to cease to comply with the Act. Section 18(1) of the Act makes it clear that revocation of registration and refusal to register are based on that criterion[12]. As explained above, I view the inadequacies of the notice as being far more serious than did the Tribunal. However, the notice relates only to the conversion option. The conversion option is a single, discrete aspect of but one of the many amendments made in 2000. Accordingly, I view as reasonable the Tribunal's determination that the inadequacies in the notice did not cause the amended Plan text to cease to comply with the Act.

**163** Accordingly, considering the reasons as a whole given by the Tribunal on this matter, its decision to refuse to order the Superintendent to refuse registration of the amendment or the 2000 Plan is reasonable and ought not to be disturbed.

## 9. APPEAL AND CROSS-APPEAL IN RESPECT OF COST ORDERS

### *Overview*

**164** After the Tribunal rendered its decisions, the Committee asked the Tribunal for an order for its costs of the two hearings, payable either from the Fund or by Kerry. Kerry asked the Tribunal for an order requiring the Committee to pay its (Kerry's) costs of the hearings.

**165** In a decision dated December 24, 2004, the Tribunal unanimously declined to make any order as to costs. Further, a majority held that the Tribunal has jurisdiction only to order costs payable by a party to the proceeding. As the Fund was not a party to the proceeding, the majority held that the Tribunal did not have jurisdiction to order payment of costs out of the Fund. The minority held that the Tribunal had the power to order costs from a pension fund but that the circumstances did not warrant making such an order.

**166** By order dated May 31, 2006 (the "Costs Order"), the Divisional Court ordered that: (1) Kerry pay the Committee its costs of the second Tribunal hearing on a partial indemnity basis; (2) Kerry pay the Committee its costs of the appeals to the Divisional Court on a partial indemnity basis; and (3) Kerry, as the administrator of the Plan, pay the balance of the Committee's legal costs of the Divisional Court appeals from the Fund.

**167** On this appeal, Kerry asks that the Costs Order be set aside in its entirety. The second and third parts of the Costs Order are addressed below, in the Disposition section of these reasons. In the following section, I deal with the first issue, namely, costs ordered in favour of the Committee in

respect of the second Tribunal hearing, payable by Kerry. Thereafter, I deal with the costs issue raised by the Committee by way of cross-appeal: whether the Tribunal has the power to order costs payable from a pension fund.

## 10. COSTS OF THE SECOND TRIBUNAL HEARING

**168** It will be recalled that the Tribunal declined to make any costs order in respect of the two hearings. However, the Divisional Court set aside that order and ordered Kerry to pay the Committee's costs, on a partial indemnity basis, of the second Tribunal hearing.

**169** For the following reasons, I would allow the appeal on this issue and restore the Tribunal's order of no costs.

### *Standard of Review*

**170** An appellate court may interfere with a costs award made by a lower court only if the costs award is clearly wrong or the court made an error in principle: *Hamilton v. Open Window Bakery Ltd.*, [2004] 1 S.C.R. 303 at para. 27. The deference owed to the lower court reflects the fact that the award is an exercise of discretion and that the lower court, having heard the matter, is in the best position to exercise that discretion.

**171** I see no principled reason why the Divisional Court ought to review a costs order of the Tribunal on any other basis. That is, in reviewing the Tribunal's costs order, the Divisional Court ought only to interfere if the Tribunal's order is clearly wrong or the Tribunal acted on an error in principle.

**172** On that basis, I see nothing in the Tribunal's costs decision that warranted interference by the Divisional Court. As discussed below, the Tribunal's decision is in accordance with its published procedures; it reflects no error in principle. And, far from being plainly wrong, the decision is eminently fair and sensible. Indeed, the Divisional Court's reasons do not allude to any error made by the Tribunal in its decision on costs. As there was no basis to interfere with the Tribunal's cost decision, it was an error in principle for the Divisional Court to set it aside.

**173** There are cases which suggest that the Tribunal's cost order ought to be reviewed on a reasonableness standard[13]. If that standard is applied, as the order was reasonable, there was no basis for interference by the Divisional Court.

**174** Finally, even if the Divisional Court had been entitled to interfere with the Tribunal's cost award, as explained below, the costs award the Divisional Court made must be set aside as it is based on an error in principle.

### *Analysis*

**175** Section 91(1) of the Act gives a party to a proceeding before the Tribunal the right to appeal to the Divisional Court. Section 134(1)(a) of the *Courts of Justice Act*, R.S.O. 1990, c. C.43, empowers the Divisional Court to make any order or decision that the Tribunal could have made.

**176** As the Divisional Court gave no reasons for ordering Kerry to pay costs to the Committee for the second Tribunal hearing, I cannot know the basis for the order. I can only suppose that the Divisional Court awarded the Committee its costs of the second Tribunal hearing because the Committee enjoyed substantial success at the Divisional Court on the issues decided in the second Tribunal hearing.

**177** In my view, it was an error in principle to award costs at the Tribunal level solely on that basis. When the Divisional Court makes a costs award in respect of a tribunal hearing, it is standing in the shoes of the tribunal. Accordingly, the Divisional Court is obliged to consider and apply the rules governing costs under which the tribunal operates.

**178** Thus, the Divisional Court was obliged to consider the Tribunal rules on costs as part of its determination on whether costs at the Tribunal level should be ordered and, if so, the quantum of those costs. Accordingly, it was an error in principle for the Divisional Court to fail to consider costs in accordance with the criteria established by the Tribunal to govern costs awards and, instead, to award costs at the Tribunal level to the Committee based simply on the Committee's success on appeal.

**179** The power of the Tribunal to make costs orders is contained in s. 24 of the *Financial Services Commission of Ontario Act, 1997*, S.O. 1997, c. 28 (the "FSCO Act"). It reads as follows:

> 24(1) The Tribunal may order that a party to a proceeding before it pay the costs of another party or the Tribunal's costs of the proceeding[14].

**180** The Tribunal adopted procedural rules for proceedings before it. Those rules address the matter of costs. Further, the Tribunal issued a practice direction on costs. Both documents make it clear that costs of Tribunal proceedings are awarded primarily on considerations relating to the conduct of the parties, rather than on the degree of success enjoyed by a party. Having said that, I hasten to add that the Rules explicitly make result a relevant consideration.

**181** Rules 44.01 and 45.01 of the *Rules of Practice and Procedure for Proceedings before the Financial Services Tribunal* (August 1, 2004) (the "Rules"), are the relevant rules for the purpose of the present case. Those rules read as follows:

> 44.01 The Tribunal may, after considering submissions from a party that asked for an award of costs and the party or parties that may be subject to such an order, order the costs of a party be paid by another party or parties.
>
> 45.01 In determining whether a party is liable to pay the costs of a party, the Tribunal shall consider:
>
> (a) whether the party engaged in conduct which is clearly unreasonable, frivolous, or vexatious;
> (b) whether the party's conduct unreasonably delayed or prolonged the proceeding, including any failure to comply with undertakings or orders;
> (c) whether the party's participation assisted the Tribunal in understanding the issues;
> (d) failure to cooperate with other parties during preliminary proceedings or at the hearing;
> (e) failure to attend a hearing or other proceeding, or to send a representative, despite notice being provided to the party;
> (f) the party's degree of success in the proceeding; and
> (g) any other matter it considers relevant.

**182** The *Financial Services Tribunal Practice Direction on Costs Awards* (August 1, 2004) (the "Costs Practice Direction"), begins by stating that its purpose is to supplement and clarify Rules 44 through 47 of the Rules. Paragraph 2 of the Costs Practice Direction provides:

> 2. The Tribunal need not follow the civil court practice where the usual rule is that the unsuccessful party pays the successful party's costs. A party will not be subject to costs only because it has lost a hearing. The Tribunal is more likely to make a cost award against a party if it has engaged in conduct which is clearly unreasonable, frivolous, or vexatious. The Tribunal is less likely to make a cost award against a party that has been reasonable, cooperative, and helpful to the Tribunal.

**183** The Costs Practice Direction goes on to provide examples of conduct likely to be found to be unreasonable, frivolous or vexatious, and conduct that will be looked on favourably.

**184** Although the Tribunal had the power to award costs under s. 24(1) of the FSCO Act, it chose to make no such award. The Tribunal concluded that a case had not been made for an award of costs. As mentioned previously, I see no basis on which to interfere with this exercise of discretion by the Tribunal. It is clear from the Rules and the Costs Practice Direction that conduct of the parties is a central consideration when deciding whether to award costs. The Tribunal found nothing in the conduct of the parties that would lead to such an award. In light of the considerations governing costs orders of the Tribunal, in my view, the change in result on appeal to the Divisional Court does not warrant interference with the Tribunal's decision on costs and I would restore it.

## 11. JURISDICTION OF THE TRIBUNAL TO ORDER COSTS FROM A PENSION FUND

**185** By way of cross-appeal, the Committee seeks an order declaring that the Tribunal has jurisdiction to order that costs payable to parties in a proceeding before it be paid out of a pension trust fund.

**186** Rather than arguing this issue in its factum, the Committee relied on the factum it filed in the Divisional Court. The Committee did so because the "Divisional Court summarily and without any analysis dismissed the Committee's appeal on whether the Tribunal has the jurisdiction to award costs from the fund."

**187** Kerry argues that the Committee ought to be regarded as having abandoned its cross-appeal on this issue and that the Committee's act of filing its factum from the Divisional Court effectively circumvents this court's page limit for factums.

**188** It would have been preferable had the Committee addressed the merits of this issue in the usual fashion. However, as this matter was fully argued before the Tribunal and the Divisional Court and is of importance generally, I will deal with it nonetheless.

***Standard of Review***

**189** It seems readily apparent that this is a question of law and that the standard of review to be applied by the Divisional Court was that of correctness. Although the standard of review was not expressly averted to, it appears that the Divisional Court applied such a standard.

***Analysis***

**190** In para. 94 of the reasons for decision dated March 15, 2006, the Divisional Court concluded as follows:

> In our view, the majority of the Tribunal was correct in law when it held that it had no jurisdiction to order costs be paid to the Appellants [i.e. the Committee] out of the Trust Fund because the Tribunal, a statutory administrative tribunal, is not clothed with such statutory power by the Legislature.

**191** To say that these reasons are "summary" in nature and provide no analysis is to ignore the preceding paragraphs in this section of the reasons of the Divisional Court. In para. 93, the Divisional Court summarizes the reasoning of the majority of the Tribunal. The wording of para. 94 makes it clear that the Divisional Court adopted that summary. Hence, the reasons are adequate to explain the result: the Tribunal is a creature of statute and can only exercise the powers conferred on it by legislation. The Tribunal was given the authority to award costs payable by a party. The Fund was not a party to the proceedings; hence, the Tribunal did not have the power to award costs payable from the Fund.

**192** A plain reading of s. 24(1) of the FSCO Act, set out above, supports the Divisional Court's conclusion. Section 24(1) empowers the Tribunal to order one party in a proceeding to pay the costs of another party to the proceeding. In the instant case, the Tribunal could not order that costs be paid from the Fund because the Fund was not a party to the proceeding. The fact that Kerry is the administrator of the Plan does not make the Fund a party in the proceedings.

**193** While it may seem unfair that pension plan members have no statutory right to fund litigation before the Tribunal from the pension fund, employers also have no such right. Policy considerations cannot override the clear terms of the statute. In any event, there are valid policy considerations for not providing access to a pension fund for the purpose of funding legal proceedings. One such consideration is that the causes pursued by litigating plan members may not be in the interests of the membership as a whole. In the present case, one of the reasons of the minority of the Tribunal for refusing to award costs was that there was insufficient evidence of the level of support for the actions of the Committee from the Plan membership. Another consideration is that the solvency of the pension plan could be adversely affected if such funding were permissible.

## 12. DISPOSITION

**194** Accordingly, I would allow the appeal and:

(1) set aside the judgment of the Divisional Court in respect of Plan expenses and contribution holidays and restore the Tribunal decisions dated March 4, 2004, and September 1, 2004; and,
(2) set aside the Costs Order of the Divisional Court.

**195** I would dismiss the cross-appeal.

**196** Kerry seeks its costs of the appeals to the Divisional Court and of this appeal and cross-appeal. It asks for an order requiring the Committee or, alternatively, the Fund to pay such costs on a substantial indemnity basis. As Kerry has been successful, it is *prima facie* entitled to costs both in this court and before the Divisional Court.

**197** Before deciding the matter of costs, however, and in accordance with the wishes of the parties, the court will accept written submissions on what party or parties are entitled to costs, from what source or sources, and on what scale. In particular, the submissions should address: whether this court has the power to order costs from a pension fund; if so, whether it ought to order that costs be paid from the Fund for the appeals to the Divisional Court and/or this court; whether, given the novelty of the issues and the role of the Committee which, arguably, sought to ensure the due administration of the Fund, the Committee ought to be awarded costs either at the Divisional Court or here or both; and, on what scale costs ought to be awarded.

**198** Accordingly, if the parties are unable to agree on the disposition of costs of the Divisional Court appeals and this appeal and cross-appeal, they shall make written submissions on the same within twenty-one days of the date of release of these reasons.

E.E. GILLESE J.A.
J.I. LASKIN J.A.:-- I agree.
P.S. ROULEAU J.A.:-- I agree.

cp/e/qlhjk/qljjn/qlcas

1 The company is identified as DCA Food Industries Ltd. in the plan text, but as the Canadian Doughnut Company Ltd. in the trust agreement creating the fund.

2 The Deputy Superintendent, acting as the Superintendent's delegate, issued both Notices of Proposal.

3 Although *Lévis* involved an application for judicial review of a labour arbitrator's decision, the breadth of the language in the reasons indicates that the principles articulated apply also to the review of tribunal decisions.

4 See *Baxter v. Ontario (Superintendent of Financial Services)* (2004), 192 O.A.C. 293 (Div. Ct.) to the same effect and for an excellent consideration of the standard of review of Tribunal decisions following the decision of the Supreme Court of Canada in *Monsanto*.

5 The first factor, as explained in the preceding section, does not.

6 (2002), 213 D.L.R. (4th) 362 at 369 - 70 and 372 - 73 *sub nom. Metropolitan Toronto Pension Plan (Trustees of) v. Toronto (City)*.

7 The Trust agreement provides that the Fund beneficiaries are those persons designated by the Plan and the Plan permits the company to designate Plan members. Thus, there is no impediment to the company so designating the Part 2 members.

8 It will be recalled that all Part 2 members except those joining the company after January 1, 2000, had been members of the Plan and Fund and had elected to transfer their entitlement from the defined benefit component to the defined contribution component of the Plan.

9 At para. 9 of the reasons, the Divisional Court stated that the standard of review for a decision of the Tribunal that involved the exercise of discretion was that of reasonableness. However, it is unclear which, if any, of the Tribunal's decisions were reviewed on that standard.

10 It is interesting to note that FSCO requires that notice be given because a conversion "alters the fundamental pension agreement between the employer and the plan members." See Financial Services Commission of Ontario Policy C200-101, "Conversion of a Plan from Defined Benefit to Defined Contribution" (effective June 1, 2004).

11 Section 22(1) reads as follows:

> The administrator of a pension plan shall exercise the care, diligence and skill in the administration and investment of the pension fund that a person of ordinary prudence would exercise in dealing with the property of another person.

12 18(1) The Superintendent may,

> (a) refuse to register a pension plan that does not comply with this Act and the regulations;
>
> (b) revoke the registration of a pension plan that does not comply with this Act and the regulations;
>
> (c) revoke the registration of a pension plan that is not being administered in accordance with this Act and the regulations;
>
> (d) refuse to register an amendment to a pension plan if the amendment is void or if the pension plan with the amendment would cease to comply with this Act and the regulations;
>
> (e) revoke the registration of an amendment that does not comply with this Act and the regulations.

13 See *Creager v. Provincial Dental Board of Nova Scotia* (2005), 230 N.S.R. (2d) 48 (C.A.) and *Brand v. College of Physicians and Surgeons (Saskatchewan)* (1990), 86 Sask. R. 18, 72 D.L.R. (4th) 446 (C.A.).

14 Although s. 17.1 of the *Statutory Powers Procedure Act*, R.S.O. 1990, c. S.22, as am. by S.O. 2006, c. 19, Sch. B, s. 21(2) (the "SPPA"), generally circumscribes the power of administrative tribunals to order costs, s. 17.1(6) creates an exception for costs orders made in accordance with the tribunal's enabling legislation so long as that legislation was in force on February 14, 2000. The FSCO Act meets that test. Therefore, the Tribunal was not circumscribed by s. 17.1 of the SPPA when making its costs decision.

# Tab 2

# 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 other Applicants listed in Schedule "A" Application under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 as amended

**[Indexed as: Stelco Inc. (Re )]**
**[* Editor's note: Schedule "A" was not attached to the copy received from the Court and therefore is not included in the judgment.]**

75 O.R. (3d) 5

[2005] O.J. No. 1171

Docket: M32289

Court of Appeal for Ontario,

**Goudge, Feldman and Blair JJ.A.**

March 31, 2005

*Corporations -- Directors -- Removal of directors -- Jurisdiction of court to remove directors -- Restructuring supervised by court under Companies' Creditors Arrangement Act -- Supervising judge erring in removing directors based on apprehension that directors would not act in best interests of corporation -- In context of restructuring, court not having inherent jurisdiction to remove directors -- Removal of directors governed by normal principles of corporate law and not by court's authority under s. 11 of Companies' Creditors Arrangement Act to supervise restructuring -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.*

*Debtor and creditor -- Arrangements -- Removal of directors -- Jurisdiction of court to remove directors -- Restructuring supervised by court under the Companies' Creditors Arrangement Act -- Supervising judge erring in removing directors based on apprehension that directors would not act in best interests of corporation - In context of restructuring, court not having inherent jurisdiction to remove directors -- Removal of directors governed by normal principles of corporate law and not by court's authority under s. 11 of Companies' Creditors Arrangement Act to supervise restructuring -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 11.*

On January 29, 2004, Stelco Inc. ("Stelco") obtained protection from creditors under the Companies' Creditors Arrangement Act ("CCAA"). Subsequently, while a restructuring under the CCAA was under way, Clearwater Capital Management Inc. ("Clearwater") and Equilibrium Capital Management Inc. ("Equilibrium") acquired a 20 per cent holding in the outstanding publicly traded common shares of Stelco. Michael Woollcombe and Roland Keiper, who were associated with Clearwater and Equilibrium, asked to be appointed to the Stelco board of directors, which had been depleted as a result of resignations. Their request was supported by other shareholders who, together with Clearwater and Equilibrium, represented about 40 per cent of the common shareholders. On February 18, 2005, the Board acceded to the request and Woollcombe and Keiper were appointed to the Board. On the same day as their appointments, the board of directors began consideration of competing bids that had been received as a result of a court-approved capital raising process that had become the focus of the CCAA restructuring.

The appointment of Woollcombe and Keiper to the Board incensed the employees of Stelco. They applied to the court to have the appointments set aside. The employees argued that there was a reasonable apprehension that Woollcombe [page6] and Keiper would not be able to act in the best interests of Stelco as opposed to their own best interests as shareholders. Purporting to rely on the court's inherent jurisdiction and the discretion provided by the CCAA, on February 25, 2005, Farley J. ordered Woollcombe and Keiper removed from the Board.

Woollcombe and Keiper applied for leave to appeal the order of Farley J. and if leave be granted, that the order be set aside on the grounds that (a) Farley J. 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 had no application to the removal of directors, (c) he had erred in interfering with the exercise by the Board of its business judgment in filling the vacancies on the Board, and (d) in any event, the facts did not meet any test that would justify the removal of directors by a court.

Held, leave to appeal should be granted, and the appeal should be allowed.

The appeal involved the scope of a 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 of the CCAA. In particular, it involved the court's power, if any, to make an order removing directors under s. 11 of the CCAA. The order to remove directors could not be founded on inherent jurisdiction. Inherent jurisdiction is a power derived from the very nature of the court as a superior court of law, and it permits the court to maintain its authority and to prevent its process from being obstructed and abused. However, inherent jurisdiction does not operate where Parliament or the legislature has acted and, in the CCAA context, 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 supplanted the need to resort to inherent jurisdiction. A judge is general ly 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 was designed to supervise the company's process, not the court's process.

The issue then was the nature of the court's power under s. 11 of the CCAA. The s. 11 discretion is not open-ended and unfettered. Its exercise was guided by the scheme and object of the Act and by the legal principles that govern corporate law issues. What the court does under s. 11 is 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. In the course of acting as referee, the court has authority 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. The court is not entitled to usurp the role of the directors and management in conducting what are in substance the company's restructurin g efforts. 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. 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.

The matters relating to the removal of directors did not fall within the court's discretion under s. 11. The fact that s. 11 did not itself provide the authority for a CCAA judge to order the removal of directors, however, did not mean that the supervising judge was powerless to make such an order. Section 20 of the CCAA offered a gateway to the oppression remedy and other provisions of the Canada [page7] Business Corporations Act, R.S.C. 1985, c. C-44 ("CBCA") and similar provincial statutes. 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.

Court removal of directors is an exceptional remedy and one that is rarely exercised in corporate law. In determining whether directors have fallen foul of their obligations, 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. The evidence in this case was far from reaching the standard for removal, and the record would not support a finding of oppression, even if one had been sought. The record did not support a finding that there was a sufficient risk of misconduct to warrant a conclusion of oppression. Further, Farley J.'s borrowing the administrative law notion of apprehension of bias was foreign to the principles that govern the election, appointment and removal of directors and to corporate governance considerations in general. There was nothing in the CBCA or other corporate legislation that envisaged the screening of directors in advance for their ability to a ct neutrally, in the best interests of the corporation, as a prerequisite for appointment. The issue to be determined was not whether there was a connection between a director and other shareholders or stakeholders, but rather whether there was some conduct on the part of the director that would justify the imposition of a corrective sanction. An apprehension of bias approach did not fit this sort of analysis.

For these reasons, Farley J. erred in declaring the appointment of Woollcombe and Keiper as directors of Stelco of no force and effect, and the appeal should be allowed.

Cases referred to

Alberta Pacific Terminals Ltd. (Re), [1991] B.C.J. No. 1065, 8 C.B.R. (3d) 99 (S.C.); Algoma Steel Inc. (Re), [2001] O.J. No. 1943, 147 O.A.C. 291, 25 C.B.R. (4th) 194 (C.A.); Algoma Steel Inc. v. Union Gas Ltd. (2003), 63 O.R. (3d) 78, [2003] O.J. No. 71, 39 C.B.R. (4th) 5 (C.A.), revg in part [2001] O.J. No. 5046, 30 C.B.R. (4th) 163 (S.C.J.); Babcock & Wilcox Canada Ltd. (Re) [2000] O.J. No. 786, 18 C.B.R. (4th) 157, 5 B.L.R. (3d) 75 (S.C.J.); Baxter Student Housing Ltd. v. College Housing Co-operative Ltd., [1976] 2 S.C.R. 475, 57 D.L.R. (3d) 1, 5 N.R. 515, [1976] 1 W.W.R. 1, 20 C.B.R. (N.S.) 240; Blair v. Consolidated Enfield Corp., [1995] 4 S.C.R. 5, [1995]

S.C.J. No. 29, 25 O.R. (3d) 480n, 128 D.L.R. (4th) 73, 187 N.R. 241, 24 B.L.R. (2d) 161; Brant Investments Ltd. v. KeepRite Inc. (1991), 3 O.R. (3d) 289, [1991] O.J. No. 683, 45 O.A.C. 320, 80 D.L.R. (4th) 161, 1 B.L.R. (2d) 225 (C.A.); Catalyst Fund General Partne r I Inc. v. Hollinger Inc., [2004] O.J. No. 4722, 1 B.L.R. (4th) 186 (S.C.J.); Chef Ready Foods Ltd. v. Hongkong Bank of Canada, [1990] B.C.J. No. 2384, 51 B.C.L.R. (2d) 84, [1991] 2 W.W.R. 136, 4 C.B.R. (3d) 311 (C.A.); Clear Creek Contracting Ltd. v. Skeena Cellulose Inc. [2003] B.C.J. No. 1335, 43 C.B.R. (4th) 187, 2003 BCCA 344, 13 B.C.L.R. (4th) 236 (C.A.); Country Style Foods Services Inc. (Re), [2002] O.J. No. 1377, 158 O.A.C. 30 (C.A.); Dylex Ltd. (Re), [1995] O.J. No. 595, 31 C.B.R. (3d) 106 (Gen. Div.); Ivaco Inc. (Re), [2004] O.J. No. 2483, 3 C.B.R. (5th) 33 (S.C.J.); Lehndorff General Partner Ltd. (Re), [1993] O.J. No. 14, 9 B.L.R. (2d) 275, 17 C.B.R. (3d) 24 (Gen. Div.); London Finance Corp. Ltd. v. Banking Service Corp. Ltd., [1922] O.J. No. 378, 23 O.W.N. 138 (H.C.); Olympia & York Developments Ltd. (Re) (1993), 12 O.R. (3d) 500, [1993] O.J. No. 545, 17 C.B.R. (3d) 1 (Gen. Div.) (sub nom. Olympia & York Dev. v. Royal Trust Co.); Peoples Department Stores Inc. (Trustee of) v. Wise, [2004] 3 S.C.R. 461, [2004] S.C.J. No. 64, 244 D.L.R. (4th) 564, 2004 SCC 68, 49 B.L.R. (3d) 165, 4 C.B.R. (5th) 215; R. v. Sharpe, [2001] 1 S.C.R. 45, [2001] [page8] S.C.J. No. 3, 88 B.C.L.R. (3d) 1, 194 D.L.R. (4th) 1, [2001] 6 W.W.R. 1, 86 C.R.R. (2d) 1, 150 C.C.C. (3d) 321, 39 C.R. (5th) 72, [2001] SCC 2; Richtree Inc. (Re) (2005), 74 O.R. (3d) 174, [2005] O.J. No. 251, 7 C.B.R. (5th) 294 (S.C.J.); Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27, [1998] S.C.J. No. 2, 36 O.R. (3d) 418n, 154 D.L.R. (4th) 193, 221 N.R. 241, 50 C.B.R. (3d) 163, 33 C.C.E.L. (2d) 173, 98 CLLC 210-006 (sub nom. Ontario Ministry of Labour v. Rizzo & Rizzo Shoes Ltd., Adrien v. Ontario Ministry of Labour); Royal Oak Mines Inc. (Re), [1999] O.J. No. 864, 7 C.B.R. (4th) 293, 96 O.T.C. 279 (Gen. Div.); Sammi Atlas Inc. (Re), [1998] O.J. No. 1089, 3 C.B.R. (4th) 171 (Gen. Div.); Stephenson v. Vokes (1896), 27 O.R. 691, [1896] O.J. No. 191 (H.C.J.); Westar Mining Ltd. (Re), [1992] B.C.J. No. 1360, 14 C.B.R. (3d) 88, 70 B.C.L.R. (2d) 6, [1992] 6 W.W.R. 331 (S.C.)

Statutes referred to

Canada Business Corporations Act, R.S.C. 1985, c. C-44, ss. 2 [as am.], 102 [as am.], 106(3) [as am], 109(1) [as am.], 111 [as am.], 122(1) [as am.], 145 [as am.], 241 [as am.]

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, ss. 11 [as am.], 20 [as am.]

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APPLICATION for leave to appeal and, if leave is granted, an appeal from the order of Farley J., reported at [2005] O.J. No. 729, 7 C.B.R. (5th) 307 (S.C.J.), removing two directors from the board of directors of Stelco Inc.

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

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

Murray Gold and Andrew J. Hatnay, for 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 Active Salaried Employee Representative.

Michael Barrack, for Stelco Inc.

Peter Griffin, for Board of Directors of Stelco Inc.

K. Mahar, for Monitor.

David R. Byers, for CIT Business Credit, Agent for DIP Lender. [page9]

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The judgment of the court was delivered by

**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 (the "CCAA")[1 at the end of the document] 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 per cent 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 per cent 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 [page10] 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. [page11]

[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 11 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 20 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 [page12 ]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 five per cent as at November 19, to 14.9 per cent as at January 25, 2005, and finally to approximately 20 per cent 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 other 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 per cent of the company's common shares. [page13]

[19] At paras. 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 per cent 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 [page14] 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] O.J. No. 1377, 158 O.A.C. 30 (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 [page15] 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 e vident 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, second, that it threatens to undermine the even-handedness and integrity of the capital raising process, thus jeopardizing the [page16] 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: Re Algoma Steel Inc., [2001] O.J. No. 1943, 25 C.B.R. (4th) 194 (C.A.), at para. 8.

[29] The crux of the respondents' concern is well-articulated in the following excerpt from para. 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 Re Olympia & York Development Ltd. (1993), 12 O.R. (3d) 500, [1993] O.J. No. 545 (Gen. Div.); Re Ivaco Inc., [2004] O.J. No. 2483, 3 C.B.R. (5th) 33 (S.C.J.), at paras. 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, 5 B.L.R. (3d) 75 (S.C.J.), at para. 11. See also, Chef Ready Foods Ltd. v. Hong Kong Bank of Canada, [1990] B.C.J. No. 2384, 4 C.B.R. (3d) 311 (C.A.), at p. 320 C.B.R.; Re Lehndorff General Partners Ltd., [1993] O.J. No. 14, 17 C.B.R. (3d) 24 (Gen. Div.). [page17 ]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] O.J. No. 595, 31 C.B.R. (3d) 106 (Gen. Div. (Commercial List)), Royal Oak Mines Inc. (Re), [1999] O.J. No. 864, 7 C.B.R. (4th) 293 (Gen. Div. (Commercial List); and Westar Mining Ltd. (Re), [1992] B.C.J. No. 1360, 70 B.C.L.R. (2d) 6 (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: LexisNexis UK, 1973 -- ), vol. 37, at para. 14, the concept is described as follows:

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

[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 [page18] not be brought into play" (para. 4). See also, Baxter Student Housing Ltd. v. College Housing Co-operative Ltd., [1976] 2 S.C.R. 475, 57 D.L.R. (3d) 1, at p. 480 S.C.R.; Richtree Inc. (Re) (2005), 74 O.R. (3d) 174, [2005] O.J. No. 251 (S.C.J.).

[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, 43 C.B.R. (4th) 187 (C.A.), 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] at the end of the docuemnt], 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 [page19 ]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] at the end fo the document]. 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 Canada Business Corporation Act, R.S.C. 1985, c. C-44 ("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 gr ounds.

[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); [page20]
> (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, [2001] S.C.J. No. 3, at para. 33, and Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27, [1998] S.C.J. No. 2, 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 p. 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 [page21 ]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 subparas. 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 Corp. Ltd. v. Banking Service Corp. Ltd., [1922] O.J. No. 378, 23 O.W.N. 138 (H.C.); Stephenson v. Vokes, [1896] O.J. No. 191, 27 O.R. 691 (H.C.J.). 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: [page22] CBCA, ss. 106(3) and 111[4] at the end of the document]. 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, 1 B.L.R. (4th) 186 (S.C.J.).

[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 S.C.R.; Royal Oak Mines Inc. (Re), supra; and Richtree Inc. (Re), supra.

[49] At para. 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 [page23] 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:

> 20. 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. [page24 ]

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] at the end of the document]

> 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. [page25]

[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] 3 S.C.R. 461, [2004] S.C.J. No. 64, 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 [page26 ]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 14 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 Ltd. (2003), 63 O.R. (3d) 78, [2003] O.J. No. 71 (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 ... [page27]

[66] In Brant Investments Ltd. v. KeepRite Inc. (1991), 3 O.R. (3d) 289, [1991] O.J. No. 683 (C.A.), at p. 320 O.R., 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] at the end of the document]

[67] McKinlay J.A. then went on to say [at p. 320 O.R.]:

> There can be no doubt that on an application under s. 234[7] at the end of the document] 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] O.J. No. 1089, 3 C.B.R. (4th) 171 (Gen. Div.); Olympia & York Developments Ltd. (Re), supra; Re Alberta Pacific Terminals Ltd., [1991] B.C.J. No. 1065, 8 C.B.R. (4th) 99 (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 [page28 ]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. 2 of the CBCA as meaning "the relationships among a corporation, its 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 [page29] 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 di rectors.

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 aebias' 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 per cent 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 [page30 ]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, [1995] S.C.J. No. 29, 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.

Order accordingly.

[page31]

Notes

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

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

Note 3: See para. 43, infra, where I elaborate on this decision.

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

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

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

Note 7: Now s. 241.

# Tab 3

*Case Name:*

# Canadian Union of Public Employees, Locals 1712, 3009, 2225-05, 2225-06 and 2225-12 v. Royal Crest Lifecare Group Inc. (Trustee of)

**IN THE MATTER OF the Bankruptcy of the Royal Crest Lifecare Group Inc.**
**Between**
**Canadian Union of Public Employees, Locals 1712, 3009, 2225-05, 2225-06 and 2225-12, and Service Employees International Union, Locals 204 and 532, appellants, and Ernst & Young Inc., in its capacity as Trustee in Bankruptcy for the Royal Crest Lifecare Group Inc., Confederation Life Insurance Company, in liquidation and the National Life Assurance Company of Canada, respondents, and Attorney General of Ontario, intervenor**

[2004] O.J. No. 174

98 C.L.R.B.R. (2d) 210

181 O.A.C. 115

46 C.B.R. (4th) 126

[2004] CLLC para. 220-014

128 A.C.W.S. (3d) 212

2004 CarswellOnt 190

Docket No. C39457

Ontario Court of Appeal
Toronto, Ontario

**Borins, MacPherson and Cronk JJ.A.**

Heard: September 17, 2003.
Judgment: January 21, 2004.

(74 paras.)

*Labour law -- Labour relations boards and judicial review -- Boards, jurisdiction -- Successor rights and obligations -- Bankruptcy -- Practice -- Actions, commencement of -- Preliminary matters -- Leave to commence action.*

Appeal by the Canadian Union of Public Employees from the dismissal of its application. The respondent Royal Crest Lifecare Group operated several nursing and retirement homes. It was petitioned into bankruptcy after it defaulted under its loan agreements. The trustee applied for an order that it was not bound by the collective agreements between Royal and the Union. It also sought an order that it not be deemed a successor employer under the Labour Relations Act. The Union applied for leave to pursue an application before the Ontario Labour Relations Board for the trustee to be designated as a successor employer. Both applications were dismissed. The bankruptcy judge considered the applications to be premature. The trustee did not appeal.

HELD: Appeal dismissed. The judge did not apply the wrong test under section 215 of the Bankruptcy and Insolvency Act. He considered that there was no evidentiary basis for the proposed application. There was evidence to support the judge's conclusion that the applications were premature. The judge did not decide the successor employer issue, which was within the exclusive jurisdiction of the Board. He did not decide this issue on its merits as he merely dismissed the applications.

**Statutes, Regulations and Rules Cited:**

Bankruptcy Act, s. 186.

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 46, 72(1), 215.

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

Courts of Justice Act, R.S.O. 1990, c. C-43, ss. 101, 109.

Employment Standards Act, S.O. 2000, c. 41.

Human Rights Code, R.S.O. 1990, c. H-19.

Labour Relations Act, S.O. 1995, c. 1, Sch. A., s. 69, 69(1), 69(2), 69(12), 114(1).

Occupational Health and Safety Act, R.S.O. 1990, c. O-1.

Pay Equity Act, R.S.O. 1990, c. P-7.

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

Pension Benefits Standards Act, R.S.C. 1985, c. 32.

Workplace Safety and Insurance Act, S.O. 1997, c. 16, Sch. A.

**Appeal From:**

On appeal from the order of Justice James M. Farley of the Superior Court of Justice dated January 16, 2003, reported at (2003), 40 C.B.R. (4th) 146.

**Counsel:**

Sean Dewart and Michael Kainer, for the appellants.
John A. MacDonald, for the respondent, Ernst & Young.
Harold P. Rolph, for independent counsel, for the trustee.
L. Joseph Latham and Joseph K. Morrison, for the respondent, Confederation Life.
Kyla E.M. Mahar, for the respondent, National Life.
Robin K. Basu, for the intervenor.

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Reasons for judgment were delivered by MacPherson J.A., concurred in by Cronk J.A. Separate reasons were delivered by Borins J.A.

**MacPHERSON J.A.**:--

A. INTRODUCTION

**1** On January 10, 2003, a large group of related companies collectively known as The Royal Crest Lifecare Group Inc. ("Royal Crest"), which operated five nursing homes, six retirement homes and six mixed care (nursing and retirement) homes in southern Ontario, was petitioned into bankruptcy by several banks after it defaulted under its loan agreements with the banks. Ernst & Young Inc. ("Ernst & Young") was appointed as trustee of the estate of the bankrupt.

**2** On the same day, and before the same judge, Farley J., who made the bankruptcy order, the trustee and the unions representing many of the employees of the bankrupt company brought duelling motions.

**3** The trustee sought an order that it not be bound by the collective agreements between Royal Crest and the unions and that it not be deemed to be a successor employer under the Labour Relations Act, S.O. 1995, c. 1, Sch. A. (the "LRA"), and other labour and employment laws.

**4** The unions resisted the trustee's motion. In addition, based on their view that the question of successor employer' came within the exclusive jurisdiction of the Ontario Labour Relations Board (the "OLRB"), the unions made a cross-motion before the bankruptcy judge. In their cross-motion, the unions sought leave, pursuant to s. 215 of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 (the "BIA"), to pursue an application before the OLRB seeking the designation of the trustee as a successor employer.

**5** The bankruptcy judge dismissed the trustee's motion. The trustee does not appeal.

**6** The bankruptcy judge also dismissed the unions' cross-motion, but "without prejudice to such a motion being brought back on again with appropriate factual underpinning". The unions appeal.

B. THE FACTS

(1) The parties and the events

**7** Royal Crest operated 17 long-term care facilities in Southern Ontario. These homes provided approximately 2300 beds for patients and residents. Royal Crest employed about 2200 full-time and part-time employees. Canadian Union of Public Employees Locals 1712, 3009, 2225-05, 2225-06 and 2225-12 and Service Employees International Union Locals 204 and 532 (the "unions") represent approximately 1400 of these employees.

**8** Unfortunately, by late 2002 Royal Crest was in serious financial difficulty. It owed its creditors, mostly banks, in excess of $128 million and was in default under its loan agreements.

**9** On October 21, 2002, Royal Crest was granted protection under the Companies Creditors Arrangement Act, R.S.C. 1985, c. C-36 (the "CCAA") by order of Crane J. On November 13, 2002, the proceedings under the CCAA were terminated and Ernst & Young was appointed as interim receiver pursuant to s. 46 of the BIA. The interim receiver immediately engaged the former employees under terms and conditions of employment similar, but not identical, to those provided in the various collective agreements. One of the terms of employment to which the employees had to agree was that they accepted that Ernst & Young was not a successor employer.

**10** On January 10, 2003, Royal Crest was petitioned into bankruptcy. Ernst & Young was appointed as trustee.

(2) The litigation

(a) Before the bankruptcy judge

**11** On January 10, 2003, the trustee and the unions brought their duelling or mirror motions on the question of whether the trustee should be deemed to be a successor employer within the meaning of s. 69 of the LRA.

**12** The bankruptcy judge dismissed the trustee's motion. He reviewed considerable case law, much of it conflicting. It seems clear from his reasons that he doubted two of the propositions advanced by the trustee: (1) a trustee in bankruptcy cannot be a successor employer; and (2) collective agreements terminate with bankruptcy. All that the bankruptcy judge was prepared to order, consistent with Re Rizzo & Rizzo Shoes Ltd., [1998] 1 S.C.R. 27, was:

> This Court orders that the employment of all employees engaged by the Interim Receiver is terminated by virtue of the bankruptcy. The Trustee is hereby authorized to engage any or all of such former employees of the Bankrupt or any other persons.

The trustee does not appeal this component of the bankruptcy judge's order.

**13** The bankruptcy judge also dismissed the unions' cross-motion. Again, the bankruptcy judge conducted a full review of the relevant legislation and case law. He concluded:

> There has been no allegation, let alone evidence, that the Trustee here (even if one were to consider E & Y Inc. in its capacity as IR) has been dragging its feet or will do so. The CUPE cross-motion for leave is dismissed without prejudice to such a motion being brought back on again with appropriate factual underpinning

which I would be of the view ought to demonstrate that the Trustee has slipped over from functioning qua realizor of assets in a diligent fashion to the role of being predominantly an employer in its activities.

The unions appeal the bankruptcy judge's decision relating to their cross-motion.

(b) The appeal

**14** The appeal is unusual in an important respect. Most appeals involve the same parties, issues and arguments that were before the trial, application or motion judge. To some extent, that is true of this appeal. Some of the matters that were before the bankruptcy judge, and which he resolved, are raised again on appeal.

**15** However, significant attention was devoted on the appeal (in facta and in oral argument) to an issue that was invisible, or almost invisible, in the hearing before the bankruptcy judge. The issue is the relationship, in constitutional law terms, between the federal BIA and the Ontario LRA.

**16** The appellants raised the purported constitutional issue in their factum by framing the first issue of the appeal as:

(a) Did the learned bankruptcy judge err in effectively finding a conflict between the provisions of the Bankruptcy and Insolvency Act and the Labour Relations Act, 1995, where none in fact exists?

**17** Rather than ignore the fact that the appellants' argument appeared to be put no higher than the assertion that the bankruptcy judge had made an implicit determination of a constitutional issue raised by no one, the respondent trustee decided to mount a full-scale attack on the applicability of the successor employer provisions of the LRA in a bankruptcy context. The trustee served a Notice of Constitutional Question upon the Attorney General of Canada and the Attorney General of Ontario, pursuant to s. 109 of the Courts of Justice Act, R.S.O. 1990, c. C.43.

**18** The Attorney General of Ontario intervened in the appeal. He noted that no Notice of Constitutional Question was served in the proceedings before the bankruptcy judge and, consequently, he had no opportunity to participate in those proceedings.

**19** During the appeal hearing, the panel permitted the appellants and the trustee to make their constitutional arguments. However, at the conclusion of these submissions, the panel indicated that it did not need to hear further submissions on this issue, including submissions from the Attorney General who had filed an extensive factum on the purported constitutional issue. The panel essentially agreed with the Attorney General's submissions that: (1) the constitutional issue was not raised before, or addressed or determined by, the bankruptcy judge; and (2) the appeal could, and should, be determined without the necessity of dealing with the constitutional issue.

C. ISSUE

**20** The sole issue on the appeal is whether the bankruptcy judge erred in the exercise of his discretion by refusing to permit the unions to proceed, on January 10, 2003, to the OLRB to have the question of the status of the trustee as successor employer resolved.

D. ANALYSIS

(1) The standard of review

**21** A bankruptcy is a disaster. A company has failed; in many cases it will not survive. Creditors, who provided goods and services in good faith, may lose substantial sums of money. Employees of the bankrupt company instantly lose their jobs.

**22** The bankruptcy judge is thrown into the middle of the disaster. The judge will need to make important decisions that will affect the future of the company, creditors and employees. The qualities of a good bankruptcy judge are therefore expertise, sensitivity and speed.

**23** Appellate courts have long recognized the unique difficulties faced by judges in bankruptcy and CCAA proceedings. The result is that appellate courts accord considerable deference to judges' decisions in these contexts: see, for example, Re Algoma Steel Inc., [2001] O.J. No. 1943 (C.A.); Banque National de Paris (Canada) v. Opiola, [2001] 6 W.W.R. 95 (Alta. C.A.); and Ford Credit Canada Ltd. v. Fred Walls & Sons Holdings Ltd., [2003] B.C.J. No. 454 (C.A.).

(2) The test under s. 215 of the BIA

**24** The LRA gives the OLRB exclusive jurisdiction to decide successor employer applications: see ss. 69(12), 114 and 116. However, in bankruptcy proceedings, a party seeking to challenge a decision by a trustee must seek leave from a judge. Section 215 of the BIA provides:

> 215. Except by leave of the court, no action lies against ... a trustee with respect to any report made under, or any action taken pursuant to, this Act.

The appellants acknowledge that they require the leave of the court in order to pursue their application to the OLRB.

**25** The case law establishes that the threshold for granting leave under s. 215 of the BIA is a low one. In Society of Composers, Authors and Music Publishers of Canada v. Armitage (2000), 50 O.R. (3d) 688 at 690 (C.A.) ("SOCAN"), Charron J.A. stated:

> [T]he evidence required to support an order under s. 215 must be sufficient to establish that there is a factual basis for the proposed claim and that the proposed claim discloses a cause of action. However, the evidence does not have to be sufficient to enable the motions judge to make a final assessment of the merits of the proposed claim. The sufficiency of the evidence must be measured in the context of the purpose of s. 215 which is to prevent the trustee from having to respond to actions which are frivolous or vexatious or which do not disclose a cause of action ...

See also: Mancini (Bankrupt) et al. v. Falconi et al. (1993), 61 O.A.C. 332 and Vanderwoude et al. v. Scott and Pichelli Ltd. et al. (2001), 143 O.A.C. 195.

(3) Discussion

**26** The appellants contend that the bankruptcy judge made three errors in his reasons relating to their cross-motion: (1) he applied the wrong test for a BIA s. 215 application; (2) he determined a matter - whether the trustee was a successor employer - within the exclusive jurisdiction of the

OLRB; and (3) he incorrectly found that the various collective agreements were in "suspended animation".

**27** I do not agree that the bankruptcy judge applied the wrong test. The cross-motion was directly related to s. 215 of the BIA and the relevant case law was argued before the bankruptcy judge. It is true that the test under s. 215 of the BIA establishes a low threshold for granting leave. However, SOCAN makes it clear that there must be an evidentiary basis for the proposed cause of action.

**28** The bankruptcy judge clearly turned his mind to this component of the test. In dismissing the cross-motion, he invited the unions to bring a further motion "with appropriate factual underpinning".

**29** It is important to place the appellants' cross-motion in its proper context. Prior to January 10, 2003, there was no live successor employer issue because Ernst & Young, acting as interim receiver, engaged current employees only if they contractually agreed that Ernst & Young was not a successor employer. On January 10, 2003, this picture changed in a major way. When receiving orders were made and Ernst & Young was appointed as trustee of the estate of Royal Crest, the status of the trustee as a potential successor employer emerged as a live issue because the existing employment relation was automatically terminated: see Re Rizzo & Rizzo Shoes Ltd., supra. Both the trustee and the unions decided, virtually instantaneously, to resort to their preferred institutions, the court and the OLRB respectively, to resolve the issue.

**30** It is clear that the bankruptcy judge regarded both motions as premature. In my view, this conclusion was amply supported by the chronology of events and the record before the bankruptcy judge.

**31** The trustee has many responsibilities - to the estate it is managing, to creditors and to the court. Where, as here, a trustee in bankruptcy seeks to hire former employees of the bankrupt company, the trustee also has a responsibility to those employees. The trustee's decision to bring a motion on the first day of its trusteeship seeking a declaration that it not be deemed a successor employer "for any purpose whatsoever" was, in the bankruptcy judge's view, premature. Accordingly, he dismissed the motion. The trustee does not appeal this component of his decision.

**32** Equally, the appellants' cross-motion, understandable perhaps because of the trustee's motion, was also, arguably, misconceived. The first day of a bankruptcy is hardly business as usual' for anyone, including the employees. The relationship between the trustee and the employees of the bankrupt company cannot be resolved instantly. Care, sensitivity, negotiation and at least some time will be necessary before an appropriate relationship can be set in place. The bankruptcy judge regarded the union's cross-motion as premature as well. Accordingly, he dismissed it, but without foreclosing the possibility that such a motion could succeed once the parties, at a minimum, had explored the establishment of an appropriate employment relationship. Again, I see no basis for interfering with the bankruptcy judge's exercise of discretion in this regard.

**33** I also do not accept the appellants' submission that the bankruptcy judge decided the successor employer issue. He explicitly did not do this. He dismissed the trustee's motion seeking an order that the trustee not be deemed a successor employer and authorized the trustee to engage former employees of the bankrupt company. He also dismissed the unions' cross-motion, but coupled that dismissal with an invitation to bring another motion later with an "appropriate factual underpinning". In my view, these careful combined dispositions establish clearly that the bankruptcy

judge did not decide the successor employer issue on its merits. Rather, he regarded resolution of that issue on January 10, 2003 as being premature. Accordingly, in the exercise of his discretion, he left it open.

**34** Finally, I do not agree with the appellants' challenge to the bankruptcy judge's description of the various collective agreements as "not terminated but rather ... put into suspended animation".

**35** On January 10, 2003, the first day of the bankruptcy, it strikes me that this description was entirely apt. On that date, it was simply too early to attach formal, and final, legal labels to the relationship between the trustee and the employees. Importantly, the bankruptcy judge explicitly recognized the existence and importance of the collective agreements. Immediately after his description of the collective agreements as contracts put into "suspended animation", he effectively gave some advice to the trustee regarding the importance of the employment relationship established by those agreements:

> The trustee will also have to appreciate that if it does not accede to the union demands for union dues, pension contributions and grievance-type procedures, then conceivably after a period of time (which may vary in length) the personnel which it has employed may become disenchanted with continuing at the various locations and value may evaporate or start to do so unless "corrective" or "ameliorating" measures are taken.

**36** For these reasons, I conclude that the bankruptcy judge did not err, in the exercise of his discretion, by deciding that the appellants' cross-motion seeking leave to make an application on the successor employer issue to the OLRB was premature and, therefore, should be dismissed.

## E. DISPOSITION

**37** I would dismiss the appeal with costs fixed at $20,000 inclusive of disbursements and G.S.T.

MacPHERSON J.A.
CRONK J.A. -- I agree.

**38** BORINS J.A. (dissenting):-- I have had the advantage of reading the reasons for judgment of my colleague, MacPherson J.A. With respect, I am unable to agree with his conclusion that this appeal should be dismissed.

**39** In my view, this appeal is about the exercise of judicial discretion in the context of an application by two trade unions (the "appellants") pursuant to s. 215 of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 (the "BIA") for leave to bring an application before the Ontario Labour Relations Board (the "OLRB") under s. 69(12) of the Labour Relations Act, S.O. 1995, c. 1, Sch. A (the "LRA") for a declaration that Ernst & Young, Inc. ("EYI"), the trustee in bankruptcy of The Royal Crest Lifecare Group ("Royal Crest"), is a successor employer. Thus, the issue in this appeal is whether there is any basis on which this court can interfere with the discretion exercised by Farley J. in dismissing the appellants' application under s. 215 of the BIA. For the reasons that follow, I have concluded that the bankruptcy judge erred in the exercise of his discretion.

**40** At the outset, I find it helpful to repeat what I said about the standard of appellate review of the exercise of judicial discretion in Wong v. Lee (2002), 58 O.R. (3d) 398 at 408-409:

> The standard of appellate review of judicial discretion has been considered by the Supreme Court of Canada in a number of cases. In Reza v. Canada, [1994] 2 S.C.R. 394 at pp. 404-05, 116 D.L.R. (4th) 61 at p. 68, the Supreme Court held that:
>
> > ... the test for appellate review of the exercise of judicial discretion is whether the judge at first instance has given sufficient weight to all relevant considerations: Friends of the Oldman River Society v. Canada (Minister of Transport), [1992] 1 S.C.R. 3, at pp. 76-77, per LaForest J. See also Manitoba (Attorney General) v. Metropolitan Stores (MTS) Ltd., [1987] 1 S.C.R. 110, at pp. 154-55.
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> In Friends of Oldman River Society v. Canada (Minister of Transport), [1992] 1 S.C.R. 3, at pp. 76-77, LaForest J. stated that in Harelkin v. University of Regina, [1979] 2 S.C.R. 561, 96 D.L.R. (3d) 14, the Supreme Court had essentially adopted the following standard of review articulated by Viscount Simon L.C. in Charles Osenton & Co. v. Johnston, [1942] A.C. 130 at p. 138 (H.L.):
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> > The law as to the reversal by a court of appeal of an order made by the judge below in the exercise of his discretion is well-established, and any difficulty that arises is due only to the application of well-settled principles in an individual case. The appellate tribunal is not at liberty merely to substitute its own exercise of discretion for the discretion already exercised by the judge. In other words, appellate authorities ought not to reverse the order merely because they would themselves have exercised the original discretion, had it attached to them, in a different way. But if the appellate tribunal reaches the clear conclusion that there has been a wrongful exercise of discretion in that no weight, or no sufficient weight, has been given to relevant considerations such as those urged before us by the appellant, then the reversal of the order on appeal may be justified.

II

**41** It is also helpful to reproduce the legislation that is relevant to this appeal.

Bankruptcy and Insolvency Act

s. 72(1) The provisions of this Act shall not be deemed to abrogate or supersede the substantive provisions of any other law or statute relating to property and civil rights that are not in conflict with this Act, and the trustee is entitled to avail himself of all rights and remedies provided by that law or statute as supplementary to and in addition to the rights and remedies provided by this Act.

s. 215 Except by leave of the court, no action lies against the Superintendent, an official receiver, an interim receiver or a trustee with respect to any report made under, or any action taken pursuant to, this Act.

Labour Relations Act, 1995

s. 69(1) In this section,

"business" includes a part or parts thereof; ("enterprise")

"sells" includes leases, transfers and any other manner of disposition, and "sold" and "sale" have corresponding meanings. ("vend", "vendu", "vente")

(2) Where an employer who is bound by or is a party to a collective agreement with a trade union or council of trade unions sells his, her or its business, the person to whom the business has been sold is, until the Board otherwise declares, bound by the collective agreement as if the person had been a party thereto and, where an employer sells his, her or its business while an application for certification or termination of bargaining rights to which the employer is a party is before the Board, the person to whom the business has been sold is, until the Board otherwise declares, the employer for the purposes of the application as if the person were named as the employer in the application.

s. 69(12) Where, on any application under this section or in any other proceeding before the Board, a question arises as to whether a business has been sold by one employer to another, the Board shall determine the question and its decision is final and conclusive for the purposes of this Act.

s. 114(1) The Board has exclusive jurisdiction to exercise the powers conferred upon it by or under this Act and to determine all questions of fact or law that arise in any matter before it, and the action or decision of the Board thereon is final and conclusive for all purposes, but nevertheless the Board may at any time, if it considers it advisable to do so, reconsider any decision, order, direction, declaration or ruling made by it and vary or revoke any such decision, order, direction, declaration or ruling.

III

**42** Although MacPherson J.A. has reviewed the facts which formed the basis for both the appellants' s. 215 application and the trustee in bankruptcy's application for declarations that it is not a successor employer under s. 69(12) of the LRA and other labour and employment laws, his review does not make reference to a number of facts that, in my view, are relevant to this appeal. Therefore, I propose to outline these additional facts.

**43** When EYI was appointed as interim receiver of the estate of Royal Crest on November 12, 2002, it immediately engaged the former Royal Crest employees on a temporary basis under terms and conditions of employment similar but not identical to those provided by the collective agreements. EYI was authorized to do so by a term of the order that appointed it as interim receiver. Excluded terms were access to a grievance procedure, full recognition of seniority, payment of union dues and contributions to the company pension plan. The former Royal Crest employees are mem-

bers of the appellant unions which, prior to the bankruptcy, had entered into collective agreements with the Royal Crest companies. At the time of the interim receivership, there were, and remain, several outstanding labour relations issues, such as: outstanding grievances involving employee discipline; outstanding pay equity adjustments; the negotiation of a first time collective agreement; and default in contributions to the pension plan.

**44** On November 13, 2002, EYI delivered a letter to each employee containing an offer of employment and discussing, inter alia, the terms of employment. In addition, the letter contained the following information:

> Our appointment as Interim-Receiver is on a temporary basis and for the limited purpose of continuing the operation of the homes and protecting the assets. It is our intent to stabilize the operations of the home by assuming control of the homes and protecting the interests of the stakeholders, including the residents whose health, safety and well being is of central concern. To assist in achieving this objective, we have retained the services of Extendicare (Canada) Inc. to manage and supervise the operations of the homes.
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> Pursuant to the terms of the Order, your employment by the Companies has been terminated. We would like to engage your services on a temporary basis to assist with the continued operation of the homes, which will assist the Interim-Receiver in fulfilling its mandate to determine the best way to ensure the future of the homes as going concerns. The purpose of this letter is to set out the terms under which we are prepared to do so.
>
> ...
>
> In making this offer, the Interim-Receiver is acting solely in its capacity as Interim-Receiver and without personal or corporate liability. By accepting this offer you acknowledge that the Interim-Receiver is not a successor employer within the meaning or contemplation of the Ontario Employment Standards Act, 2000, the Ontario Labour Relations Act or other similar federal or provincial legislation.

**45** On January 10, 2003, EYI was appointed as trustee in bankruptcy of the estate of Royal Crest under the BIA. On January 17, 2003, pursuant to s. 101 of the Courts of Justice Act, R.S.O. 1990, c. C.43 (the "CJA"), EYI was appointed as receiver over the assets, property and undertaking of Royal Crest for the purpose of realizing thereon. Although clause 11 of this order expressly precluded the engagement of any or all of Royal Crest's former employees, on January 17, 2003, the trustee delivered a letter to the former employees that contained an offer of employment.

**46** The relevant portions of this letter read as follows:

> As noted previously, the Interim Receiver was appointed on a temporary basis until the appointment of the Trustee, and therefore the role of the Interim Receiver has come to an end effective January 17, 2003. The Trustee will continue to operate the homes in the same manner as the Interim Receiver, and the Trustee

has retained the services of Extendicare (Canada) Inc. to manage and supervise the operations of the homes.

Your employment with the Interim Receiver has ceased effective January 17, 2003 and the Trustee will immediately re-engage your services on a temporary basis to assist with the continued operation of the homes, on the same terms and conditions as outlined in the Offer of Employment. Your services are required to assist the Trustee in fulfilling its mandate to determine the best way to ensure the future of the homes as going concerns. The purpose of this letter is to set out the terms under which we are prepared to do so.

You will be paid the same regular wages or salary that you have been receiving from the Interim Receiver. The Trustee will continue to provide all benefits provided by the Interim Receiver to you. The Trustee, in the same manner as the Interim Receiver, is unable to continue to provide benefits provided by the Companies to you prior to the appointment of the Interim Receiver (including, but not limited to, life insurance, disability or pension benefits or RRSP contributions). The Trustee will be making the usual payroll deductions to the appropriate government authority on your behalf.

In making this offer, the Trustee is acting solely in its capacity as Trustee and without personal or corporate liability. By continuing to work in the homes after January 17, 2003 you will be deemed to have accepted this offer, have read and understand fully the terms of this letter and agreed to be bound by its terms. You have also acknowledged that the Trustee is not a successor employer within the meaning or contemplation of the Ontario ESA, the Ontario Labour Relations Act or similar federal or provincial legislation.

**47** From the foregoing, it is clear that from the outset EYI, in its various capacities, recognized that it was prudent to operate the nursing homes as a going concern for two related reasons: (1) to accommodate the 2300 patients and residents of the homes; and (2) to maximize the potential dividend to be paid to Royal Crest's creditors by selling the nursing homes as a going concern. Moreover, it recognized that the most efficient way to continue to operate the homes was to engage the former employees of Royal Crest. Indeed, this appeared to be of such importance to EYI that in its second letter to the employees it wrote: "Your services are required to assist the Trustee in fulfilling its mandate to determine the best way to ensure the future of the homes as going concerns".

**48** When the appellants' motion was before the court, it was clear that the operation of the homes was continuing in the same manner as it had before Royal Crest was granted protection under the Companies Creditors Arrangement Act, R.S.C. 1985, c. C.36 (the "CCAA") on October 21, 2002, and throughout the two month period of the interim receivership. It appeared that this operation would continue in the same manner until the trustee in bankruptcy was able to sell the nursing home business as a going concern. Thus, when the appellants' s. 215 motion was before the court, approximately 2200 employees were continuing the operation of the nursing homes for approximately 2300 patients and residents, and would continue to do so subsequent to EYI's appointment as trustee in bankruptcy and receiver until EYI was able to obtain a purchaser willing to acquire the nursing homes as a going concern.

**49** From the letters it wrote to the former employees of Royal Crest, it is clear that EYI did not wish to be declared a successor employer under s. 69(12) pf the LRA. It is evident from EYI's application for an order declaring that the trustee in bankruptcy is not a successor employer under the LRA, the Occupational Health and Safety Act, R.S.O. 1990, c. O.1, the Employment Standards Act, S.O. 2000, c. 41, the Workplace Safety and Insurance Act, S.O. 1997, c. 16, Sch. A, the Pay Equity Act, R.S.O. 1990, c. P.7, the Human Rights Code, R.S.O. 1990, c. H.19, the Pension Benefits Act, R.S.O. 1990, c. P.8 and the Pension Benefits Standards Act, R.S.C. 1985, c. 32 (2nd Supp.) or any other legislation or common law governing labour relations, that EYI recognized that in the administration of an estate under the BIA, a trustee in bankruptcy is required to do so in conformity with provincial legislation governing employees and employee rights.

IV

**50** The test that applies in considering an application under s. 215 of the BIA for leave to bring proceedings against a trustee has received considerable judicial attention. As MacPherson J.A. points out, the case law establishes that the threshold for granting leave is a low one. However, in applying the test it is necessary to consider that s. 215 is part of the machinery of the BIA which is designed to ensure that the purposes of the Act can be carried out properly without the undue intervention of other proceedings. As such, the purpose of s. 215 is to protect the trustee against frivolous and vexatious proceedings, or proceedings that have no factual basis.

**51** This court considered s. 186 of the former Bankruptcy Act, the predecessor of s. 215, in Mancini (Bankrupt) et al. v. Falconi et al. (1993), 61 O.A.C. 332. After reviewing a number of authorities, in para. 7 Osborne J.A. set out the factors to be considered on a s. 215 application:

> The following principles can be taken from the decided cases:
>
> 1. Leave to sue a trustee should not be granted if the action is frivolous or vexatious. Manifestly unmeritorious claims should not be permitted to proceed.
> 2. An action should not be allowed to proceed if the evidence filed in support of the motion, including the intended action as pleaded in draft form, does not disclose a cause of action against the trustee. The evidence typically will be presented by way of affidavit and must supply facts to support the claim sought to be asserted: see Peat Marwick Ltd. v. Thorne Riddell, supra.
> 3. The court is not required to make a final assessment of the merits of the claim before granting leave: see Re Lufro Ltée; Leblond v. Tremblay (1985), 54 C.B.R. (N.S.) 199 (Que. C.A.).

**52** In para. 12 Osborne J.A. stated that the court is required to consider the evidence filed in support of the application in the context of the proposed proceeding when adjudicating a s. 215 leave application. He continued: "The issue is not whether the evidence on the [s. 215] motion discloses the existence of a cause of action against the trustee, but rather whether the evidence provides the required support for the cause of action sought to be asserted [against the trustee]" [emphasis in original].

**53** Osborne J.A. commented further on what factors the evidence must establish and the sufficiency of the evidence in paras. 16-17:

> In my opinion, the motions court judge was correct in reaching the conclusion he did on this issue. *On a continuum of evidence ranging from no evidence to evidence which is conclusive, the evidence required to support an order under s. 186 must be sufficient to establish that there is a factual basis for the proposed claim and that the proposed claim discloses a cause of action.*
>
> The sufficiency of the evidence must be measured in the context of the purpose of s. 186 which, as stated earlier, is to prevent the trustee from having to respond to actions which are frivolous or vexatious or from claims which do not disclose a cause of action. As I have previously noted, the evidence on a motion under s. 186 does not have to be sufficient to enable the motions court judge to make a final assessment of the merits of the claim sought to be made, but it must be sufficient to address the issues that I have identified, having in mind the objectives of s. 186 [emphasis added].

V

**54** The bankruptcy judge's reasons for rejecting the appellants' s. 215 application are reported as Royal Crest Lifecare Group Inc. (Re), [2003] O.J. No. 756. Early in his reasons, in para. 6, the bankruptcy judge identified "the contentious issue or battlefield [to be] whether the trustee in bankruptcy can become a successor employer [pursuant to s. 69 of the LRA] if the trustee hires employees to do the work previously engaged in by employees pre-bankruptcy". After reviewing the positions of the parties, the bankruptcy judge considered the trustee's submission that collective agreements terminate upon an employer's bankruptcy. He appears to have accepted the reasoning of the Nova Scotia Court of Appeal in Saan Stores Ltd. v. Nova Scotia (Labour Relations Board) (1999), 172 D.L.R. (4th) 134 that although bankruptcy terminates the employment relationship between a bankrupt employer and its employees, a collective agreement is "not rendered inoperative" by reason of an employer's bankruptcy.

**55** In paras. 24-26 the bankruptcy judge discussed the statutory mandate of a trustee in bankruptcy. In my opinion, as this discussion is relevant to his ultimate decision to dismiss the appellants' application, it is helpful to reproduce it in its entirety:

> It seems to me that when one appreciates that the mandate of a trustee in bankruptcy is to maximize value of the assets vested in the trustee on a bankruptcy for the purpose of providing a dividend to the creditors to partially satisfy their claims, the circumstance of operating the business (if the assets are the business and undertaking) *is merely ancillary and incidental to that function of realizing upon the assets*. Coupled with the rather "new-found" objective and thrust of the BIA since the 1992 amendments with the significant social and economic policy with particular positive impact for employees and the communities in which these employees live to have businesses, if possible and practicable, sold as a going concern (such being the usual way in which to maximize value as well), *it would be undesirable to saddle the Trustee with (heavy) personal liabilities which may arise either from a finding of "successor employer" against the trustee or a conclusion that a trustee who hires personnel "inherits" an operative collective agreement. Simply put, what role is the trustee truly playing - is it acting qua*

*realizor of the assets or is it acting qua employer in essence.* Where the business cannot be conveniently mothballed (e.g. a steel mill where the blast furnaces must be kept active or otherwise the furnaces would "solidify" or, as here, where the residents cannot be easily transferred both physically and as well with concern for their emotional disruption), it seems that the trustee may be "forced" to operate the business during the period of marketing through sale. The maintenance of going concern goodwill will also be an important factor in determining whether it is reasonable to continue some or all of the operations, even if it were not a physical problem to shut down operations. *If the trustee did not operate the business where that was physically necessary or to maximize value of realization, then the trustee would be acting contrary to the principles of the BIA and in so acting would be derelict in its duties and obligations under that federal insolvency statute.*

It seems to me that where a trustee is operating the business as incidental to the trustee disposing of it and realizing on the assets and there is no question or issue raised that it is pursuing a marketing and ultimately sale/disposition program *in a reasonable and bona fide way with due dispatch, then the question of employment of personnel is only incidental to its function of realizing on the assets (and protecting stakeholder interests in going concern preservation).*

I certainly agree with the observations of Spence J. in 588871 at p. 33:

> PMTI also contended that this motion involves an important policy question. If, in circumstances such as those in the present case, a trustee in bankruptcy who is given authority to carry on the business is to be exposed to the risk of being considered a successor employer and the attendant liabilities of the status, *no trustee would ever undertake to carry on that business and that could thwart the proper operation of the BIA.*. I think this concern may properly be taken into account.

I do not regard this as an "in terrorem" argument as so characterized by CUPE's counsel. Spence J. went on to state at p. 33:

> With respect to the request for leave, I think a delicate balancing of the relevant considerations is required. The [OLRB] clearly has jurisdiction under the OLRA to make a determination that there has been a sale of a business and that PMTI is a successor employer. The considerations which have been raised here concerning the apparent inconsistencies between a positive determination to that effect and bankruptcy principles and the order of December 14, 1994 could presumably be considered in those proceedings to the extent germane and in any other proceedings that may be taken in this matter. *The courts should ordinarily defer to the [OLRB] on a matter clearly within its statutory jurisdiction. On the other hand, if a decision were taken by the [OLRB] against the trustee, it would involve the inconsistencies mentioned above. It would be incompatible with the termi-*

> *nation of the collective agreement as a result of the bankruptcy and the limited role of a trustee in bankruptcy in carrying on a business. It seems to me that such matters are properly to be addressed by this court on this application for leave under the BIA and not to be deferred for decision to a tribunal which is not charged with responsibility in respect of the bankruptcy law.* The stay of proceedings imposed by s. 215 of the BIA is one part of the machinery of the Act which functions to ensure that the purposes of the Act can be carried out properly without the undue intervention of other proceedings. The stay imposed under s. 215 has a proper effect in this case, for the reasons mentioned above. Accordingly, the request for leave nunc pro tunc should not be granted [emphasis added].

**56** In paras. 29-30, the bankruptcy judge then gave what I understand to be his reasons for dismissing the appellants' application:

> *There has been no allegation, let alone evidence, that the Trustee here (even if one were to consider E&Y Inc. in its capacity as IR) has been dragging its feet or will do so. The CUPE cross-motion for leave is dismissed without prejudice to such a motion being brought back on again with appropriate factual underpinning which I would be of the view ought to demonstrate that the Trustee has slipped over from functioning qua realizor of assets in a diligent fashion to the role of being predominantly an employer in its activities.*

In the meantime it appears to me that the collective agreement is not terminated but rather is put into suspended animation, to be revived if, as, and when a purchaser with a personal economic interest in the operation of the business acquires the business [emphasis added].

**57** Read as a whole, as I read his reasons, the bankruptcy judge dismissed the appellants' application for leave to commence proceedings before the OLRB for a declaration that EYI is a successor employer under s. 69(12) of the LRA because he was of the view that if the application before the Board were to succeed, a declaration that the trustee in bankruptcy is a successor employer would interfere with the mandate of a trustee, saddle the trustee "with (heavy) personal liabilities", would discourage trustees from carrying on a business as a going concern and would be incompatible with the termination of a collective agreement consequent to the bankruptcy of an employer. As a result, the bankruptcy judge agreed with the opinion of Spence J. in Re 588871 Ontario Ltd. (1995), 33 C.B.R. (3d) 28 (Ont. Gen. Div.), that although the OLRB has exclusive jurisdiction over the determination of "whether a business has been sold by one employer to another", the court should not defer to the jurisdiction of the Board where a successor employer application is made in the context of a bankruptcy; instead, this determination should be made by a court "charged" with responsibilities in respect to bankruptcy law.

**58** As his ultimate reason for dismissing the application for leave, the bankruptcy judge stated that the trustee in bankruptcy had not "been dragging its feet" and there was no suggestion that it would do so. However, the dismissal of the application was without prejudice to it being reinstated "with appropriate factual underpinning ... to demonstrate that the trustee has slipped over from functioning qua realizor of assets in a diligent fashion to the role of being predominantly an employer in its activities".

**59** In analyzing the bankruptcy judge's reasons for dismissing the appellants' application under s. 215 of the BIA it is helpful to recall that the authorities are uniform that the test to be applied by the court sets a low threshold.

**60** With respect to the first element of the test established in Mancini, in my view, there can be no question that the proposed application to the OLRB is neither frivolous nor vexatious. At the time of the application, EYI was operating the same business that was operated by Royal Crest and had hired the same employees that had been employed by Royal Crest to perform the same function that they had performed previously. EYI had done so as interim receiver for two months prior to its appointment as trustee in bankruptcy and receiver. Moreover, neither EYI nor the bankruptcy judge suggested that the proposed application to the OLRB was frivolous or vexatious.

**61** Under the second element of the test, the proposed application to the OLRB must disclose "a cause of action" against the trustee in bankruptcy. This is to be decided on the basis of evidence that is sufficient to establish a factual basis for the proposed OLRB application. In the context of these proceedings, the "cause of action" against the trustee consists of the assertion that in the operation of the Royal Crest's business as a going concern, the trustee had become a successor employer within the meaning of s. 69(12) of the LRA. It would appear that the trustee's operation of Royal Crest's business as a going concern for the benefit of its creditors and the patients and residents mitigates in favour of a finding by the OLRB that the trustee is a successor employer. There is little doubt that the evidence of the history of EYI's operation of the business since its appointment as interim receiver on November 12, 2002, provided a factual basis for the appellants' application as contemplated by the second element of the Mancini test.

**62** In considering whether the proposed application to the OLRB discloses a cause of action against the trustee in bankruptcy it is important to recognize that s. 69(2) of the LRA provides that a union continues to be the bargaining agent for the employees of the person, or entity, to whom a business is sold until the OLRB otherwise declares. As pointed out by George W. Adams in his text, Canadian Labour Law, 2nd ed. looseleaf (Aurora: Canada Law Book Inc., 2003) at 8.10:

> ... collective bargaining rights flow through changes in ownership so long as there is a continuation of the same business. It is the business - and not the employer - to which collective bargaining rights have become attached ... The successor provisions [of the LRA] have a two-fold purpose: to protect the trade union's right to bargain and to protect any subsisting collective agreement from termination upon sale.

**63** Moreover, as Mr. Adams points out at 8.190, labour boards have adopted a broad and liberal interpretation of successorship provisions, including what constitutes the sale of a business under s. 69(1) of the LRA, in accordance with the remedial nature of the legislation. After reviewing the case law, Mr. Adams concludes:

> For the most part, the Ontario and British Columbia courts accept and recognize that the substantial similarity of work performed subsequent to a transaction to that performed prior to a transaction normally creates a strong inference there has been a transfer of a business. The criteria relevant to such an interpretation are: (a) substantially the same jobs being performed at the same time and places; (b)

in respect of substantially the same goods and services; and (c) for substantially the same customers or patrons.

**64** In determining whether the appellants' proposed application to the OLRB disclosed a "cause of action" against the trustee in bankruptcy, it was necessary that the bankruptcy judge consider not only the purpose of the successorship provision in s. 69 of the LRA, but the criteria relevant to the determination of whether the trustee could be found by the OLRB to be a successor employer. The bankruptcy judge failed to do so. Based on the above criteria, there is an abundance of evidence in the record to establish a factual basis for the proposed successorship application to the OLRB.

**65** As for the third element of the Mancini test, the bankruptcy judge must not make a final assessment of the proposed claim or application. Although the bankruptcy judge did not in fact do so in this case, in my view he came perilously close to doing so. He followed the decision of Spence J. in Re 588871 Ontario Ltd. that the question of successorship should be effectively decided on a motion to the bankruptcy court under s. 215 of the BIA, contrary to s. 114(1) of the LRA that provides that the OLRB has exclusive jurisdiction to exercise the powers conferred upon it by the LRA.

**66** In addition, I have difficulty in understanding what the bankruptcy judge meant in para. 24 by his characterization of the trustee's role as "acting qua realizor of the assets or qua employer in essence". In my view, if it is the opinion of the trustee in bankruptcy that the maximum dividend for creditors can be achieved by selling the bankrupt's business as a going concern it stands to reason that the trustee can do so only if it has the necessary employees to operate the business. The bankruptcy judge reasoned that the trustee's employment of personnel was "only incidental" to its function of realizing on the assets and "protecting stakeholder interests in going concern preservation". With respect, I do not agree with this reasoning. The operation of the business as a going concern and the re-hiring of Royal Crest's employees to accomplish this are neither incidental nor ancillary to the trustee's role to maximize and maintain the value of the assets for the benefit of the creditors. In my view, they are central to that role. Without the former Royal Crest employees, the trustee could not operate the nursing home business as a going concern. The employees have statutory rights which an employer must respect. The unions were attempting to protect and enforce their members' rights in seeking leave to apply to the OLRB to obtain a successorship ruling.

**67** The bankruptcy judge returned to this theme in para. 29, where he gave his ultimate reason for dismissing the appellants' s. 215 application. He was of the view that the length of time during which the trustee in bankruptcy had operated the business was pertinent to whether or not the trustee might be declared a successor employer under s. 69 of the OLRA. Thus, he permitted the appellants to make a further application should the trustee "[slip] over from functioning qua realizor of assets in a diligent fashion to the role of being predominantly an employer in its activities".

**68** Moreover, in my view the bankruptcy judge minimized the fact that this case involves the rights of employees and workers and that under the legislative scheme of the LRA the only recourse available to the unions in protecting the rights of their members was to bring the appropriate proceeding before the OLRB. In addition, the bankruptcy judge appears to have placed the trustee's role under the BIA ahead of the employees' statutory rights conferred by the statutes that I have listed in para. 12. In doing so, it seems that he overlooked the proposition that except in the case of "operational conflict", valid provincial law of general application continues to apply in a bankruptcy context: Husky Oil Operations Ltd. v. M.N.R., [1995] 3 S.C.R. 453. This is also recognized in s. 72(1) of the BIA where Parliament has explicitly called for the application of provincial law in administering a bankrupt estate, except to the extent that it is inconsistent with the terms of the BIA.

**69** In making these observations I am mindful that the court did not require submissions from the parties on the constitutional issue raised by the respondent trustee and I do not intend, by my observations, to be taken as determining that issue. The purpose of my observations is to indicate that as the rights of employees and workers are central to the unions' s. 215 application, it is my view that early recourse to the OLRB was an appropriate factor for the bankruptcy judge to take into account in applying the Mancini test.

**70** In summary, the bankruptcy judge placed too much emphasis on the bankruptcy environment and gave insufficient weight to the essential character of the issues that the unions sought to advance before the OLRB on behalf of their members. While the important role performed by bankruptcy trustees is deserving of protection, the rights of labour unions to pursue legitimate issues on behalf of their members must also be respected. As, in my view, the bankruptcy judge did not give sufficient weight to these considerations and to the test to be applied on an application under s. 215 of the BIA as explained in Mancini, he erred in the exercise of his discretion.

**71** In my opinion, the unions' s. 215 application was timely and prudent. Nothing about the application was premature. The unions should not be faulted for bringing it on the day that the court appointed EYI as trustee in bankruptcy. It was brought in response to EYI's application for a declaration that it be deemed not to be a successor employer. EYI was no stranger to the business operation of Royal Crest. For two months prior to its appointment as trustee, as interim receiver it had operated the nursing home business with Royal Crest's former employees. As trustee, it was intending to operate the business with the same employees. The employees had statutory rights which the unions believed required recourse to the OLRB for their protection. Had the bankruptcy judge granted the unions' application for leave to apply to the OLRB, or, indeed, should this court do so, the work of the trustee in administering the estate would not have been delayed or frustrated as it would have continued its operation of the nursing homes, thereby benefiting both the creditors and the residents, while it continued its search for a purchaser of the business as a going concern. At the same time, the unions would have been able to prepare their application to the OLRB.

**72** Indeed, nothing changed in the operation of the business on January 10, 2003 other than the status of EYI, which continued that operation as trustee in bankruptcy rather than as interim receiver. The trustee was of the opinion that the record supported its application, which acknowledged the existence of the collective agreements, for a declaration that it was not a successor employer. The unions relied on the same record. Moreover, had the bankruptcy judge granted the unions' application for leave to bring a s. 69(12) application before the OLRB, the record could only have improved in the time that it would have taken for the application to be heard by the OLRB.

## VII

**73** For all of the foregoing reasons, it is my view that there was a wrongful exercise of discretion by the bankruptcy judge as a result of his failure to apply the test in Mancini and to give sufficient weight to the relevant considerations as argued before us by the appellants. Therefore, this is a proper case for this court to interfere with the bankruptcy judge's exercise of discretion.

**74** In the result, I would allow the appeal with costs, set aside the order of the bankruptcy judge and substitute an order granting leave to the appellants pursuant to s. 215 of the BIA to bring an application to the OLRB under s. 69(12) of the LRA.

BORINS J.A.

cp/e/nc/qw/qlhcc/qlgxc

# Tab 4

*Case Name:*

# Liberty Oil & Gas 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 Liberty Oil & Gas Ltd. Between Lexxor Energy Inc. and Liberty Oil & Gas Ltd., appellants, and Richter, Allan & Taylor Inc. Monitor of Liberty Oil & Gas Ltd., respondents**

[2003] A.J. No. 615

2003 ABCA 158

44 C.B.R. (4th) 96

122 A.C.W.S. (3d) 976

2003 CarswellAlta 684

Docket No.: 0301-0038-AC

Alberta Court of Appeal
Calgary, Alberta

**Wittmann J.A.**

Heard: April 23, 2003.
Judgment: filed May 14, 2003.

(25 paras.)

*Creditors and debtors -- Debtors' relief legislation -- Companies' creditors arrangement legislation -- General estate, amounts included in -- Practice -- Appeals -- Leave to appeal -- Application for -- Grounds for refusal to grant leave.*

Application by Lexxor Energy and Liberty Oil & Gas for leave to appeal from a decision fixing the terms of an order. Lexxor acquired Liberty after a plan of arrangement filed under the Companies'

Creditors Arrangement Act was accepted by creditors. A dispute arose between the creditors and Lexxor as to the amounts received for production of oil and gas in the interval between the petition date and the transaction date. The chambers judge found that the matching principle applied and the earnings between the date of the petition and the closing date were taken into account. Lexxor attempted to settle the order including a statement that the matching principle was to be applied in accordance with generally accepted accounting principles. The judge applied the matching principle as applied in the monitor's report.

HELD: Application dismissed. There was no demonstrable error in the judge's decision. The appeal concerned a matter of significance to insolvency practice and the parties to the proceedings. However, the interpretation of the plan and the adoption of the monitor's proposal was not an error of law. The order recognized the revenue during the period of the arrangement and its availability to satisfy excluded claims. The judge did not intend to extend the matching principle beyond revenue recognition.

**Statutes, Regulations and Rules Cited:**

Companies' Creditors Arrangement Act, ss. 13, 14(1).

**Appeal From:**

On application for leave to appeal the decision of Hart J., dated January 24, 2003.

**Counsel:**

G. Brian Davison, for the Various Unsecured Creditors.
Larry B. Robinson, for the appellants, Lexxor Energy Inc. and Liberty Oil & Gas Ltd.
Geoffrey D. Baker, for Rick Martin.
Frank R. Dearlove, for the respondents, Richter, Allan & Taylor Inc., Monitor of Liberty Oil & Gas Ltd.
Peter S. Jull, Q.C., for Various Unsecured Creditors.

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MEMORANDUM OF DECISION

WITTMANN J.A.:--

INTRODUCTION

**1** Lexxor Energy Inc. ("Lexxor") acquired Liberty Oil & Gas Ltd. ("Liberty") after Liberty's plan of arrangement ("the Plan") pursuant to the Companies Creditors' Arrangement Act ("CCAA") R.S.C. 1985 c. C-36 was accepted by its creditors. The transaction closed July 23, 2002.

**2** Hart, J. at all material times was the supervising judge pursuant to the CCAA and Richter, Allan & Taylor Inc. acted as the court-appointed Monitor. The business of Liberty included the production of oil and gas. As is customary in the industry, payment for the previous month's production was not received until the following month. In the case of Liberty, on or about the 25th of each month. A dispute arose between the unsecured creditors and Lexxor as to the amounts availa-

ble attributable to the post-petition interval between February 25, 2002, the petition date, and July 23, 2002 ("the CCAA Period").

**3** At the core of the dispute was whether revenue accruing during the CCAA Period was available to pay excluded claims, a defined term under the Plan. Lexxor took the position before Hart, J. that the matching principle of accounting was inapplicable, that the Plan indicated that only cash received during the CCAA Period would be used to pay excluded claims and that therefore the cash proceeds ("the basket") were available to pay any unsecured creditor deficiency arising. The impact on the unsecured creditors if Lexxor's position were adopted is significant. It markedly decreases their recovery.

FACTS

**4** The relevant provisions of the Plan voted upon by the unsecured creditors and affirmed by court order dated June 29, 2002 are as follows:

> 2.1 Purpose
>
> . . . Liberty's Unsecured Creditors are to be paid their first $1,500.00 of Proven Claims in cash and receive their pro rata share of a pool of cash and Lexxor Shares estimated to enable them to recover $0.75 per dollar of Proven Claim. . . .
>
> 2.2 Claims Not affected - Excluded Claims
>
> This Plan does not compromise the following Claims and rights that arise in the following capacities (the "Excluded Claims"):
>
> . . .
>
> (b) All Claims arising or accruing for either or both of the provision of goods and performance of services to Liberty from and after the date of the Initial Order;
>
> . . .
>
> 4.1 Overview
>
> . . . it is expected that this Plan will enable Liberty to go forward as a viable business entity. It is expected that this Plan will result in:
>
> (a) repayment of 100% of all Excluded Claims from the Cash Proceeds with the exception of the National Bank Debt which will be dealt with . . .
> (b) a distribution to Unsecured Creditors of approximately $0.75 per dollar, consisting of the balance of Cash Proceeds and Lexxor Shares;
>
> . . .
>
> 4.2 Details of the Plan

. . .

(d) Payment of Excluded Claims and Distributions to Secured Creditors, and Unsecured Creditors:

(i) Excluded Claims: If Excluded Claims which are to be repaid in accordance with the provisions of the Plan have not been paid by the Plan Implementation Date, then Liberty shall pay such Excluded Claims from the Cash Proceeds as soon as practicable following the Plan Implementation Date . . .

(ii) Cash Distributions to Unsecured Creditors: The Monitor shall distribute the portion of Cash Proceeds due to Unsecured Creditors with Proven Claim after payment of or allowance for all Excluded Claims . . .

"Cash Proceeds" means a cash payment of $6,811,425.00 which will be available to Liberty and the Monitor which will permit Liberty or the Monitor, as applicable, to make the payments to Creditors contemplated by this Plan.

THE MONITOR'S FIFTH REPORT TO THE COURT

**5** In that part of the Fifth Report of the Monitor to the Court dealing with "Lexxor's Interpretation of the Plan", the Monitor stated at p. 2:

> At the closing date of July 23, 2002, the Liberty had $1,362,484 in liabilities relating to post-petition trade creditors that had not yet been paid by Liberty. These creditors are to be satisfied in full as the amounts owed to them arose subsequent to the Initial Order [FEB. 25, 2002]. Lexxor is of the view that the $1,362,484 is to be paid from the Cash Proceeds as Lexxor acquired no debt. Interpreting the Plan in this fashion has the effect of reducing the cash recovery to Liberty's unsecured creditors from 45 cents on the dollar to 27.5 cents on the dollar.

**6** He continued at pp. 2-3:

> . . . The Plan, however, does not address revenues earned by Liberty during the post-petition period. Those revenues which Lexxor believes they are entitled to, are required to pay Liberty's post-petition creditors.
>
> When Liberty's Plan was advanced to creditors to vote upon, unsecured creditors expected a recovery of 75 cents on the dollar, 45 cents in cash, and 35 cents in Lexxor shares. Paying post-petition trade creditors from the Cash Proceeds advanced by Lexxor was not contemplated. It is the Monitor's view that if the Plan is interpreted in this way the resulting removal of $1,362,484 from funds available to unsecured creditors may have significantly affected their vote on the Plan. Moreover, there were alternatives available other than Lexxor's proposal which both Liberty and the unsecured creditors may have considered differently if those parties were aware that the cash component of their recovery would only be 27.5

> cents not 45 cents as a result of post-petition trade creditors sharing in the cash proceeds.
>
> As well, given Lexxor's interpretation of the Plan, it appears that the quantum of post-petition trade creditors left in Liberty is arbitrary based on the closing date. If Lexxor had acquired Liberty on July 26, 2002, not July 23, 2002, the revenues for June 2002 production would have been received by Liberty and would have been used to pay a portion of Liberty's post-petition trade creditors. Consequently, the date of closing has a substantial impact on the recovery to Liberty's unsecured creditors. The gross revenues received by Liberty for June and July 2002 total approximately $1.55 million net of royalties. It seems consistent to the Monitor that these funds should be available to satisfy Liberty's post-petition trade creditor debt, not the Cash Proceeds.

**7** There were other issues put forward by Lexxor that are not subject to this leave application but which were dealt with by Hart, J. on January 24, 2003.

MONITOR'S SIXTH REPORT TO THE COURT

**8** This report was part of the material before Hart, J. on January 24, 2003. It is dated January 21, 2003. It is short. It repeats the issue as set out in the Monitor's Fifth Report in terms of the position of Lexxor and the payment of post-petition trade creditors. It also indicates that the Monitor had requested a summary of receipts and disbursements for the period February 25 to February 28, 2003 from Lexxor but that that information had not been provided. It goes on to reference Exhibit 1 which the Monitor at p. 3 stated :

> . . . reflects Liberty's receipts for July and August, 2002 as well as the disbursements made by Liberty in July 2002, the majority of which were made after the July 23, 2002 closing date. Based on the information available to the Monitor, it appears that during the CCAA Period Liberty had positive cash flow. Consequently, if the revenues and expenses (receipts and disbursements) were matched, it appears that the post-petition trade creditors would have been paid in full and the unsecured creditors of Liberty would receive a greater percentage of the Cash Proceeds.
>
> Lexxor's interpretation of the Plan may be contrary to a fundamental accounting concept. The concept is known as matching whereby expenses that are linked to a revenue generating activity are matched with the revenues in the period the revenue is recognized. Liberty would have prepared its statements on an accrual basis and therefore would have recognized or recorded the revenue in the period it occurred as well as when the expenses were incurred. Lexxor's interpretation would only reflect Liberty's expenses and not its revenues. The treatment of revenues in Liberty's Plan is not addressed and it is the Monitor's view that in the absence of clear language fundamental accounting principles should be applied.

THE DECISION OF THE SUPERVISING CHAMBERS JUDGE - JANUARY 24, 2003

**9** The transcript of the reasons includes the following:

> . . . looking at the plan as a whole and considering the process as a whole and included in that, of course, are the monitor's ongoing reports reporting on positive cashflow, that data coming from the operating company, looking at the various clauses in the plan itself, I am satisfied that the matching principle, as set out by the monitor in its reports, most notable the sixth report, and as contained in the briefs of - at least as contended for - in the briefs of Mr. Davison and Mr. Jull, is the proper principle and that the plan should be and was intended to be interpreted accordingly.
>
> There is no clear language to rebut a proper application of generally accepted accounting principles and it is clear that the unsecured creditors, at least, were given very strong representations that they could expect, on the basis of ongoing operations between the petition date and the closing date, that they could expect something in the order of $.75 on the dollar. There were other expenses that were not contemplated at the time that drives that figure down. But implicit in that representation I am satisfied was the notion that the matching principle would be applied between those dates and that earnings would be taken into account.
>
> Now that is the advice and direction that I give to the monitor.

**10** The application for leave to appeal to this Court was filed February 10, 2003. During the period from January 24, 2003 to March 3, 2003, the parties could not agree on the form of order to be taken out pursuant to Hart, J. reasons. On March 3, 2003, another hearing before Hart, J. was held to settle the minutes of his January 24, 2003 order.

THE DECISION OF THE SUPERVISING JUDGE ON MARCH 3, 2003

**11** At this hearing, counsel for Lexxor and Liberty shifted gears, perhaps in an attempt to grasp too much of a good thing. Two alternate forms of order were put forward to Hart, J. on March 3, 2003. So far as this leave application is concerned, the relevant clauses are, as put forward by Lexxor:

> 2. The Court approves and adopts the matching principle as set out by the Monitor in its Reports, most notably the Sixth Report, and, in particular:
>
> (a) the application of the matching principle is to be applied in accordance with generally accepted accounting principles for the period between February 25, 2002 and July 23, 2002.

**12** The second form of order put forward by the remainder of the parties, including the Monitor and the unsecured creditors, stated:

> 2. The Court approves and adopts the concept of "matching" as applied in the Monitor's Sixth Report, and, in particular, Exhibit "1" to that Report.

**13** At the hearing before Hart, J., Lexxor's counsel repeatedly advocated that the words "generally accepted accounting principles" be used in the form of the order because Hart, J. had mentioned that terminology in his decision on January 24, 2003 and wanted to make sure it applied to the entire CCAA period. Extensive argument occurred before Hart, J. as to the difference in impact on the

unsecured creditors if Lexxor's version of the order were adopted or if the remainder, i.e. the majority of the parties' version were adopted. Hart, J. stated at p. 42-43 of his March 3, 2003 decision as follows:

> The purpose of this hearing today on - this aspect of the hearing at least is to fix the terms of the order that I granted on January 24th on the monitor's application.
>
> I have heard all counsel who have spoken on this settlement of terms hearing and I am satisfied that the version that - as between the two versions of the order, the one that accords with the actual order that I granted on the 24th is the order acceptable to the majority of the parties.
>
> I was at pains in January to make it clear that the matching principle that I wanted to see applied and which formed a basis for the rationale of the order I gave at that time was the matching principle as discussed by the monitor in his sixth report. And that was clear then, it remains clear and, in my belief, the order sponsored by the monitor and the majority of the parties reflects that position. I am not satisfied that the order proposed by Mr. Robinson on behalf of his client [Lexxor] does that.
>
> Indeed, in my view, his order distorts the matching principle and could well result in a clawback or a diversion of funds from the unsecured creditor or the estate back to Lexxor contrary to the spirit and intent of my order of January the 24th and, indeed, as I see it, contrary to the proper meaning of the plan of arrangement itself.
>
> So I order and direct that the form of order to be used in the circumstances is the form of order agreed to by the majority of the parties.

THE TEST FOR LEAVE TO APPEAL

**14** Leave to appeal is available under the CCAA by virtue of s. 13. Sections 13 and 14(1) state as follows:

> 13. Except in the Yukon Territory, any person dissatisfied with an order or a decision made under this Act may appeal therefrom on obtaining leave of the judge appealed from or of the court or a judge of the court to which the appeal lies and on such terms as to security and in other respects as the judge or court directs.
> 14. (1) An appeal under section 13 lies to the highest court of final resort in or for the province in which the proceeding originated.

**15** The test for granting leave, as articulated in this Court, involves a single criterion subsuming four factors. The single criterion is that there must be serious and arguable grounds that are of real and significant interest to the parties: Resurgence Asset Management LLC v. Canadian Airlines Corporation, (2000), 261 A.R. 120, 2000 ABCA 149 ("Resurgence #1") at para 6; Luscar Ltd. v. Smoky River Coal Ltd., [1999] A.J. No. 185, 1999 ABCA 62 at para. 22; Resurgence Asset Management LLC v. Canadian Airlines Corporation (2000) 266 A.R. 131, 2000 ABCA 238 ("Resur-

gence #2") at para. 19; Re Multitech Warehouse Direct [1995] A.J. No. 663 at para. 3; 32 Alta. L.R. (3d) 62 at 63 (C.A.).

**16** The four factors subsumed in an assessment whether the criterion is present are:

(1) Whether the point on appeal is of significance to the practice;
(2) Whether the point raised is of significance to the action itself;
(3) Whether the appeal is prima facie meritorious or, on the other hand, whether it is frivolous; and
(4) Whether the appeal will unduly hinder the progress of the action: Resurgence #1 at para. 7; Resurgence #2 at para. 19.

**17** The first factor may be influenced by whether there is appellate authority on the question proposed to be considered on appeal: Resurgence #1 at para. 33. It is also interpreted broadly to include not only in the insolvency practice but the industry involving the claimant: Re Blue Range Resource Corp. (2001) 281 A.R. 172 at para. 1. It was argued by the unsecured creditors that the point on appeal had no significance to the insolvency practice because it involved an interpretation of the terms of a specific plan of arrangement. Therefore, it was not a point of significance in the sense used. Perhaps. But the timing of payment for oil and gas production in relation to the CCAA period may be of significance to the practice.

**18** The second factor - whether the point raised is of significance to the action itself - is conceded. In argument before me, Lexxor asserted that the proper application of the matching principle would result in a clawback of over a million dollars but Lexxor proposed to cap the clawback at a million dollars in any event of the result. The unsecured creditors indicated that the broader import of the matching principle as put forward by Lexxor would indeed have that result. So it is of significance to the parties.

**19** The third factor involves a consideration as to whether there appears to be an error in principle of law or a palpable and overriding error of fact or that the exercise of discretion by a supervising CCAA judge has been exercised improperly, such as by taking into consideration irrelevant factors or failing to consider relevant factors: Resurgence #1 at para. 41-42. Lexxor's counsel argued strenuously that the alleged misstatement of the matching principle was an error of law, subject to the standard of review of correctness. The other parties submitted that there was no error of law or principle, that the interpretation of the Plan and the adoption of the Monitor's proposal was at most an error of mixed law and fact or the exercise of discretion by the supervising judge. I agree.

**20** The standard of review that would govern the appeal is to be considered: Resurgence #2 at para. 42; Resurgence #1 at para. 28-29. Ancillary to these considerations are indications that a supervising chambers judge under the CCAA should be accorded considerable deference. Their decisions will be interfered with only in the event of unreasonable acts, errors in principle or manifest errors: UTI Energy Corp. v. Fracmaster Ltd. (1999) 244 A.R. 93 at para. 3. It has also been stated that an appellate court scrutinizing leave applications under the CCAA should exercise its powers sparingly, that a supervising CCAA judge has an ongoing management process similar to that of a judge making orders during a trial: Duke Energy Marketing Limited Partnership v. Blue Range Resource Corporation, [1999] A.J. No. 975, 1999 ABCA 255 at para. 3; Luscar Ltd at para. 62. Finally, the four factors are to be assessed in the context of determining whether the criterion has been met by ascribing appropriate weight to each of the elements of the general criterion: Resurgence #1 at para. 46.

APPLICATION IN THIS CASE

**21** Central to the issue proposed for appeal is the impact of the application of the matching principle either as propounded by Lexxor or as propounded by the Monitor. The issue is not whether the matching principle is to be applied in accordance with generally accepted accounting principles. It is whether Hart, J. erred in law in approving the Monitor's proposed application of the matching principle in his Sixth Report. In my view, he did not. No details were articulated as to what the error complained of was. Only that the words "generally accepted accounting principles" were absent from the formal order actually settled on when they were, in fact, included in the reasons. It is clear from the quotation from the Monitor's Sixth Report what Hart, J. had in mind. He said what he had in mind when he settled the minutes of the order. He, in effect, approved the Monitor's version of the matching principle, i.e. the recognition of revenue during the CCAA period and its availability to satisfy excluded claims. Neither the Monitor nor Hart, J. intended to extend "the matching principle" beyond revenue recognition. In other words, there was no intent to derive a new accounting from February 25 to July 23 on a full accrual basis according to the version put forward by Lexxor.

**22** Whether the appeal would unduly hinder the progress of the action was not strenuously argued. Apparently, an interim distribution can be made and there must be some delay because there is another contingent claim brought by one Martin which remains outstanding and which will delay a final distribution in any event. I am prepared to proceed on the basis that this factor would not and does not influence the decision to grant leave.

CONCLUSION

**23** What is fatal to the applicant's position here is the absence of any demonstrable or, with respect, arguable error in the decision of the supervising chambers judge. He did not pronounce on the matching principle as if he were writing a chapter of the Canadian Institute of Chartered Accountants ("CICA") Handbook in setting out generally accepted accounting principles. What he did do was adopt the Monitor's interpretation of fundamental accounting concepts for the purposes of revenue recognition during the CCAA period. Recognition in terms of revenue is a specialized term pursuant to the CICA Handbook at 1000.41 where it is indicated that "recognition is the process of including an item in the financial statements of an entity". It has a particular application to revenue in terms of the timing of it: See s. 3400 revenue .06, .07 of the CICA Handbook.

**24** Generally accepted accounting principles are defined at paragraph 1000 .59, .60, .61 of the CICA Handbook including departure and applicability. That terminology would not be helpful in a general sense to the resolution of the dispute between the parties here. The particular application of a fundamental accounting concept in terms of revenue recognition and measurement, as recommended in detail by the Monitor, is what is relevant, and that is what Hart, J. ordered.

**25** The application for leave to appeal is denied.

WITTMANN J.A.

cp/e/qw/qlmmm/qlhcs

# Tab 5

*Indexed as:*

# Blue Range Resource Corp. (Re)

**IN THE MATTER OF The Companies' Creditors Arrangement Act, R.S.C. 1985, C. C-36, as amended**
**AND IN THE MATTER OF Blue Range Resource Corporation**

[2000] A.J. No. 14

2000 ABQB 4

[2000] 4 W.W.R. 738

76 Alta. L.R. (3d) 338

259 A.R. 30

15 C.B.R. (4th) 169

94 A.C.W.S. (3d) 223

Action No. 9901-04070

Alberta Court of Queen's Bench
Judicial District of Calgary

**Romaine J.**

Judgment: filed January 10, 2000.

(84 paras.)

**Counsel:**

R.J. (Bob) Wilkins and Gary Befus, for Big Bear Exploration Ltd.
A. Robert Anderson and Bryan Duguid, for Enron Trade & Capital Resources Canada Corp.
Glen H. Poelman, for the Creditors' Committee.
Virginia A. Engel, for MRF 1998 II Limited Partnership.

REASONS FOR JUDGMENT

ROMAINE J.:--

INTRODUCTION

**1** This is an application for determination of three preliminary issues relating to a claim made by Big Bear Exploration Ltd. against Blue Range Resource Corporation, a company to which the Companies' Creditors Arrangement Act, R.S.C. 1985, c.C-36, as amended, applies. Big Bear is the sole shareholder of Blue Range, and submits that its claim should rank equally with claims of unsecured creditors. The preliminary issues relate to the ranking of Big Bear's claim, the scope of its entitlement to pursue its claim and whether Big Bear is the proper party to advance the major portion of the claim.

**2** The Applicants are the Creditors' Committee of Blue Range and Enron Canada Corp., a major creditor. Big Bear is the Respondent, together with the MRF 1998 II Limited Partnership, whose partners are in a similar situation to Big Bear.

FACTS

**3** Between October 27, 1998 and February 2, 1999, Big Bear took the following steps:

(a) it purchased shares of Blue Range for cash through The Toronto Stock Exchange on October 27 and 29, 1998;
(b) it undertook a hostile takeover bid on November 13, 1998, by which it sought to acquire all of the issued and outstanding Blue Range shares;
(c) it paid for the Blue Range shares sought through the takeover bid by way of a share exchange: Blue Range shareholders accepting Big Bear's offer received 11 Big Bear shares for each Blue Range share;
(d) it issued Big Bear shares from treasury to provide the shares used in the share exchange.

**4** The takeover bid was accepted by Blue Range shareholders and on December 12, 1998, Big Bear acquired control of Blue Range. It is now the sole shareholder of Blue Range.

**5** Big Bear says that its decision to undertake the takeover was made in reliance upon information publicly disclosed by Blue Range regarding its financial situation. It says that after the takeover, it discovered that the information disclosed by Blue Range was misleading, and in fact the Blue Range shares were essentially worthless.

**6** Big Bear as the sole shareholder of Blue Range entered into a Unanimous Shareholders' Agreement pursuant to which Big Bear replaced and took on all the rights, duties and obligations of the Blue Range directors. Using its authority under the Unanimous Shareholders' Agreement, Big Bear caused Blue Range to apply for protection under the CCAA. An order stipulating that Blue Range is a company to which the CCAA applies was granted on March 2, 1999.

**7** On April 6, 1999, LoVecchio, J. issued an order which provides, in part, that:

(a) all claims of any nature must be proved by filing with the Monitor a Notice of Claim with supporting documentation, and

(b) claims not received by the Monitor by May 7, 1999, or not proved in accordance with the prescribed procedures, are forever barred and extinguished.

**8** Big Bear submitted a Notice of Claim to the Monitor dated May 5, 1999 in the amount of $151,317,298 as an unsecured claim. It also filed a Notice of Motion on May 5, 1999, seeking an order lifting the stay of proceedings granted by the March 2, 1999 order for the purpose of filing a statement of claim against Blue Range. Big Bear's application for leave to file its statement of claim was denied by LoVecchio, J. on May 11, 1999.

**9** On May 21, 1999, the Monitor issued a Notice of Dispute disputing in full the Big Bear claim. Big Bear filed a Notice of Motion on May 31, 1999 for:

(a) a declaration that the unsecured claim of Big Bear is a meritorious claim against Blue Range; and
(b) an order directing the expeditious trial and determination of the issues raised by the unsecured claim of Big Bear.

**10** On October 4, 1999, LoVecchio, J. directed that there be a determination of two issues in respect of the Big Bear unsecured claim by way of a preliminary application. On October 28, 1999, I defined the two issues and added a third one.

**11** Big Bear's Notice of Claim sets out the nature and amount of its claim against Blue Range. The amount is particularized by the schedule attached to the Notice of Claim, which identifies the claim as being comprised of the following components:

(a) the price of shares acquired for cash on October 27 and 29, 1998 ($724,454.91);
(b) the value of shares acquired by means of the share exchange of Big Bear treasury shares for Blue Range shares held by Blue Range shareholders ($147,687,298); and
(c) "transaction costs," being costs incurred by Big Bear for consultants, professional advisers, filings, financial services, and like matters incidental to the share purchases generally, and the takeover bid in particular ($3,729,498).

ISSUE #1

**12** With respect to the alleged share exchange loss, without considering the principle of equitable subordination, is Big Bear:

(a) an unsecured creditor of Blue Range that ranks equally with the unsecured creditors of Blue Range; or
(b) a shareholder of Blue Range that ranks after the unsecured creditors of Blue Range.

**13** At the hearing, this question was expanded to include reference to the transaction costs and cash share purchase damage claims in addition to the alleged share exchange loss.

Summary of Decision

**14** The nature of the Big Bear claim against Blue Range for an alleged share exchange loss, transaction costs and cash share purchase damages is in substance a claim by a shareholder for a return of what it invested qua shareholder. The claim therefore ranks after the claims of unsecured creditors of Blue Range.

Analysis

**15** The position of the Applicants is that the share exchange itself was clearly an investment in capital, and that the claim for the share exchange loss derives solely from and is inextricably intertwined with Big Bear's interest as a shareholder of Blue Range. The Applicants submit that there are therefore good policy reasons why the claim should rank after the claims of unsecured creditors of Blue Range, and that basic corporate principles, fairness and American case law support these policy reasons. Big Bear submits that its claim is a tort claim, allowable under the CCAA, and that there is no good reason to rank the claim other than equally with unsecured creditors. Big Bear submits that the American cases cited are inappropriate to a Canadian CCAA proceeding, as they are inconsistent with Canadian law.

**16** There is no Canadian law that deals directly with the issue of whether a shareholder allegedly induced by fraud to purchase shares of a debtor corporation is able to assert its claim in such a way as to achieve parity with other unsecured creditors in a CCAA proceeding. It is therefore necessary to start with basic principles governing priority disputes.

**17** It is clear that in common law shareholders are not entitled to share in the assets of an insolvent corporation until after all the ordinary creditors have been paid in full: Re: Central Capital Corp. (1996), 132 D.L.R. (4th) 223 (Ont. C.A.) at page 245; Canada Deposit Insurance Corp. v. Canadian Commercial Bank (1992), 97 D.L.R. (4th) 385 (S.C.C.) at pages 402 and 408. In that sense, Big Bear acquired not only rights but restrictions under corporate law when it acquired the Blue Range shares.

**18** There is no doubt that Big Bear has exercised its rights as a shareholder of Blue Range. Pursuant to the Unanimous Shareholders' Agreement, it authorized Blue Range to file an application under the CCAA "to attempt to preserve the equity value of [Blue Range] for the benefit of the sole shareholder of [Blue Range]" (Bourchier November 1, 1999 affidavit). It now attempts to recover its alleged share exchange loss through the claims approval process and rank with unsecured creditors on its claim. The issue is whether this is a collateral attempt to obtain a return on an investment in equity through equal status with ordinary creditors that could not be accomplished through its status as a shareholder.

**19** In Canada Deposit Insurance (supra), the Supreme Court of Canada considered whether emergency financial assistance provided to the Canadian Commercial Bank by a group of lending institutions and government was properly categorized as a loan or as an equity investment for the purpose of determining whether the group was entitled to rank pari passu with unsecured creditors in an insolvency. The court found that, although the arrangement was hybrid in nature, combining elements of both debt and equity, it was in substance a loan and not a capital investment. It is noteworthy that the equity component of the arrangement was incidental, and in fact had never come into effect, and that the agreements between the parties clearly supported the characterization of the arrangement as a loan.

**20** Central Capital (supra) deals with the issue of whether the holders of retractable preferred shares should be treated as creditors rather than shareholders under the CCAA because of the re-

traction feature of the shares. Weiler, J.A. commented at page 247 of the decision that it is necessary to characterize the true nature of a transaction in order to decide whether a claim is a claim provable in either bankruptcy or under the CCAA. She stated that a court must look to the surrounding circumstances to determine "whether the true nature of the relationship is that of a shareholder who has equity in the company or whether it is that of a creditor owed a debt or liability."

**21** The court in Central Capital found that the true nature of the relationship between the preferred shareholders and the debtor company was that of shareholders. In doing so, it considered the statutory provision that prevents a corporation from redeeming its shares while insolvent, the articles of the corporation, and policy considerations. In relation to the latter factor, the court commented that in an insolvency where debts will exceed assets, the policy of federal insolvency legislation precludes shareholders from looking to the assets until the creditors have been paid (supra, page 257).

**22** In this case, the true nature of Big Bear's claim is more difficult to characterize. There may well be scenarios where the fact that a party with a claim in tort or debt is a shareholder is coincidental and incidental, such as where a shareholder is also a regular trade creditor of a corporation, or slips and falls outside the corporate office and thus has a claim in negligence against the corporation. In the current situation, however, the very core of the claim is the acquisition of Blue Range shares by Big Bear and whether the consideration paid for such shares was based on misrepresentation. Big Bear had no cause of action until it acquired shares of Blue Range, which it did through share purchases for cash prior to becoming a majority shareholder, as it suffered no damage until it acquired such shares. This tort claim derives from Big Bear's status as a shareholder, and not from a tort unrelated to that status. The claim for misrepresentation therefore is hybrid in nature and combines elements of both a claim in tort and a claim as shareholder. It must be determined what character it has in substance.

**23** It is true that Big Bear does not claim recission. Therefore, this is not a claim for return of capital in the direct sense. What is being claimed, however, is an award of damages measured as the difference between the "true" value of Blue Range shares and their "misrepresented" value - in other words, money back from what Big Bear "paid" by way of consideration. Although the matter is complicated by reason that the consideration paid for Blue Range shares by Big Bear was Big Bear treasury shares, the Notice of Claim filed by Big Bear quantifies the loss by assigning a value to the treasury shares. A tort award to Big Bear could only represent a return of what Big Bear invested in equity of Blue Range. It is that kind of return that is limited by the basic common law principal that shareholders rank after creditors in respect of any return on their equity investment. Whether payment of the tort liability by Blue Range would affect Blue Range's stated capital account is irrelevant, since the shares were not acquired from Blue Range but from its shareholders.

**24** In considering the question of the characterization of this claim, it is noteworthy that Mr. Tonken in his March 2, 1999 affidavit in support of Blue Range's application to apply the CCAA did not include the Big Bear claim in his list of estimated outstanding debt, accounts payable and other liabilities. The affidavit does, however, set out details of the alleged mispresentations.

**25** I find that the alleged share exchange loss derives from and is inextricably intertwined with Big Bear's shareholder interest in Blue Range. The nature of the claim is in substance a claim by a shareholder for a return of what it invested qua shareholder, rather than an ordinary tort claim.

**26** Given the true nature of the claim, where should it rank relative to the claims of unsecured creditors?

**27** The CCAA does not provide a statutory scheme for distribution, as it is based on the premise that a Plan of Arrangement will provide a classification of claims which will be presented to creditors for approval. The Plan of Arrangement presented by CNRL in the Blue Range situation has been approved by creditors and sanctioned by the Court. Section 3.1 of the Plan states that claims shall be grouped into two classes: one for Class A Claimants and one for Class B Claimants, which are described as claimants that are "unsecured creditors" within the meaning of the CCAA, but do not include "a Person with a Claim which, pursuant to Applicable Law, is subordinate to claims of trade creditors of any Blue Range Entities." The defined term "Claims" includes indebtedness, liability or obligation of any kind. Applicable Law includes orders of this Court.

**28** Although there are no binding authorities directly on point on the issue of ranking, the Applicants submit that there are a number of policy reasons for finding that the Big Bear claim should rank subordinate to the claims of unsecured creditors.

**29** The first policy reason is based on the fundamental corporate principle that claims of shareholders should rank below those of creditors on an insolvency. Even though this claim is a tort claim on its face, it is in substance a claim by a shareholder for a return of what it paid for shares by way of damages. The Articles of Blue Range state that a holder of Class A Voting Common Shares is entitled to receive the "remaining property of the corporation upon dissolution in equal rank with the holders of all other common shares of the Corporation". As pointed out by Laskin, J. in Central Capital (supra at page 274):

> Holding that the appellants do not have provable claims accords with sound corporate policy. On the insolvency of a company the claims of creditors have always ranked ahead of the claims of shareholders for the return of their capital. Case law and statute law protect creditors by preventing companies from using their funds to prejudice creditors' chances of repayment. Creditors rely on these protections in making loans to companies.

**30** Although what is envisaged here is not that Blue Range will pay out funds to retract shares, the result is the same: Blue Range would be paying out funds to the benefit of its sole shareholder to the prejudice of third-party creditors.

**31** It should be noted that this is not a case, as in the recent restructuring of Eatons under the CCAA, where a payment to the shareholders was clearly set out in the Plan of Arrangement and approved by the creditors and the court.

**32** As counsel for Engage Energy, one of the trade creditors, stated on May 11, 1999 during Big Bear's application for an order lifting the stay order under the CCAA and allowing Big Bear to file a statement of claim:

> We've gone along in this process with a general understanding in our mind as to what the creditor pool is, and as recently as middle of April, long after the evidence will show that Big Bear was identifying in its own mind the existence of this claim, public statements were continuing to be made, setting out the creditor

> pool, which did not include this claim. And this makes a significant difference in how people react to supporting an ongoing plan...

**33** Another policy reason which supports subordinating the Big Bear claim is a recognition that creditors conduct business with corporations on the assumption that they will be given priority over shareholders in the event of an insolvency. This assumption was referred to by Laskin, J. in Central Capital (supra), in legal textbooks (Hadden, Forbes and Simmonds, Canadian Business Organizations Law Toronto: Butterworths, 1984 at 310, 311), and has been explicitly recognized in American case law. The court in In the Matter of Stirling Homex Corporation, 579 F. 2d 206 (1978) U.S.C.A. 2nd Cir. at page 211 referred to this assumption as follows:

> Defrauded stockholder claimants in the purchase of stock are presumed to have been bargaining for equity type profits and assumed equity type risks. Conventional creditors are presumed to have dealt with the corporation with the reasonable expectation that they would have a senior position against its assets, to that of alleged stockholder claims based on fraud.

**34** The identification of risk-taking assumed by shareholders and creditors is not only relevant in a general sense, but can be illustrated by the behaviour of Big Bear in this particular case. In the evidence put before me, Big Bear's president described how, in the course of Big Bear's hostile takeover of Blue Range, it sought access to Blue Range's books and records for information, but had its requests denied. Nevertheless, Big Bear decided to pursue the takeover in the absence of information it knew would have been prudent to obtain. Should the creditors be required to share the result of that type of risk-taking with Big Bear? The creditors are already suffering the results of misrepresentation, if it occurred, in the inability of Blue Range to make full payment on its trade obligations.

**35** The Applicants submit that a decision to allow Big Bear to stand pari passu with ordinary creditors would create a fundamental change in the assumptions upon which business is carried on between corporations and creditors, requiring creditors to re-evaluate the need to obtain secured status. It was this concern, in part, that led the court in Stirling Homex to find that it was fair and equitable that conventional creditors should take precedence over defrauded shareholder claims (supra at page 208).

**36** The Applicants also submit that the reasoning underlying the Central Capital case (where the court found that retraction rights in shares do not create a debt that can stand equally with the debt of shareholders) and the cases where shareholders have attempted to rescind their shareholdings after a corporation has been found insolvent is analogous to the Big Bear situation, and the same result should ensue.

**37** It is clear that, both in Canada and in the United Kingdom, once a company is insolvent, shareholders are not allowed to rescind their shares on the basis of misrepresentation: McAskill v. The Northwestern Trust Company, [1926] S.C.R. 412 at 419; Milne v. Durham Hosiery Mills Ltd., [1925] 3 D.L.R. 725 (Ont. S.C.A.D.); Trusts and Guarantee Co. v. Smith (1923), 54 O.L.R. 144 (Ont. S.C.A.D.); Re: National Stadium Ltd. (1924), 55 O.L.R. 199 (Ont. S.C.); Oaks v. Turquend [1861-73] All E.R. Rep. 738 (H.L.) at page 743-744.

**38** The court in McAskill (supra at page 419) in obiter dicta refers to a claim of recission for fraud, and comments that the right to rescind in such a case may be lost due to a change of circum-

stances making it unjust to exercise the right. Duff, J. then refers to the long settled principle that a shareholder who has the right to rescind his shares on the ground of misrepresentation will lose that right if he fails to exercise it before the commencement of winding-up proceedings, and comments:

> The basis of this is that the winding-up order creates an entirely new situation, by altering the relations, not only between the creditors and the shareholders, but also among the shareholders inter se.

**39** This is an explicit recognition that in an insolvency, a corporation may not be able to satisfy the claims of all creditors, thus changing the entire complexion of the corporation, and rights that a shareholder may have been entitled to prior to an insolvency can be lost or limited.

**40** In the Blue Range situation, Big Bear has actively embraced its shareholder status despite the allegations of misrepresentation, putting Blue Range under the CCAA in an attempt to preserve its equity value and, in the result, holding Blue Range's creditors at bay. Through the provision of management services, Big Bear has participated in adjudicating on the validity of creditor claims, and has then used that same CCAA claim approval process to attempt to prove its claim for misrepresentation. It may well be inequitable to allow Big Bear to exercise all of the rights it had arising from its status as shareholder before CCAA proceedings had commenced without recognition of Blue Range's profound change of status once the stay order was granted. Certainly, given the weight of authority, Big Bear would not likely have been entitled to rescind its purchase of shares on the basis of misrepresentation, had the Blue Range shares been issued from treasury.

**41** Finally, the Applicants submit that it is appropriate to take guidance from certain American cases which are directly on point on this issue.

**42** The question I was asked to address expressly excludes consideration of the principle of "equitable subordination". The Applicants submit that the principle of equitable subordination that is excluded for the purpose of this application is the statutory principle codified in the U.S. Bankruptcy Code in 1978 (Bankruptcy Code, Rules and Forms (1999 Ed.) West Group, Subchapter 1, Section 510 (b)). This statutory provision requires notice and a full hearing, and relates to the ability of a court to subordinate an allowed claim to another claim using the principles of equitable subordination set out and defined in case law. The Applicants submit, however, that I should look to three American cases that preceded this statutory codification and that dealt with subordination of claims by defrauded shareholders to the claims of ordinary unsecured creditors on an equitable basis.

**43** The first of these cases is Stirling Homex (supra). The issue dealt with by the United States Court of Appeals, Second Circuit, is directly on point: whether claims filed by allegedly defrauded shareholders of a debtor corporation should be subordinated to claims filed by ordinary unsecured creditors for the purposes of formulating a reorganization plan. The court referred to the decision of Pepper v. Litton (308 U.S. 295 at page 305, 60 S.Ct. 238, 84 L. Ed. 281 (1939)) where the Supreme Court commented that the mere fact that a shareholder has a claim against the bankrupt company does not mean it must be accorded pari passu status with other creditors, and that the subordination of that claim may be necessitated by principles of equity. Elaborating on this, the court in Stirling Homex (supra at page 213) stated that where the debtor corporation is insolvent, the equities favour the general creditors rather than the allegedly defrauded shareholders, since in this case, the real party against which the shareholders are seeking relief is the general creditors whose percentage of realization will be reduced if relief is given to the shareholders. The court quotes a comment made by an earlier Court of Appeals (Newton National Bank v. Newbegin, 74 F. 135, 140 (8th Cir. 1896):

> When a corporation becomes bankrupt, the temptation to lay aside the garb of a stockholder, on one pretense or another, and to assume the role of creditor, is very strong, and all attempts of that kind should be viewed with suspicion.

**44** Although the court in Stirling Homex refers to its responsibility under US bankruptcy law to ensure that a plan of reorganization is "fair and equitable" and to the "absolute priority" rule of classification under US bankruptcy principles, it is clear that the basis for its decision is the general rule of equity, a "sense of simple fairness" (supra, page 215). Despite the differences that may exist between Canadian and American insolvency law in this area, this case is persuasive for its reasoning based on equitable principles.

**45** If Big Bear's claim is allowed to rank equally with unsecured creditors, this will open the door in many insolvency scenarios for aggrieved shareholders to claim misrepresentation or fraud. There may be many situations where it could be argued that there should have been better disclosure of the corporation's declining fortunes, for who would deliberately have invested in a corporation that has become insolvent. Although the recognition that this may greatly complicate the process of adjudicating claims under the CCAA is not of itself sufficient to subordinate Big Bear's claim, it is a factor that may be taken into account.

**46** The Applicants also cite the case of In re U.S. Financial Incorporated 648 F. 2d 515 (1980)(U.S.C.A. 9th Cir.). This case is less useful, as it was decided primarily on the basis of the absolute priority rule, but while the case was not decided on equitable grounds, the court commented that support for its decision was found in the recognition of the importance of recognizing differences in expectations between creditors and shareholders when classifying claims (supra at page 524). The court also stated that although both creditors and shareholders had been victimized by fraud, it was equitable to impose the risks of insolvency and illegality on the shareholders whose investment, by its very nature, was a risky one.

**47** The final case cited to me on this issue is In re THC Financial 679 F. 2d 784 (1982) (U.S.C.A. 9th Cir.), where again the court concluded that claims of defrauded shareholders must be subordinated to the claims of the general creditors. The court commented that the claimant shareholders had bargained for equity-type profits and equity-type risks in purchasing their shares, and one such risk was the risk of fraud. As pointed out previously, Big Bear had an appreciation of the risks of proceeding with its takeover bid without access to the books and records of Blue Range and took the deliberate risk of proceeding in any event.

**48** In THC Financial, the claimants argued that since they had a number of possible causes of action in addition to their claim of fraud, they should not subordinated merely because they were shareholders. The court found, however, that their claim was essentially that of defrauded shareholders and not as victims of an independent tort. All of the claimants' theories of recovery were based on the same operative facts - the fraudulent scheme.

**49** Big Bear submits that ascribing some legal impediment to a shareholder pursuing a remedy in tort against a company in which it holds shares violates the principle set out in Salomon v. Salomon and Company, Limited [1897] A.C. 22 (H.L.) that corporations are separate and distinct entities from their shareholders. In my view, this is not in issue. What is being sought here is not to limit a tort action by a shareholder against a corporation but to subordinate claims made qua shareholder to claims made by creditors in an insolvency situation. That shareholder rights with respect

to claims against a corporation are not unlimited has already been established by the cases on rescission and recognized by statutory limitations on redemption and retraction. In this case, the issue is not the right to assert the claim, but the right to rank with creditors in the distribution of the proceeds of a pool of assets that will be insufficient to cover all claims. No piercing of the corporate veil is being suggested or would result.

**50** Counsel for Big Bear cautions against the adoption of principles set out in the American cases on the basis that some decisions on equitable subordination require inequitable conduct by the claimant as a precondition to subordinating a claim, referring to a three-part test set out in a number of cases. This discussion of the inequitable conduct precondition takes place in the broader context of equitable subordination for any cause as it is codified under Section 510 of the US Bankruptcy Code. In any event, it appears that more recent American cases do not restrict the use of equitable subordination to cases of claimant misconduct, citing, specifically, that stock redemption claims have been subordinated in a number of cases even when there is no inequitable conduct by the shareholder. "Stock redemption" is the term used for cases involving fraud or misrepresentation: U.S. v. First Truck Lines, Inc. (1996) 517 U.S. 535; SPC Plastics Corporation et al v. Griffiths et al (1998) 6th Circuit Case No. 88-21236. Some of the American cases draw a distinction between cases where misconduct is generally required before subordination will be imposed and cases where "the claim itself is of a status susceptible to subordination, such as...a claim for damages arising from the purchase ... of a security of the debtor": U.S. v. First Truck Lines, Inc. (supra, at paragraph 542).

**51** The issue of whether equitable subordination as codified in Section 510 of the U.S. Bankruptcy Code should form part of the law in Canada has been raised in several cases but left undecided. Big Bear submits that these cases establish that if equitable subordination is to be part of Canadian law, it should be on the basis of the U.S. three-part test which includes the condition of inequitable conduct. Again, I cannot accept this submission. It is true that Iacobucci, J. in Canada Deposit Insurance Corp., while he expressly refrains from deciding whether a comparable doctrine should exist in Canada, refers to the three-part test and states that he does not view the facts of the Canada Deposit Insurance Corp. case as giving rise to inequitable conduct. It should be noted, however, that that case did not involve a claim by a shareholder at all, since the lenders had never received the securities that were an option under the agreements, and that the relationship had at this point in the case been characterized as a debtor/creditor relationship.

**52** At any rate, this case, together with Olympia and York Developments Ltd. v. Royal Trust Co. [1993] O.J. No. 181 (Ont. G.D.) and Unisource Canada Inc. v. HongKong Bank of Canada [1998] O.J. No. 5586 (Ont. H.C.) all refer to the doctrine of equitable subordination codified in the U.S. Bankruptcy Code which is not in issue here. The latter two cases appear to have accepted the erroneous proposition that inequitable misconduct is required in all cases under the American doctrine.

**53** Big Bear also submits that the equitable principles that exist in U.S. law which have led the courts to ignore separate corporate personality in the case of subsidiary corporations are related to equitable principles used to subordinate shareholder claims. The basis for this submission appears to be a reference by the British Columbia Court of Appeal in B.G. Preeco I (Pacific Coast) Ltd. v. Bon Street Holdings Ltd. et al (1989) 43 B.L.R. 68 (1989) to the Pepper v. Litton case (supra) and the so-called "Deep Rock doctrine" under American law. I do not see a link between the comments made in Pepper v. Litton and referred to in B.C. Preeco on an entirely different issue and comments

concerning the court's equitable jurisdiction in the case of claims by shareholders against insolvent corporations.

**54** I acknowledge that caution must be used in following the approach taken in American cases to ensure that the principles underlying such approach do not arise from differences between U.S. and Canadian law. However, I find that the comments made by the American courts in these cases relating to the policy reasons for subordinating defrauded shareholder claims to those of ordinary creditors are persuasive, as they are rooted in principles of equity that are very similar to the equitable principles used by Canadian courts.

**55** American cases are particularly useful in the areas of commercial and insolvency law given that the larger economy in the United States generates a wider variety of issues that are adjudicated by the courts. There is precedent for the use of such cases: Laskin, J. in Central Capital Corp. (supra) used the analysis set out in American case law on whether preferred shareholders can claim as creditors in an insolvency to help him reach his conclusion.

**56** The three American cases decided on this direct issue before the 1978 statutory codification of the law of equitable subordination are not based on a doctrine of American law that is inconsistent with or foreign to Canadian common law. It is not necessary to adopt the U.S. absolute priority rule to follow the approach they espouse, which is based on equitable principles of fairness and policy. There is no principled reason to disregard the approach set out in these cases, which have application to Canadian business and economy, and I have found them useful in considering this issue.

**57** Based on my characterization of the claim, the equitable principles and considerations set out in the American cases, the general expectations of creditors and shareholders with respect to priority and assumption of risk, and the basic equitable principle that claims of defrauded shareholders should rank after the claims of ordinary creditors in a situation where there are inadequate assets to satisfy all claims, I find that Big Bear must rank after the unsecured creditors of Blue Range in respect to the alleged share exchange loss, the claim for transaction costs and the claim for cash share purchase damages.

ISSUE #2

**58** Assuming (without admitting) misrepresentation by Blue Range and reliance on it by Big Bear, is the alleged share exchange loss a loss or damage incurred by Big Bear and, accordingly, is Big Bear a proper party to advance the claim for such a loss?

Summary of Decision

**59** As the alleged share exchange loss is not a loss incurred by Big Bear, Big Bear is not the proper party to advance this claim.

Analysis

**60** The Applicants submit that negligence is only actionable if a plaintiff can prove that it suffered damages, as the purpose of awarding damages in tort is to compensate for actual loss. This is a significant difference between damages in tort and damages in contract. In order for a plaintiff to have a cause of action in negligent misrepresentation, it must satisfy the court as to the usual elements of duty of care and breach thereof, and it must establish that it has sustained damages from that breach.

**61** The Applicants argue that Big Bear did not suffer any damages arising from the share exchange. The Big Bear shares used in the share exchange came from treasury: Big Bear did not use any corporate funds or corporate assets to purchase the Blue Range shares. As the shares used in the exchange did not exist prior to the transaction, Big Bear was essentially in the same financial position pre-issuance as it was post-issuance in terms of its assets and liabilities. The nature and composition of Big Bear's assets did not change as the treasury shares were created and issued for the sole purpose of the share exchange. Therefore, Big Bear did not sustain a loss in the amount of the value of the shares. The Applicants submit that the only potential loss is that of the pre-takeover shareholders of Big Bear, as the value of their shares may have been diluted as a result of the share exchange. However, even if there was such a loss, Big Bear is not the proper party to pursue such an action. Just as shareholders may not bring an action for a loss which properly belongs to the corporation, a corporation may not bring an action for a loss directly incurred by its shareholders.

**62** Big Bear claims that it is entitled to recover the value of the Big Bear shares that were issued in furtherance of the share exchange. It says that it can prove all the elements of negligent misrepresentation: there was a special relationship; material misrepresentations were made to Big Bear; those representations were made negligently; Big Bear relied on those representations; and Big Bear suffered damage.

**63** It submits that damages for negligent misrepresentation are calculated as the difference between the represented value of the shares less their sale value. Big Bear contends that it matters not that the consideration for the Blue Range shares was Big Bear shares issued from treasury. As long as the consideration is adequate consideration for legal purposes, its form does not affect the measure of damages awarded by the courts for negligent misrepresentation. Big Bear says that it bargained for a company with a certain value, and, in doing so, it gave up its own shares worth that value. Therefore, Big Bear submits that it clearly incurred a loss.

**64** Big Bear submits that it is the proper party to pursue this head of damages. While the corporation has met the test for negligent misrepresentation, the shareholders likely could not, as the representations in questions were not made to them. In any event, Big Bear indicates that it does not claim for any damages caused by dilution of the shares. It also notes that a claim for dilution would not be the same as the face value of the shares issued in the share exchange, which is the amount claimed in the Notice of Claim.

**65** Big Bear's claim is in tort, not contract. This is an important distinction, as the issue at hand concerns the measure of damages. The measure of damages is not necessarily the same in contract as it is in tort.

**66** It is a first principle of tort law that a person is entitled to be put in the position, insofar as possible, that he or she was before the tort occurred. While the courts were historically loath to award damages for pure economic loss, this position was softened in Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd., [1964] A.C. 465 (H.L.) where the court confirmed that damages could be recovered in this type of case. When assessing damages for negligent misrepresentation resulting in pure economic loss, the goal is to put the party who relied on the misrepresentation in the position which it would have been in had the misrepresentation not occurred. While the parties to this application appear to agree on this principle, it is the application thereof with which they disagree.

**67** The proper measure of damages in cases of misrepresentation is discussed in S.M. Waddams, The Law of Damages (Toronto: Canada Law Book Inc., Looseleaf, Dec. 1998), where the author states:

> The English and Canadian cases have consistently held that the proper measure [with respect to fraudulent misrepresentation] is the tortious measure, that is the amount of money required to put the plaintiff in the position that would have been occupied not if the statement had been true but if the statement had not been made. The point was made clearly in McConnel v. Wright , [1903] 1 Ch. 546 (C.A.):
>
> > It is not an action for breach of contract, and, therefore, no damages in respect of prospective gains which the person contracting was entitled by his contract to expect come in, but it is an action of tort - it is an action for a wrong done whereby the plaintiff was tricked out of certain money in his pocket; and therefore, prima facie, the highest limit of his damages is the whole extent of his loss, and that loss is measured by the money which was in his pocket and is now in the pocket of the company. That is the ultimate, final, highest standard of his loss. (at 5-19, 5-20)
>
> ...
>
> Since the decision of the House of Lords in 1963 in Hedley Byrne Ltd. v. Heller & Partners Ltd., [1964] A.C. 465 (H.L.) it has been established that an action lies for negligent misrepresentation causing economic loss. It naturally follows from acceptance of out-of pocket loss rather than the contractual measure as the basic measure of damages for fraud, that the same basic measure applies to negligent misrepresentation. (at 5-28).

**68** Big Bear claims to be entitled to the difference between the actual value and the exchange value of the shares. The flaw in this assertion is that it focuses on what Big Bear bargained for as opposed to what it actually received, which is akin to a contractual measure of damages. Big Bear clearly states that it is not maintaining an action in contract, only in tort. Damages in tort are limited to the losses which a plaintiff actually incurs as a result of the misrepresentation. Thus, Big Bear is not entitled to recover what it expected to receive as a result of the transaction; it is entitled to be compensated only for that which it actually lost. In other words, what did Big Bear have before the loss which it did not have afterwards? To determine what losses Big Bear actually sustained, its position after the share exchange must be compared with its position prior to the share exchange.

**69** The situation at hand is unique. Due to a negligent misrepresentation, Big Bear was induced to give up something which, although it had value, was of substantially no cost to the corporation, and in fact did not even exist but for the misrepresentation. Big Bear created shares which had a value for the purpose of the share exchange, in that Blue Range shareholders were willing to accept them in exchange for Blue Range shares. However, outside of transaction costs, those shares had no actual cost to Big Bear, as compared to the obvious costs associated with a payment by way of cash or tangible assets. Big Bear cannot say that after the share exchange, it had lost approximately $150 million dollars, because the shares essentially did not exist prior to the transaction, and the cost of

creating those shares is not equivalent to their face value. Big Bear retains the ability to issue a limitless number of shares from treasury in the future; any loss in this regard would not be equivalent to the actual value of the shares. Therefore, all that is required to return Big Bear to its pre-misrepresentation position is compensation for the actual costs associated with issuing the shares.

**70** That Big Bear has not incurred a loss in the face value of the exchanged shares is demonstrated by comparing the existing facts with hypothetical situations in which such a loss may be found. Had Big Bear been required to pay for the shares used in the exchange, for instance, by purchasing shares from existing Big Bear shareholders, there would have been a clear loss of funds evidenced in the Big Bear financial statements. Big Bear's financial position prior to the exchange would have been significantly better than its position afterwards. However, no such difference results from the mere exchange of newly-issued shares. If there had been evidence that Big Bear was or could be compelled to redeem or retract the new shares at the value assigned to them at the time of the share exchange, Big Bear may have a loss in the amount of the exchange value of the shares. However, there is no evidence of such a redemption or retraction feature attaching to these shares.

**71** In sum, Big Bear's position prior to the share exchange is that the Big Bear shares issued as part of the exchange did not exist. As a result of the alleged misrepresentation, Big Bear issued shares from treasury. These shares would not have been issued but for the misrepresentation. All that is required to put Big Bear back into the position it was in prior to the negligent misrepresentation is compensation for the cost of issuing the shares, which is not the same as the exchange value of those shares. Although this is somewhat of an anomalous situation, it is consistent with the accepted tort principle that, except in cases warranting punitive damages, damages in tort are awarded to compensate for actual loss. A party may not recover in tort for a loss of something it never had. Indeed, if Big Bear was awarded damages for the share exchange equal to what it has claimed, it would be in a better position financially than it was prior to the exchange. To the extent that shareholders would indirectly benefit, they would not only be Big Bear's pre-exchange shareholders, who may have suffered a dilution loss, but a new group of shareholders, including former Blue Range shareholders who participated in the exchange.

**72** Big Bear submits that it incurred other losses as a result of the misrepresentation. Transaction costs incurred in the share exchange may be properly characterized as damages in tort, as those costs would not have been incurred but for the negligent misrepresentation. The same is true for the Big Bear claim for cash expended to purchase Blue Range shares prior to the share exchange. However, as I have indicated in my decision on Issue #1, Big Bear's claim for transaction costs and for cash share purchase damages ranks after the claims of other unsecured creditors. There may also be losses such as loss of ability to raise equity. There was no evidence of this before me in this application, and I have addressed Big Bear's ability to advance a claim for this type of loss in the decision relating to Issue #3.

**73** Finally, there may also be a loss in the form of dilution of the value of the Big Bear shares. However, as Big Bear admits in its submissions, no such claim is made by the corporation, and any loss relating to a diluted share value would not be the same amount as the exchange value of the shares.

**74** In the result, I find that Big Bear is not the proper party to pursue a claim for the alleged share exchange loss.

ISSUE #3

**74a** Is Big Bear entitled to make or advance by way of argument in these proceedings the claims represented by the heads of damage specified in the draft Statement of Claim set out at Exhibit "F" to the affidavit of A. Jeffrey Tonken dated June 25, 1999?

[The Court did not paragraph number Issue #3. Quicklaw has assigned the number 74a.]

**75** In addition to claims for damages for negligent misrepresentation, the claims that are set out in the draft Statement of Claim are claims for remedies for oppressive and unfairly prejudicial conduct and claims for loss of opportunity to pursue valuable investments and endeavours and loss of ability to raise equity.

Summary of Decision

**76** Given the orders made by LoVecchio, J. on April 6, 1999 and May 11, 1999, Big Bear is not entitled to advance the claims represented by the heads of damage specified in the draft Statement of Claim other than as set out in its Notice of Claim.

Analysis

**77** Big Bear submits that it is clear that, in an appropriate case, a complex liability issue that arises in the context of CCAA proceedings may be determined by a trial, including provision for production and discovery: Algoma Steel Corp. v. Royal Bank of Canada [1992] O.J. No. 889 (Ont. C.A.). Big Bear also submits that the court has the jurisdiction to overlook technical complaints about the contents of a Notice of Claim. The CCAA does not prescribe a claim form, nor set the rules for completion and contexts of a claim form, and it is common ground that in this case, the form used for the "Notice of Claim" was not approved by any order of the court. At any rate, Big Bear submits that it is not seeking to amend its claim to add new claims or to claim additional amounts.

**78** It makes that assertion apparently on the basis that the major parties concerned with CCAA proceedings in the Blue Range matter were aware of the nature of Big Bear's additional claims by reason of the draft Statement of Claim attached to Mr. Tonken's May 5, 1999 affidavit, although that affidavit was filed in support of an application to lift the stay imposed under the CCAA, an application which was dismissed by LoVecchio, J. on May 11, 1999.

**79** Big Bear characterizes the issue as whether it must prove the exact amount claimed in its Notice of Claim or otherwise have its claim barred forever. It submits that the bare contents of the Notice of Claim cannot be construed as a fixed election barring a determination and assessment of an unliquidated claim for tort damages, and that it would be inequitable to deny Big Bear a hearing on the substance of its claim based on a perceived technical deficiency in the contents of the Notice of Claim.

**80** In summary, Big Bear asks that the court direct an expedited trial for the hearing of its claim as outlined in the draft Statement of Claim.

**81** The Applicants submit that, by attempting now to make claims other than the claims set out in the Notice of Claim, Big Bear is attempting to indirectly and collaterally attack the orders of LoVecchio, J. dated April 6, 1999 and May 11, 1999, specifically:

a) by adding claims for alleged heads of damage other than those specified in the Notice of Claim contrary to the claims bar order of April 6, 1999; and

b) by attempting to include portions of the draft Statement of Claim relating to other alleged heads of damage in the Notice of Claim contrary to the May 11, 1999 order dismissing leave to file the draft Statement of Claim.

**82** While it is true that a court has jurisdiction to overlook technical irregularities in a Notice of Claim, the issue is not whether the court should overlook technical non-compliance with, or ambiguity in, a form, but whether it is appropriate to do so in this case where previous orders have been made relating to these issues. Here, Big Bear chose to pursue its claims through two different routes. It filed a Notice of Claim alleging damages for a share exchange loss, transaction costs and the cost of shares purchased before the takeover bid, all damage claims that can reasonably be identified as being related to an action for negligent misrepresentation. At about the same time, it brought an application to lift the stay granted under the CCAA and file a Statement of Claim that alleged other causes of action. That application was dismissed, and the order dismissing it was never appealed. This is not a situation as in Re Cohen (1956) 19 W.W.R. 14 (Alta. C.A.) where a claim made on one basis was later sought to be made on a different basis, nor an issue of Big Bear lacking the necessary information to make its claim, although quantification of damage may have been difficult to determine. Given the previous application by Big Bear, this is a collateral or indirect attack on the effectiveness of LoVecchio, J.'s orders, and should not be allowed: Wilson v. The Queen (1983) 4 D.L.R. (4th) at 599). The effect of the two orders made by LoVecchio, J. is to prevent Big Bear from advancing its claim other than as identified in its Notice of Claim, which cannot reasonably be interpreted to extend beyond the claims for damages for negligent misrepresentation.

**83** It is true that the Notice of Claim form is not designed for unliquidated tort claims. I do not accept, however, that it was not possible for Big Bear to include claims under other heads of damages in the claim process by, for example, attaching the draft Statement of Claim to the Notice of Claim, or by incorporating such claims by way of schedule or appendix, as was done with respect to the claims for damages for negligent misrepresentation.

**84** I note that LoVecchio, J. issued a judgment after this application was heard relating to claims for relief from the impact of the claims procedure established by the court by a number of creditors who filed late or wished to amend their claims after the claims bar date of May 7, 1999 had passed. Although LoVecchio, J. allowed these claims, and found that it was appropriate in the circumstances to grant flexibility with respect to the applications before him, he noted that total amount of the applications made to him would be less than 1.4 million dollars, and the impact of allowing the applications was minimal to the remaining creditors. The applications before him do not appear to involve issues which had been the subject of previous court orders, as in the current situation, nor would they have the same implication to creditors as would Big Bear's claim. The decision of LoVecchio, J. in the circumstances of the applications before him is distinguishable from this issue.

ROMAINE J.

cp/i/qljpn

# Tab 6

*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**

[2006] O.J. No. 276

14 B.L.R. (4th) 260

17 C.B.R. (5th) 78

145 A.C.W.S. (3d) 194

2006 CarswellOnt 406

2006 CanLII 1773

Court File No. 04-CL-5306

Ontario Superior Court of Justice
Commercial List

**J.M. Farley J.**

Heard: January 17-18 and 20, 2006.
Judgment: January 20, 2006.

(41 paras.)

*Creditors and debtors law -- Legislation -- Debtors' relief -- Companies Creditors Arrangement Act -- Motion by equity shareholders to extend the powers of a monitor dismissed -- Proposed plan of arrangement under Companies' Creditors Arrangement Act was approved.*

*Insolvency law -- Receivers, managers and monitors -- Property -- Sale of -- Motion by equity shareholders to extend the powers of a monitor dismissed -- Proposed plan of arrangement under Companies' Creditors Arrangement Act was approved.*

Motion by certain shareholders of a company to extend the powers of a monitor to conduct a sale of the company's business as a going concern -- In the alternative, the shareholders sought suspension of a proposed plan of arrangement under the Companies' Creditors Arrangement Act -- The shareholders also requested that approval of the plan be adjourned for 60 days to have the monitor conduct an independent sale process -- HELD: Motion dismissed -- All statutory requirements and previous court orders had been complied with -- The plan was fair, reasonable and equitable in relation to the affected creditors -- The existing shareholders could not lay claim to there being any existing equity value -- The plan was implementable, therefore it was sanctioned and approved.

**Statutes, Regulations and Rules Cited:**

Canada Business Corporations Act, s. 191

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

**Counsel:**

Michael Barrack, James D. Gage and Geoff R. Hall, for the Applicants

Robert Thornton and Kyla Mahar, for the Monitor

Peter Jervis, George Glezos and Karen Kiang, for the Equity Holders

John Varley, for the Salaried Employees

David Jacobs, for USW Locals 8782 and 5328

Aubrey Kauffman, for Tricap Management Ltd.

Kevin Zych and Rick Orzy, for the 8% and 10.4% Stelco Bondholders

Lawrence Thacker, for the Directors of Stelco

Sharon White, for USW Local 1005

Ken Rosenberg, for USW International

Kevin McElcheran, for GE

Gale Rubenstein and Fred Myers, for the Superintendent of Financial Services

Derrick Tay, for Mittal

David R. Byers and Sean Dunphy, for CIT Business Credit as DIP and ABL Lender

V. Gauthier, for BABC Global Finance

L. Edwards, for EDS Canada Inc.

Peter Jacobsen, for Globe & Mail

Paul Macdonald and Andy Kent, for Sunrise and Appalloosa

Murray Gold and Andrew Hatnay, for the Salaried Retirees

Flaviano Stanc, Self-Represented

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ENDORSEMENT

(Motion by the Applicants for a Sanction Order
and Cross-Motion of Certain Equity Holders)

**1** J.M. FARLEY J. (endorsement):-- The Applicants (collectively "Stelco") moved for:

(a) a declaration that Stelco has complied with the provisions of the Companies' Creditors Arrangement Act ("CCAA") and the orders of this court made in this CCAA proceeding;
(b) a declaration that the Stelco plan of arrangement pursuant to the CCAA and the reorganization of Stelco Inc. ("S") under the Canada Business Corporations Act ("CBCA") (collectively the "Plan") as voted on by the affected creditors of Stelco is fair and reasonable;
(c) an order sanctioning and approving the Plan; and
(d) an order extending the Stay Period and Stay Date in the Initial Order until March 31, 2006.

**2** This relief was unopposed by any of the stakeholders except for various existing shareholders of S (who may also be employees or retirees of Stelco). In particular there was organized objection to the Plan, especially as in essence the Plan would eliminate the existing shareholders, by a group of shareholders (AGF Management Ltd., Stephen Stow, Pollitt & Co., Levi Giesbrecht, Joe Falco and Phil Dawson) who have styled themselves as "The Equity Holders" ("EH"). On December 23, 2005 the EH brought in essence a cross motion seeking the following relief:

(a) An order extending the powers of the Monitor, Ernst & Young, in order to conduct a sale of the entire Stelco enterprise as a going concern through a sale of the common shares or assets of Stelco on such terms and conditions as are considered fair;
(b) An order authorizing and directing the Monitor to implement and to take all steps necessary to complete and fulfil all requirements, terms, conditions and steps of such a sale;
(c) An order authorizing and directing the Monitor to conduct the sale process in accordance with a plan for the sale process approved by the court;
(d) An order directing the Monitor to retain such fully independent financial advisors and other advisors as necessary to conduct this sale process;
(e) An order confirming that the powers granted herein to the Monitor supersede any provision of any prior Order of this Court made in the within proceedings to the extent that such provision of any prior order is inconsistent with or contradictory to this order, or would otherwise limit or hinder the power and authority granted to the Monitor;

(f) An order directing Stelco and its directors, officers, counsel, agents, professional advisors and employees, and its Chief Restructuring Officer, to cooperate fully with the Monitor with regard to this sale process, and to provide the Monitor with such assistance as may be requested by the Monitor or its independent advisors;

(g) In the alternative, an order suspending the sanctioning of the Proposed Plan of Arrangement, approved by the creditors on December 9, 2005, for a period of two months from the date of such order, so that the Monitor may conduct the independent sale process that may result in a more profitable outcome for all stakeholders, including the Equity Holders;

(h) In the further alternative, an order lifting the Companies' Creditors Arrangement Act stay of proceedings in respect of Stelco without approving the Plan of Arrangement, as approved by the creditors on December 9, 2005, pursuant to such terms as are just and are directed by court; and

(i) Such further and other relief as counsel may advise and this Honourable Court may permit.

**3** In its factum, the EH requested that the court adjourn approval of the Plan for 60 days and direct the Monitor to conduct an independent sale process for the shares of S. In the attendances on January 17 and 18, 2006, the EH then asked that approval of the Plan be adjourned for 30 days in order to see if there were expressions of interest for the shares of S forthcoming in the interim.

**4** I indicated that I would defer my consideration of the adjournment request until after I had had submissions on the motions before me as set out above. I also indicated that while there did not appear to be any concern by anyone including the EH as to the first two elements concerning CCAA plan sanctioning as discussed in Re Algoma Steel Inc. (2001), 30 C.B.R. (4th) 1 (Ont. S.C.J.) at p. 3:

> In a sanction hearing under the Companies' Creditors Arrangement Act ("CCAA") the general principles to be applied in the exercise of the court's discretion are:
>
> (a) There must be strict compliance with all statutory requirements and adherence to the previous orders of the court;
> (b) All materials filed and procedures carried out must be examined to determine if anything has been done or purported to be done which is not authorized by the CCAA; and
> (c) The Plan must be fair and reasonable.
>
> See Northland Properties Ltd., Re (1988), 73 C.B.R. (N.S.) 175 (B.C. S.C.), affirmed Northland Properties Ltd. v. Excelsior Life Insurance Co. of Canada (1989), 73 C.B.R. (N.S.) 195 (B.C. C.A.) at p. 201; Campeau Corp., Re (1992), 10 C.B.R. (3d) 104 (Ont. Gen. Div.) at p. 109; Olympia & York Developments Ltd. v. Royal Trust Co. (1993), 12 O.R. (3d) 500 (Ont. Gen. Div.) at p. 506; Sammi Atlas Inc., Re (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List]), at pp. 172-3; Canadian Airlines Corp., Re, [2000] 10 W.W.R. 269 (Alta.

Q.B.), leave to appeal dismissed, [2000] 10 W.W.R. 314 (Alta. C.A. [In Chambers]).

it would not be sufficient to only deal in this hearing with the third test of whether the Plan was fair and reasonable (including the aspect of "fair, reasonable and equitable" as discussed in Sammi). Rather the court also had to be concerned as to whether the Plan was implementable. In other words, it would be futile and useless for the court to approve a plan which stood no reasonable prospect of being implemented. That concern of the court had been raised by my having been alerted by the Monitor in its 46th Report at paragraphs 8-9:

> 8. The Monitor has had discussions with the proposed ABL lenders, Tricap, the Province and Stelco regarding the status of the ABL Loan and the Bridge Loan. The Monitor has been advised that the parties are continuing to work at resolving issues that are outstanding as at the date of this Forty-Sixth Report. However, all of the parties remain optimistic that acceptable solutions to the outstanding issues will be found and implemented.
> 9. In the Monitor's view, the principal issues to be resolved include:
>
> (a) the corporate structure of Stelco, which could involve the transfer of assets of some of the operations or divisions of the Applicants to new affiliates; and
> (b) satisfying the ABL lenders and Tricap as to the priority of the new financing.
>
> These issues need to be resolved primarily among the proposed ABL lenders, Tricap and Stelco and will also involve the Province insofar as they affect pension and related liabilities.

**5** I was particularly disquieted by the lack of progress in dealing with these outstanding matters despite the passage of 39 days since the Plan was positively voted on December 9, 2005. I do appreciate that Christmas, Hanukkah and New Year's were celebrated in this interval and that there had been a certain "negotiation fatigue" leading up to the December 9th revisions to the Plan and that I have advocated that counsel, other professionals and litigation participants balance their lives and pay particular attention to family and health. However I find it unfortunate that there would appear to have been such a lengthy hiatus, especially when the workers at Stelco continued (as they have for the past two years while Stelco has been under CCAA protection) to produce steel in record amounts. I therefore demanded that evidence be produced forthwith to demonstrate to my satisfaction that progress was real and substantial so that I could be satisfied about implementability. As a side note I would observe that in the "normal" case, sanction orders are typically sought within two or three days of a positive creditor vote so that it is not unusual for documentation to be sorted out for a month before a plan is implemented with a closing.

**6** The EH filed material to support its submission that the Plan is not fair, reasonable and equitable because it is alleged that there is currently sufficient value in Stelco to fully satisfy the claims of affected and unaffected creditors and to provide at least some value to current shareholders. The EH prefers to have a search for some entity to take out the current shareholders for "value". Fabrice Taylor, a chartered financial analyst with Pollit & Co. swore an affidavit on the eve of this hearing

which was sent electronically to the service list on January 16, 2006 at approximately 7:30 p.m. In that affidavit, he states:

> 2. The Dofasco bidding war has highlighted a crucial fact about steel asset valuations, notably that strategic buyers place a much higher value on them than public market investors. Attached as Exhibit "1" is an article entitled "Restructuring of steel industry revives investors' interest", published in the Financial Times on December 14, 2005.
> 3. I, along with Murray Pollitt and a number of Stelco shareholders, have spent the past three months attempting to attract strategic buyers and/or equity investors in Stelco. These strategic buyers and equity investors are mostly international. Some had already considered buying Stelco or had made bids for the company but had stopped following the story some months ago. Others were not very familiar with Stelco.
> 4. Three factors hindered our efforts. First, Stelco is under CCAA protection, a complicated situation involving multiple players and interests (unions, politics, pensions) that is difficult to understand, particularly for foreigners. Second, there has not been enough time for these strategic buyers or equity investors to deepen their understanding or to perform due diligence. Finally, the Dofasco bid process, while providing emphatic evidence that steel assets are increasingly valuable, hinders certain strategic buyers and financial institutions interested in participating in Stelco because they are distracted and/or conflicted by the Dofasco sale. I have been advised by some of the participants in the Dofasco negotiations that they would be willing to carefully consider a Stelco transaction once the Dofasco sale has been resolved.
> 5. The Forty Fifth Report of the Monitor confirmed that Stelco had not received any offers in the last several months. The report does not answer the question of whether the company or its financial advisors have in fact attempted to attract any offers. I believe that Stelco would have received expressions of interest had the company made efforts to attract offers, or had the Dofasco sale been resolved earlier. I believe that the Monitor should be authorized, for a period of at least 60 days, to canvas interest in a sale of Stelco before the approval of the proposed plan of restructuring.

**7** No satisfactory explanation was forthcoming as to why this affidavit, if it needed to be filed at all, was not served and filed by December 23, 2005, in accordance with the timetable which the EH and the other stakeholders agreed to. Certainly there is nothing in the affidavit which is such late breaking news that this deadline could not have been met, let alone that it was served mere hours before the hearing commenced on January 17, 2006. Aside from the fact that the financing arrangements forming the basis of the Plan contained "no shop" covenants which would make it inappropriate and a breach to try to attract other offers, the foregoing excerpts from the Taylor affidavit clearly illustrate that despite apparently diligent efforts by the EH, no one has shown any real or realistic interest in Stelco. Reading between the lines and without undue speculation, it would appear that the efforts of the EH were merely politely rebuffed.

**8** Certainly Stelco is not Dofasco, nor is it truly a comparable (as opposed to a contrastor). Stelco has been a wobbly company for a long time. Further as I indicated in my October 3, 2005 endorsement, in the preceding 20 months under the CCAA protection, Stelco has become "shopped worn". The unusual elevation of steel prices in the past two years has helped Stelco avoid the looming liquidity crisis which it anticipated in its CCAA filing on January 29, 2004. However even this financial transfusion has not allowed it to become a healthy company or truly given it a burgeoning war chest to weather bad times the way that other steel companies (including some in Canada) have so benefited. The redness of the visage of Stelco is not a true indication of health and well being; rather it seems that it is rouge to mask a deep pallor.

**9** I am satisfied on the evidence of Hap Stephen, the Chief Restructuring Officer of Stelco and of the Monitor that there has been compliance with all statutory requirements and adherence to previous orders of the court and further that nothing has been done or purported to be done that is not authorized by the CCAA.

**10** The next question to be dealt with is whether the Plan is fair, reasonable and equitable. I was advised that creditors of the affected creditor classes representing approximately 90% in value of each class voted on the Plan. The Monitor reported at para. 19 of its 44th Report as to the results of the vote held December 9th as follows:

| Class of Affected Creditors | Percentage in favour by Number | Percentage in favour by Dollar Value |
|---|---|---|
| Stelco | 78.4% | 87.7% |
| Stelwire | 89.01% | 83.47% |
| Stelpipe | 94.38% | 86.71% |
| CHT Steel | 100% | 100% |
| Welland Pipe | 100% | 100% |

**11** This favourable vote by the affected creditors is substantially in excess of the statutory two-thirds requirement. By itself that type of vote, particularly with such a large quorum present, would ordinarily be very convincing for a court not interfering with the informed decisions of busi-

ness people. With that guideline, plus the aspect that a plan need not be perfect, together with the lack of any affected creditor opposition to the Plan being sanctioned and the fact that the Plan including its ingredients and nature and amount of compromise compensation to be given to affected creditors having been exhaustively negotiated in hard bargaining by the larger creditor groups who are recognized as generally being sophisticated and experienced in this area, and the consideration of the elements in the next paragraph, it would seem to me that the Plan is fair, reasonable and equitable vis-à-vis the affected creditors and I so find. See Sammi, at p. 173; Re T. Eaton Co. (1999), 15 C.B.R. (4th) 311 (Ont. S.C.J.) at p. 313; Re Olympia & York Developments Ltd. (1993), 12 O.R. (3d) 500 (Gen. Div) at p. 510.

**12** I also think it helpful to examine the situation pursuant to the analysis which Paperny J. did in Re Canadian Airlines Corp. (2000), 20 C.B.R. (4th) 1 (Alta. Q.B.), leave to appeal refused (2000), 20 C.B.R. (4th) 46 (Alta C.A. [In Chambers]). That proceeding also involved an application pursuant to the corporate legislation, the Business Corporations Act (Alberta), concerning the shares and shareholders of Canadian Airlines. In that case, Paperny J. found the following factors to be relevant:

(a) the composition of the vote: claims must have been properly classified, with no secret arrangements to give an advantage to a creditor or creditors; approval of the plan by the requisite majority of creditors is most important (in the case before me of Stelco: the challenge to classification was dismissed; there was no suggestion of secret arrangements; and, as discussed above, the quorum and size of the positive vote were very high);

(b) anticipated receipts in liquidation or bankruptcy: it is helpful if the Monitor or other disinterested person has prepared a liquidation analysis (in Stelco, the Monitor determined that on liquidation, affected creditor recovery would likely range from 13 to 28 cents on the dollar; it should also be observed that Stelco has engaged in extensive testing of the market as to possible capital raising or sale with the aid of established firms and professionals of great experience and had come up dry.);

(c) alternatives to the proposed plan: it is significant if other options have been explored and rejected as unworkable (in Stelco; see comment in (b));

(d) oppression of the rights of certain creditors (in Stelco, this was not a live issue as nothing of this sort was alleged);

(e) unfairness to shareholders (in Stelco, this will be dealt with later in my reasons; however allow me to observe that the interests of shareholders becomes engaged if they are not so far underwater that there is a reasonable prospect in the foreseeable future that the fortunes of a company would otherwise likely be turned around so that they would not continue to be submerged); and

(f) the public interest: the retention of jobs for employees and the support of the plan by the company's unions is important (in Stelco, the Plan does not call for reductions in employment; there is provision for continuation of the capital expenditure program and its funding; an important enterprise for the municipal and provincial levels of government would be preserved with continuing benefits for those communities; an important customer and supplier would continue in the industry and maintain competition; the

> USW International Union and its locals (except for local 1005) supported the Plan and indeed were instrumental in bringing Tricap Management Limited to the table (local 1005's position was that it did not wish to engage in the CCAA process in any meaningful way as it was content to rely upon its existing collective agreement which now still has several months to go before expiring).

However that is not the end of that issue: what of the shareholders?

**13** Is the Plan fair, reasonable and equitable for the existing shareholders of S? They will be wiped out under the Plan and their shares eliminated. New equity will be created in which the existing shareholders will not participate. They have not been allowed to vote on the Plan.

**14** It is well established that a reorganization pursuant to s. 191 of the CBCA may be made in conjunction with a sanction order under the CCAA and that such a reorganization may result in the cancellation of existing shares of the reorganized corporation based on those shares/equity having no present value (in the sense of both value "now" and the likelihood of same having value in the reasonably foreseeable future, absent the reorganization including new debt and equity injections and permitted indulgences or other considerations and adjustments). See Re Beatrice Foods Inc. (1996), 43 C.B.R. (4th) 10 (Ont. Gen. Div.) at para. 10-15; Re Laidlaw Inc. (2003), 39 C.B.R. (4th) 239 (Ont. S.J.C.); Algoma at para. 7; Cable Satisfaction International Inc. v. Richter & Associés Inc. (2004), 48 C.B.R. (4th) 205 (Que. S.C.) at p. 217. The Dickenson Report, which articulated the basis for the reform of corporate law that resulted in the enactment of the CBCA, described the object of s. 191 as being:

> to enable the court to effect any necessary amendment to the articles of the corporation in order to achieve the objective of the reorganization without having to comply with all the formalities of the Draft Act, particularly shareholder approval of the proposed amendment (emphasis added): R.W.V. Dickenson, J.L. Howard, L. Getz, Proposals for a New Business Corporations Law for Canada, vol. 1 (Ottawa: Information Canada. 1971) at p. 124.

**15** The fairness, reasonableness and equitable aspects of a plan must be assessed in the context of the hierarchy of interests recognized by insolvency legislation and jurisprudence. See Canadian Airlines at pp. 36-7 where Paperny J. stated:

> Where a company is insolvent, only the creditors maintain a meaningful stake in its assets. Through the mechanism of liquidation or insolvency legislation, the interests of shareholders are pushed to the bottom rung of the priority ladder. The expectations of creditors and shareholders must be viewed and measured against an altered financial and legal landscape. Shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditors' claims are not being paid in full. It is through the lens of insolvency that the court must consider whether the acts of the company are in fact oppressive, unfairly prejudicial or unfairly disregarded. CCAA proceedings have recognized that shareholders may not have "a true interest to be protected" because there is no reasonable prospect of economic value to be realized by the shareholders given the existing financial misfortunes of the company: Royal Oak Mines Ltd., supra, para. 4., Re

> Cadillac Fairview Inc., [1995] O.J. No. 707, (March 7, 1995), Doc. B28/95 (Ont. Gen. Div. [Commercial List]), and T. Eaton Company, supra. To avail itself of the protection of the CCAA, a company must be insolvent. The CCAA considers the hierarchy of interests and assesses fairness and reasonableness in that context. The court's mandate not to sanction a plan in the absence of fairness necessitates the determination as to whether the complaints of dissenting creditors and shareholders are legitimate, bearing in mind the company's financial state. The articulated purpose of the Act and the jurisprudence interpreting it, "widens the lens" to balance a broader range of interests that includes creditors and shareholders and beyond to the company, the employees and the public, and tests the fairness of the plan with reference to its impact on all of the constituents.
>
> It is through the lens of insolvency legislation that the rights and interests of both shareholders and creditors must be considered. The reduction or elimination of rights of both groups is a function of the insolvency and not of oppressive conduct in the operation of the CCAA. The antithesis of oppression is fairness, the guiding test for judicial sanction. If a plan unfairly disregards or is unfairly prejudicial it will not be approved. However, the court retains the power to compromise or prejudice rights to effect a broader purpose, the restructuring of an insolvent company, provided that the plan does so in a fair manner."

**16** The question then is does the equity presently existing in S have true value at the present time independent of the Plan and what the Plan brings to the table? If it does then the interests of the EH and the other existing shareholders must be considered appropriately in the Plan. This is fairly put in K.P. McElcheran, Commercial Insolvency in Canada (Toronto, Lexis Nexis Canada Inc.: 2005) at p. 290 as:

> If, at the time of the sanction hearing, the business and assets of the debtor have a value greater than the claims of the creditors, a plan of arrangement would not be fair and reasonable if it did not offer fair consideration to the shareholders.

**17** However if the shareholders truly have no economic interest to protect (keeping in mind that insolvency and the depth of that insolvency may vary according to which particular test of insolvency is applied in respect of a CCAA proceeding: as to which, see Re Stelco Inc., [2004] O.J. No. 1257 (S.C.J. [Commercial List]), leave to appeal dismissed [2004] O.J. No. 1903 (C.A.), leave to appeal dismissed, 336, [2004] S.C.C.A. No. 336 (S.C.C.) No. 30447). In Cable Satisfaction, Chaput J. at p. 218 observed that when shareholders have no economic interest to protect, then they have no claim to a right under the proposed arrangement and the "[m]ore so when, as in the present case, the shareholders are not contributing to any of the funding required by the Plan." I do note in the case of the Stelco Plan and the events leading up to it, including the capital raising and sale processes, that despite talk of an equity financing by certain shareholders, including the EH, no concrete offer ever surfaced.

**18** If the existing equity has no true value at present, then what is to be gained by putting off to tomorrow (the ever present and continuous problem in these proceedings of manana - which never comes) what should be done today. The EH speculate, with no concrete basis for foundation as demonstrably illustrated by the eve of hearing Taylor affidavit discussed above, that something good may happen. I am of the view that that approach was accurately described in court by one counsel

as a desperation Hail Mary pass and the willingness of someone, without any of his own chips, in the poker game willing to bet the farm of someone else who does have an economic interest in Stelco.

**19** I also think it fair to observe that in the determination of whether someone has an economic value, that analysis should be conducted on a reasonable and probable basis. In a somewhat different but applicable context, I observed in New Quebec Raglan Mines Ltd. v. Blok-Andersen, [1993] O.J. No. 727 at p. 3:

> The "highest price" is not the price which could be derived on the basis of the most optimistic and risky assumptions without any regard as to their likelihood of being realized. It also seems to me that prudence would involve a consideration that there be certain fall back positions. Even in betting on horses, the most savvy and luckiest punter will not continue to stake all his winnings of the previous race on the next (and so on). If he does, he will go home wearing the barrel before the last race is run.

Alternatively there is a saying: "If wishes were horses, then beggars would ride."

**20** Unless I were to now dismiss the motion for sanctioning and approving the Plan because I found that it was not implementable and/or that it was not fair, reasonable and equitable to the existing shareholders (based upon the proviso that I did determine that the existing shareholders did have a valid present material equity of value), then I see no reason not to dismiss the motion of the EH concerning its request for an adjournment and its request for a further sale (or other related disposition) process. Allow me to observe that no matter how well intentioned the motion of the EH in that regard, I find that that request to be lacking in any valid substance. Rather, the evidence presented was in essence a chimera. I think it fair to observe that, with all the capital raising and sales processes to date which Stelco has undertaken in conjunction with its experienced and well placed professional advisers together with its Chief Restructuring Officer and the Monitor, the bushes have been exhaustively and well beaten as to any real possible interest. Despite three months of what one must presume to be diligent efforts, the EH have come up with nothing concrete. I do not find that the three factors mentioned by Taylor in his late-blooming affidavit of January 16th to be remotely close to convincing. The first two, if taken at face value, would lead one to the conclusion that no one has the time, interest or ability to take an interest in Stelco in any meaningful timeframe. The third presumes that the losing bidder for Dofasco, be it Arcelor or ThyssenKrupp, will almost automatically want Stelco - and at a price and upon terms which would result in present equity being attributed value. I must say in fairness that this is wishful thinking as neither of these warring bidders pursued any interest in Stelco during the previous processes. It is neither clear nor obvious why mere municipal proximity of Dofasco to Stelco's Hilton Works in Hamilton would now ignite any interest in Stelco.

**21** I also think it fair to observe that not proceeding with the sanction hearing now and indeed starting a brand new search for someone who will think Stelco so worthwhile that it will offer such a large amount (with or without onerous conditions) is akin to someone coming into court when a receiver is seeking court approval on a sale - and that someone being allowed to know the price and conditions - and then being able to make an offer for a price somewhat higher. (I reiterate that here we do not even have an offer or a price.) I do not see that such a procedure would be consistent with the principles laid out in Royal Bank v. Soundair Corp. (1991), 7 C.B.R. (3d) 1 (Ont. C.A.). Given

that the affected creditors have rather resoundingly voted in favour of the Plan, all in accordance with the provisions of the CCAA and the Court orders affecting the sanction, I would be of the view that if the existing equity has no value, then the EH's request in this respect would, if granted, be of significant detriment to the integrity of the insolvency system and regime. I would find that inappropriate to attempt to justify proceeding along that line.

**22** Allow me to return to the pivotal point concerning the question of whether the Plan is fair, reasonable and equitable, vis-à-vis the existing equity. The EH retained Navigant Consulting which relied upon the views of Metal Bulletin Research ("MBR") which, inter alia, predicted a selling spot price of hot roll steel at $525 U.S. per ton. Navigant's conclusion in its December 8, 2005 report was that the value of residual shareholder equity was between $1.1 to $1.3 billion or a per share value of between $10.76 and $12.71. However, when Stelco pointed out certain deficiencies in this analysis, Navigant took some of these into account and reduced its assessment of value to between $745 million to $945 million for residual shareholder value on per share value of $7.29 to $9.24, using a discounted cash flow ("DCF") approach. Navigant tested the DCF approach against the EBITDA approach. It is interesting to note that on the EBITDA analysis approach Navigant only comes up to a conclusion that the equity is valued at $8 million to $83 million or $0.09 to $0.81 per share. If the Court were to accept that as an accurate valuation, or something at least of positive value even if not in that neighbourhood, then I would have to take into account existing shareholder interests in determining whether the Plan was fair, reasonable and equitable - and not only vis-à-vis the affected creditors but also vis-à-vis the interests of the existing shareholders given that at least some of their equity would be above water. I understand the pain and disappointment of the existing shareholders, particularly those who have worked hard and long with perhaps their life savings tied up in S shares, but regretfully for them I am not able to come to a conclusion that the existing equity has a true positive value.

**23** The fight in the Stelco CCAA proceedings has been long and hard. No holds have been barred as major affected creditors have scrapped to maximize their recovery. There were direct protracted negotiations between a number of major affected creditors and the new equity sponsors under the Plan, all of whom had access to the confidential information of Stelco pursuant to Non Disclosure Agreements. These negotiations established a value of $5.50 per share for the new common shares of a restructured Stelco. That translates into an enterprise value (not an equity value since debt/liabilities must be taken into consideration) of $816.6 million for Stelco, or a recovery of approximately 65% for affected creditors. The parties engaged in these negotiations are sophisticated experienced enterprises. There would be no particular reason to believe that in the competition involved here that realistic values were ignored. Further, the affected creditors generally were rather resoundingly of the view by their vote that an anticipated 65% recovery was as good as they could reasonably expect.

**24** The 45th Report of the Monitor had a chart of calculations to determine the level of recovery of affected creditors at various assumed enterprise values up to and including the top end of Navigant's range of enterprise value (as contrasted with residual equity value). At the high end of Navigant's range of revised enterprise value, $1.6 billion, the Monitor calculated that affected creditors would still not receive full recovery of their claims.

**25** The EH cited the sale of the EDS Canada claim to Tricap as being at a premium as evidence in support of Navigant's conclusion. However, the fact was that this claim was purchased not at a

premium, but rather at a discount. That would be confirmation of the opposite of which the EH has been contending.

**26** Despite a very comprehensive capital raising and asset sale process, with the market alerted and well canvassed, and with the ability to conduct due diligence, no interested party came forwarded to conclude a deal. Even since the December 9, 2005 vote when the terms of the Plan were available, no interested party has come forward with any expression of interest which would attribute value to the existing shareholders.

**27** Stelco's experts, UBS and BMO Nesbitt Burns, both have given opinions that there is no value to the existing equity. Their expert opinions were not challenged by cross-examination. Both these advisors are large sophisticated institutions; both have extensive experience in the steel industry.

**28** UBS calculated the enterprise value of Stelco as being in the range of $550 million to $750 million; BMO Nesbitt Burns at $650 million to $850 million. On that basis the unsecured creditors would receive less than full recovery of their claims, which would lead to the conclusion that there is no value for the existing shareholders. The Monitor commissioned an independent estimate of the enterprise value from its affiliate, Ernst & Young Orenda Corporate Finance Inc.'s Valuation Group. That opinion came in at $635 million to $785 million.

**29** I would note that Farley Cohen, the principal author of the Navigant report, does not have experience in dealing with integrated steel companies. I find it unusual that he would have customized his approach in calculating equity value by not deducting the Asset Based Lenders loan. Brad Fraser of BMO Nesbitt Burns stated that such customization was contrary to the practice at his firms both present and past and that the Navigant's approach was internally inconsistent with respect thereto as to 2005 to 2009 cash flows as contrasted with terminal value. The Navigant report appears to have forecasted a high selling price for steel combined with low costs for imports such as coal and scrap, which would be contrary to historical complementary movements between steel prices and these inputs.

**30** Navigant relies on an average price of $525 US per ton as provided by MBR. This is a single source as to this forecast. While a single analyst may come up with a forecast which is shown by the passage of time to be dead on accurate, it would seem to me to be more realistic and prudent to rely on the consensus approach of considering the views of a greater number of "representative" analysts, especially when prices appear volatile for the foreseeable future. That consensus approach allows for consideration of the way that each analyst looks at the market and the factors and weights to be given. The UBS opinion reviewed the pricing forecast of eight analysts and BMO Nesbitt Burns' ten analysts. Interestingly, MBR's choice of a price at the top of the band would seem at odds as the statements on the MBR website foreseeing downward pressure on steel prices in 2006 because of falling prices in China; although this inconsistency was pointed out, there was no response forthcoming.

**31** Navigant estimated Stelco's financial performance for the last quarter of 2005 and made a significant upward adjustment. However, the actual experience would appear to indicate that such an adjustment would overstate Stelco's results by $124 million.

**32** Navigant's DCF approach involved a calculation of Stelco's enterprise value by adding the present value of a stream of cash flow from the present to 2009 and the present value of the terminal value determined as at 2009 so that the terminal value represents the majority (60% approximately)

of enterprise value as calculated by Navigant. MBR chose a 53-year average steel price despite significant changes over that time in the industry. However, coal and scrap costs were determined as at 2009. This produced the anomalous result that steel prices are rising while costs are falling. This would imply great structural difficulties (economically and functionally) in the steel industry generally and a lack of competition. A terminal value EBITDA margin for Stelco would then be implied at approximately 26% or some 11% higher than the EBITDA margin actually achieved by Stelco in the first quarter of 2005, the most profitable quarter in the history of Stelco.

**33** Interestingly, since Navigant's approach in fact would decrease calculated value, UBS and BMO Nesbitt Burns used a weighted average cost of capital ("WACC") for Stelco in the range of 10% to 14%; Navigant used 24%. A higher WACC will result, all other things being equal, in a lower enterprise value. Navigant considered that there should be a 10% to 15% company-specific premium because of the risks associated with Stelco vis-à-vis the higher steel prices forecast by MBR. This would appear to imply that there was recognition that either MBR was aggressive in its forecasting or that price volatility would caution one to use consensus forecasting. Colin Osborne, a senior executive of Stelco, with considerable experience in the steel industry provided direct evidence on the substantial differences between each of Stelco, AK Steel, U.S. Steel and Algoma. Mr. Cohen acknowledged in cross-examination that these differences made Dofasco a more valuable company than Stelco. As set out at para. 74 of the Stelco Factum:

> 74. The specific difference identified by Mr. Osborne which made Dofasco unique include but are not limited to:
>
> (a) non-union, flexible work environment (vs. Stelco, Algoma, AK Steel and U.S. Steel);
> (b) legacy costs which are very low due to non-conventional profit sharing, which limits liability (vs. Stelco, AK Steel, Algoma and U.S. Steel);
> (c) high historical cap-ex spend per ton (vs. Stelco, Algoma and U.S. Steel);
> (d) a flexible steelmaking stream in terms of a hybrid EAF and blast furnace BOF stream in Hamilton and a mini-mill operation in the U.S. (vs. Stelco, Algoma, U.S. Steel and AK Steel which are all blast furnace based steel makers);
> (e) a value added product mix focused on coated products and tubing (vs. Stelco and Algoma which focus on hot roll); and
> (f) a strong raw material position with excess iron ore and self-sufficiency in coke (Algoma, Stelco and AK Steel all have dependence to various degrees on either iron ore or coke or both).

Dofasco and Stelco are not in my view fungible. There are incredible differences between these two enterprises, to the disadvantage of Stelco.

**34** The reply affidavit of Mr. Fraser of BMO Nesbitt Burns calculated the effect of all of the acknowledged corrections to the initial Navigant report and other adjustments. The result of this exercise was a conclusion by him that there was no value available for existing shareholders. This, along with all the other affidavits provided on the Stelco side, was not cross-examined on.

**35** While not referred to in the Factum of EH, there were a number of quite serious allegations raised in material filed by the EH against management of Stelco concerning bias and manipulation. Mr. Osborne responded to each of these allegations; he was not cross-examined. I find it unfortunate that such allegations appear to have been made on an unsubstantiated shotgun approach.

**36** The position of the EH is that certain of the features of the Plan should be assumed as transportable directly and without change into a scenario where some insolvency rescuer emerges on the scene as the equivalent of a White Knight, one it would seem which has been awakened from slumber. I am of the view that presumes too much. For example, I take it that the Province would not automatically accept this potential newcomer without question; nor would it likely relish the resumption of weeks of hard bargaining. I would think it unwise, impudent and high stakes poker (with other peoples' money) to speculate as did Taylor in para. 41 of his December 23, 2005 affidavit:

> 41. Were Stelco to emerge from CCAA protection and were the province to carry out its threat to revoke Stelco's entitlement to the benefit of section 5.1 the end result would likely be a liquidation of the company. The Province would be responsible for a substantial portion of Stelco's pension promise. It would clearly not be in the Province's self-interest to force Stelco into liquidation. It was, in other words, an obvious bluff. Yet the notion of calling this bluff does not appear to have crossed management's mind.

This should be contrasted with the views of the Monitor in its 44th Report at para. 61:

> 61. It should also be noted that the Pension Plan Funding Arrangements and the $150 million New Province Note embodied in the Approved Plan were agreed to by the Province only in the context of the terms of the Approved Plan and, in particular, the capital structure, liquidity and other elements contemplated therein. The Province has advised that its proposed financing and the Pension Plan Funding Arrangements should not be assumed to be available if any of the elements of the Approved Plan are changed.

**37** The end result is that given the above analysis, I have no hesitation in concluding that it would be preferable to rely upon the analysis of UBS, BMO Nesbitt Burns and Ernst & Young Orenda, both as to their direct views as to the enterprise value of existing Stelco and as to their criticism of the Navigant and MBR reports concerning Stelco. Therefore, I conclude that the existing shareholders cannot lay claim to there being any existing equity value. Given that conclusion, it would be inappropriate to justify cutting in these existing shareholders for any piece of the emergent restructured Stelco. If that were to happen, especially given the relative values and the depth of submersion of existing equity, then it would be unfair, unreasonable and inequitable for the affected creditors.

**38** That then leaves the remaining question: Does it appear likely that the Plan will be implementable? I have been advised on Wednesday, January 18th that I would receive executed term sheets (which would address the issues raised by the Monitor discussed above) by 5 p.m., Friday, January 20th.

**39** The motion and adjournment request of the EH is dismissed.

**40** There was a request to extend the stay to March 31, 2006. I am of the view that it would be sufficient and desirable to extend the stay (subject, of course, to further extension) to March 3, 2006.

**41** I have received the term sheets together with the Monitor's 48th Report by the 5 p.m. January 20th deadline and find them satisfactory as demonstrating to my analysis and satisfaction that the Plan is implementable as discussed above, subject to a comeback provision if anyone wishes to dispute the implementability issue (the onus remaining on Stelco). My decision today re: implementability should in no way be taken as deciding any corporate reorganization issue or anything of that or related nature. I therefore sanction and approve the Plan.

J.M. FARLEY J.

cp/e/qw/qlmpp/qlhcs/qlmll/qlana

# Tab 7

*Case Name:*

# Royal Bank of Canada v. Central Capital Corp.

**RE: Royal Bank of Canada et al., and Central Capital Corporation**

[1996] O.J. No. 359

27 O.R. (3d) 494

132 D.L.R. (4th) 223

88 O.A.C. 161

26 B.L.R. (2d) 88

38 C.B.R. (3d) 1

61 A.C.W.S. (3d) 18

Nos. C21479 and C21477

Ontario Court of Appeal
Toronto, Ontario

**Finlayson, Weiler and Laskin JJ.A.**

February 7, 1996.

(154 paras.)

**Counsel:**

Bryan Finlay, Q.C., and John M. Buhlman, for appellants, James W. McCutcheon and Central Guaranty Trust.

James H. Grout and Anne Sonnen, for appellant, Consolidated S.Y.H. Corp.

Terrence J. O'Sullivan and Paul G. Macdonald, for the unsecured creditors of Central Capital Corp.

Neil C. Saxe, for Peat Marwick Thorne Inc.

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Raesons for judgment were delivered by Finlayson J.A., concurred in by Weiler J.A. Separate reasons were delivered by Laskin JJ.A.

1 **FINLAYSON J.A.** (dissenting): -- The appellant James W. McCutcheon and Central Guarantee Trust Company as Trustee for the Registered Retirement Savings Plan of James W. McCutcheon (hereinafter sometimes referred to collectively as "McCutcheon") and the appellant Consolidated S.Y.H. Corporation ("SYH") appeal from the order of the Honourable Madam Justice Feldman of the Ontario Court (General Division) dated January 9, 1995 (reported as Re Central Capital Corp. (1995), 29 C.B.R. (3d) 33, 22 B.L.R. (2d) 210). Feldman J. dismissed appeals from decisions dated January 20, 1993 and February 16, 1993 of the respondent Peat Marwick Thorne Inc., in its capacity as Interim Receiver, Manager and Administrator ("Administrator") of certain assets of Central Capital Corporation ("Central Capital"). The Administrator disallowed proofs of claim submitted by the appellants with respect to a plan of arrangement under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 ("CCAA"). Leave to appeal the order of Feldman J. was granted on March 17, 1995 by the Honourable Mr. Justice Houlden.

Overview of the Proceedings

2 These appeals arise out of the insolvency of Central Capital which in and prior to December 1991 defaulted under its obligations to various unsecured lenders, note holders and subordinated debt holders. In early December of 1991, Central Capital advised its creditors that, pending implementation of new financial arrangements, it had decided to discontinue payment of all interest and principal due under outstanding loans, with the exception of indebtedness due under secured notes issued to the Royal Trust Company. In an agreed statement of facts, which was prepared by the parties for the purposes of appeals from the disallowances of the Administrator, it was agreed that at all material times since in or prior to December 1991, Central Capital was insolvent. It had a total unsecured debt of $1,577,359,000 and, among other things:

(a) it was unable to pay its liabilities as they became due; and
(b) the realizable value of its assets was less than the aggregate of its liabilities.

3 By notice of application issued June 12, 1992, 39 of the creditors commenced an application pursuant to the CCAA for an order declaring the following: that Central Capital was a debtor company to which the CCAA applied; that Peat Marwick Thorne Inc. be appointed Administrator of the property, assets and undertaking of Central Capital; that a stay of proceedings against Central Capital, except with leave of the court, be granted; and that the applicants be authorized and permitted to file a plan of compromise or arrangement under the CCAA.

4 By order of Houlden J. made June 15, 1992, Central Capital was declared to be a company to which the CCAA applied and all proceedings against Central Capital were stayed. By further order of Houlden J. made July 9, 1992, it was provided, among other things, that:

(a) Peat Marwick Thorne Inc. was appointed Administrator, Interim Receiver and Manager of such of the undertaking, property and assets of Central Capital as necessary for the purpose of effecting the transaction described in the order pursuant to which specified significant assets of Central Capital would be transferred

to a newly incorporated company called Canadian Insurance Group Limited ("CIGL");

(b) the Administrator was authorized to enter into and carry out a subscription and escrow agreement with creditors of Central Capital pursuant to which creditors of Central Capital would be entitled to elect to exchange a portion of the indebtedness owing to them by Central Capital for shares and debentures to be issued by CIGL;

(c) the Administrator was authorized and directed to supervise the calling for claims of creditors of Central Capital who elected to exchange a portion of the indebtedness from Central Capital for shares and debentures to be issued by CIGL as aforesaid; and

(d) Central Capital was authorized and permitted to file with the court a formal plan of compromise or arrangement with Central Capital's secured and unsecured creditors and shareholders in accordance with the CCAA and the Canada Business Corporations Act, R.S.C. 1985, c. C-44 (the "CBCA"), which would provide for the restructuring and reorganization of the debt and equity of Central Capital in the manner set out in the said order.

**5** According to the agreed statement of facts, the order of Houlden J. was made without prejudice to the rights of the appellants to assert claims as creditors in the CIGL transaction. Pursuant to the terms of the July 9, 1992 order, all claims of creditors of Central Capital who wished to participate in CIGL were required to be submitted to the Administrator by September 8, 1992, or such other date fixed by the court. The Administrator received claims from various persons who wished to participate, including the claims submitted by the appellants herein.

**6** The Administrator disallowed the claims of McCutcheon and SYH by notices of disallowance dated January 20, 1993 and February 16, 1993 in which various reasons were cited as to why the appellants did not qualify as creditors. The effect of this disallowance was that McCutcheon and SYH could participate only as shareholders in the plan of compromise and arrangement under the CCAA to be put forward by Central Capital. In dismissing the appeals from this disallowance, Feldman J. found that the appellants were not creditors because they did not have a claim provable under the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 ("Bankruptcy and Insolvency Act").

Issue

**7** The agreed statements of facts sets out the issue in the appeal in the following language:

> Do the appellants, or any of them, have claims provable against CCC [Central Capital] within the meaning of the Bankruptcy Act (Canada), as amended as of the date of the Restated Subscription and Escrow Agreement? If the appellants, or any of them, have provable claims, then the proof of claim of any appellant that has a claim provable is to be allowed as filed and the appeal from the disallowance allowed, and the appellants, or any of them, whose claim is allowed are to participate in the Plan of Arrangement of Central Capital as a senior creditor.

**8** The determination of this issue was deferred by Houlden J.'s order of October 27, 1992. He ordered therein that preferred shareholders who had filed claims against Central Capital as creditors were not permitted to vote at the meeting of creditors called to consider the plan of arrangement

"but such is without prejudice to the rights of those claimants to prosecute their claims as filed". The last paragraph in the order ended:

> For greater certainty, the validity of any claim filed by a preferred shareholder shall not be affected by the terms of this paragraph.

Overview of the Restructuring of Central Capital

**9** The order of Houlden J. of July 9, 1992 directed the restructuring of Central Capital under the aegis of the court. The order, and others that would follow, contemplated that the restructuring would take place in two stages. The first stage involved the transfer to the Administrator of certain major assets of Central Capital to a company to be incorporated called Central Insurance Group Limited (CIGL). This company is frequently referred to in the documentation and the reasons of Feldman J. as "Newco". CIGL was then to be owned by those Central Capital creditors who chose to participate in the reorganization by accepting a reduction in their debts due from Central Capital and exchanging this reduced indebtedness for debentures in CIGL. Subscription for debentures by this means additionally entitled the creditors to subscribe for shares in CIGL. Our understanding from counsel is that the assets transferred to CIGL included the assets acquired by Central Capital from the appellants in purchase agreements described later in these reasons.

**10** The court approved a subscription and escrow agreement setting out this arrangement. In order to participate, the creditors were required to file with the Administrator a proof of claim in the prescribed form along with other documents confirming the creditor's intention to reduce its claim against Central Capital and to subscribe for debentures and shares of CIGL. Claims were to be based on Central Capital's indebtedness to creditors as of June 15, 1992, the date of the court-ordered stay of proceedings. This transaction was completed on October 1, 1992 and resulted in CIGL being owned by the creditors of Central Capital in exchange for a reduction in Central Capital's unsecured debt in the amount of $603 million.

**11** The second stage of the restructuring involved a plan of arrangement under the CCAA. That plan as put forward by Central Capital recognized four classes of creditors, only one of which, namely that of "Senior Creditors", could apply to the appellants. The plan of arrangement, as amended, provided that Central Capital would issue to Senior Creditors pro rata on the basis of their senior claims a class of secured promissory notes in the aggregate principal amount of $20 million of secured debt, which were to be known as first secured notes. A similar arrangement was made for the issuance of $1 million of second secured promissory notes to subordinated creditors. Senior and subordinated creditors included any creditor whose claim had been allowed under the CIGL claims procedure in the first stage, to the extent of that creditor's reduced claim.

**12** The plan of arrangement also called for the creation of a new class of shares in Central Capital to be called the Central New Common Shares. Central Capital would issue to the above Senior and Subordinated Creditors 90 per cent of the new share capital of Central Capital in extinguishment of the balance of their debt. The Central Capital shareholders of all classes would have their existing shares converted into the remaining 10 per cent of the Central New Common Shares. All of the existing preferred and common shares would be cancelled upon implementation of the plan.

**13** The amended plan of arrangement was ultimately voted on and approved by all four classes of creditors of Central Capital. On December 18, 1992, Houlden J. sanctioned this plan of arrangement under the CCAA. He authorized and directed Central Capital to apply for articles of reorgani-

zation pursuant to s. 191 of the CBCA, so as to authorize the creation of the Central New Common Shares for implementation of the amended plan of arrangement. He also lifted the stays of proceedings affecting Central Capital and its ability to carry on business as of January 1, 1993.

**14** The effect of the amended plan of arrangement after approval was that all remaining debts and obligations owed by Central Capital to its creditors on or before June 15, 1992 were extinguished and all outstanding and unissued shares of any kind in Central Capital were cancelled and replaced by Central New Common Shares. Central Capital was then free to carry on business. It was no longer insolvent.

Facts as they Relate to the Claim of McCutcheon

**15** By a share purchase agreement dated June 15, 1987 between Central Capital and Gormley Investments Limited ("Gormley") and Heathley Investments Limited ("Heathley"), Central Capital agreed to purchase all Class "B" voting shares of Canadian General Securities Limited ("CGS") that were owned by Gormley and Heathley. James W. McCutcheon and his brother, who were the sole shareholders of Gormley, represented to Central Capital that CGS owned substantially all of the shares of Canadian Insurance Sales Limited, which in turn owned substantially all of the shares in a number of operating insurance, credit and trust companies. The consideration for the purchase of the CGS shares was $575 per share. The vendors were to be paid $400 per share in cash on closing and were to receive seven Series B senior preferred shares of Central Capital. These shares contained a retraction clause entitling the holder to retract each preferred share on July 1, 1992 for $25. Failing issuance of the shares by Central Capital, the vendors were to receive an additional $175 for each CGS share. The share purchase agreement and later the Articles of Central Capital further provided that the holders of Series B Senior Preferred Shares were entitled to receive dividends as and when declared by the directors of Central Capital out of moneys of the corporation properly applicable to the payment of dividends and in the amount of $1.90625 per share per annum (being 7 5/8 per cent per annum on the stated capital of $25 per share) payable in equal quarterly payments. No dividends were in fact declared.

**16** The certificate of amendment for Central Capital dated July 30, 1987, and the articles of amendment setting out the provisions attaching to the Series B Senior Preferred Shares contain all the terms and conditions governing the said shares. I am setting out below a description of those that are relevant to this appeal.

**17** Pursuant to art. 4.1 of the Senior Series B Provisions, each holder of Series B Senior Preferred Shares was entitled, subject to and upon compliance with the provisions of art. 4, to require Central Capital to redeem all or any part of the Series B Senior Preferred Shares registered in the name of that holder on July 1, 1992 at a price equal to $25 per share, plus all accrued and unpaid dividends thereon, calculated to but excluding the retraction date.

**18** Article 4.2 of the Senior Series B Provisions sets out the procedure for retraction of the shares. Article 4.3 of the Senior Series B Provisions provides that if the redemption by Central Capital of all of the Series B Senior Preferred Shares required to be redeemed on the retraction date would be contrary to applicable law or the rights, privileges, restrictions and conditions attaching to any shares of Central Capital ranking prior to Series B Senior Preferred Shares, then Central Capital shall redeem only the maximum number of Series B Senior Preferred Shares which it determined was permissible to redeem at that time. Article 4.3 provides the mechanism for a pro rata redemp-

tion from each holder of the tendered Series B Senior Preferred Shares and redemption of the tendered Series B Senior Preferred Shares by Central Capital at further dates.

**19** Article 4.4(a) provides that subject to s. 4.4(b), the election of any holder to require Central Capital to redeem any Series B Senior Preferred Shares shall be irrevocable upon receipt by the transfer agent of the certificates for the shares to be redeemed and the signification of election of the holder of the Series B Senior Preferred Shares.

**20** Article 4.4(b) of the Senior Series B Provisions provides that if the retraction price is not paid by Central Capital, Central Capital shall forthwith notify each holder of the Series B Senior Preferred Shares who has not received payment for his deposited shares of the holder's right to require Central Capital to return all (but not less than all) of the holder's deposited share certificates and the holder's rights under art. 4.3 outlined above.

**21** Article 4.5 of the Senior Series B Provisions provides that the inability of Central Capital to effect a redemption shall not affect or limit the obligation of Central Capital to pay any dividends accrued or accruing on the Series B Senior Preferred Shares from time to time not redeemed and remaining outstanding.

**22** Article 7 of the Series Senior B Provisions provides that in the event of the liquidation, dissolution or winding-up of Central Capital, whether voluntary or involuntary, or any other distribution of assets of Central Capital among its shareholders for the purposes of winding up its affairs, the holders of the Series B Senior Preferred Shares shall be entitled to receive, from the assets of Cental Capital, $25 per Series B Senior Preferred Shares, plus all accrued and unpaid dividends thereon, to be paid prior to payment to junior ranking shareholders. Upon payment of such amounts, the holders of the Series B Senior Preferred Shares shall not be entitled to share in any further distribution of assets of Central Capital.

**23** A notice of retraction privilege was sent by Central Capital to the holders of Series B Senior Preferred Shares with a cover letter dated April 23, 1992. The letter stated, among other things, that Central Capital would not redeem any shares because the redemption of such shares would be contrary to applicable law in the context of Central Capital's then current financial situation. McCutcheon and Central Guaranty Trust deposited for redemption 406,800 and 26,000 Series B Senior Preferred Shares, respectively, in accordance with the Senior Series B Provisions and the notice of retraction privilege. The shares were deposited on May 28, 1992, with Montreal Trust Company of Canada, pursuant to the notice of retraction privilege. The shares were properly tendered for redemption in the manner and within the time required by Central Capital's articles of amendment.

**24** Central Capital did not pay the redemption price on July 1, 1992 and on July 20, 1992 it notified each holder of Series B Senior Preferred Shares of its right to require Central Capital to return all of the holder's deposited share certificates as required by art. 4.4(b) of the Senior Series B Provisions. McCutcheon and Central Guaranty Trust did not exercise that right.

**25** Pursuant to the terms of Houlden J.'s order of July 9, 1992 directing the restructuring of Central Capital, McCutcheon submitted to the Administrator, as a creditor of Central Capital, proofs of claim dated September 3, 1992 and September 4, 1992, respectively. McCutcheon claimed the amount of $10,913,593.69 in respect of his Series B Senior Preferred Shares tendered for redemption. Central Guaranty Trust claimed the amount of $697,526.68 in respect of its tendered 26,000 Series B Senior Preferred Shares. McCutcheon also executed and submitted the restated subscrip-

tion and escrow agreement and other documents electing to participate in CIGL. These claims were completed and submitted in the prescribed form and within the time required by Houlden J.'s order.

**26** As was previously noted, these claims were disallowed by the Administrator. The substance of the Administrator's reasons for disallowance was that the ability of Central Capital to redeem these preference shares is restricted by the provisions of the CBCA and it would be contrary to applicable law to redeem the shares in the context of Central Capital's financial position. The relevant provision of the CBCA provides:

> 36(1) [Redemption of shares] Notwithstanding subsection 34(2) or 35(3), but subject to subsection (2) and to its articles, a corporation may purchase or redeem any redeemable shares issued by it at prices not exceeding the redemption price thereof stated in the articles or calculated according to a formula stated in the articles.
>
> (2) [Limitation] A corporation shall not make any payment to purchase or redeem any redeemable shares issued by it if there are reasonable grounds for believing that
>
> (a) the corporation is, or would after the payment be, unable to pay its liabilities as they become due; or
> (b) the realizable value of the corporation's assets would after the payment be less than the aggregate of
>
> (i) its liabilities, and
> (ii) the amount that would be required to pay the holders of shares that have a right to be paid, on a redemption or in a liquidation, rateably with or prior to the holders of the shares to be purchased or redeemed.

Evidently, the Administrator equated redemption by the corporation with the right of retraction by the preferred shareholder. It agreed with Central Capital's position that once it became insolvent in December of 1991, Central Capital no longer had the ability to redeem the shares tendered for retraction and thus McCutcheon was restricted to exercising what rights it might have as a shareholder.

Facts as they Relate to the Claim of SYH

**27** Pursuant to an agreement of purchase and sale made as of June 30, 1989, as amended, Scottish & York Holdings Limited (the predecessor to SYH) sold to Central Capital the shares of Central Canada Insurance Services Limited, Eaton Insurance Company, Scottish & York Insurance Co. Limited and Victoria Insurance Company of Canada (collectively the "Insurance Companies"), except for certain preference shares held by the directors of those corporations. In consideration of this transfer, Central Capital issued to Scottish & York Holdings Limited 60,116,000 Series A Junior Preferred Shares and 9,618,560 Series B Junior Preferred Shares.

**28** The articles of Central Capital provided that it would pay on each dividend payment date prior to the fifth anniversary of this issue, as and when declared by the directors out of the assets of

the corporation properly applicable to the payment of dividends, a dividend of $.08 for each outstanding Series A Junior Preferred Share. The dividend was payable quarterly by the issuance of .02 Series B Junior Preferred Shares for every outstanding Series A Junior Preferred Share. No dividends were in fact declared.

**29** The Articles also provided that Central Capital was obligated to retract the Series A Junior Preferred Shares and Series B Junior Preferred Shares, at the option of the holders of those shares, on the fifth anniversary of their issuance. The retraction price was $1.00 per share plus all accrued and unpaid dividends. Payment of the retraction price of these shares by Central Capital was subject to the provisions of the CBCA, which governs the affairs of Central Capital. For the purposes of this appeal, I believe that we can treat the balance of the provisions relating to these preferred shares as being the same as those governing the McCutcheon Series B Senior Preferred Shares.

**30** Given that the operative date for proving claims against Central Capital was June 15, 1992, the retraction date governing the preferred shares of SYH was some two years removed. Notwithstanding, on September 8, 1992 SYH executed and delivered to the Administrator a proof of claim, a counterpart of the restated subscription and escrow agreement, an initial share subscription and an instrument of claims reduction form, all in the prescribed form and within the time required. The claim was that SYH was holding or entitled to hold the following shares of Central Capital:

(a) 60,116,000 Junior Preferred Series A shares;
(b) 9,618,560 Junior Preferred Series B shares;
(c) 4,611,095 Junior Preferred Series B shares accrued to June 15, 1992 but not yet issued to SYH;

for a total of 74,345,655 shares, each having a retraction value of $1.00. However, because of some adjustments in favour of Central Capital to the purchase price of the shares sold by SYH to Central Capital under the June 30, 1989 agreement of purchase and sale, the net claim as of June 15, 1992 was reduced from $74,345,655 to $72,388,836.

**31** By notice of disallowance dated January 20, 1993, the Administrator disallowed the claim by SYH to subscribe for debentures and common shares to be issued by CIGL. The reasons for the disallowance are similar to those provided for disallowing the claims of McCutcheon. The Administrator found that SYH's right to require Central Capital to retract the Series A and B Junior Preferred Shares only arose on the expiry of the fifth anniversary of their issuance and that Central Capital was precluded from retracting those shares by virtue of its insolvency and the provisions of the CBCA. Hence SYH, like McCutcheon, was limited to exercising what other rights it might have as a shareholder.

Analysis

**32** Although the factual groundwork is necessary for putting in perspective the sole issue before the court, the final question confronting us is a narrow one. Did the retraction clauses in the appellants' shares create a debt owed by Central Canada as of June 15, 1992 within the meaning of the Bankruptcy Act? I think that they did.

**33** It is agreed that the operative section of the Bankruptcy and Insolvency Act is s. 121(1). It reads as follows:

> 121(1) All debts and liabilities, present or future, to which the bankrupt is subject at the date of the bankruptcy or to which he may become subject before his discharge by reason of any obligation incurred before the date of the bankruptcy shall be deemed to be claims provable in proceedings under this Act.

There was no bankruptcy in this case and thus the relevant date was agreed to be June 15, 1992. The obligations of Central Capital to the appellants were incurred before that date, and so the only question becomes whether the obligations created a debt between the appellants and Central Capital.

**34** What then is a debt? All the parties turn to Black's Law Dictionary, quoting different editions. The following is from the Sixth Edition (1990), at p. 403:

> Debt. A sum of money due by certain and express agreement. A specified sum of money owing to one person from another, including not only the obligation of debtor to pay but right of creditor to receive and enforce payment ...
>
> A fixed and certain obligation to pay money or some other valuable thing or things, either in the present or in the future.

**35** The above is consistent with what is defined as a debt by Jowitt's Dictionary of English Law, 2d ed. (1977), at p. 562:

> A debt exists when a certain sum of money is owing from one person (the debtor) to another (the creditor). Hence "debt" is properly opposed to unliquidated damages; to liability, when used in the sense of an inchoate or contingent debt; and to certain obligations not enforceable by ordinary process. "Debt" denotes not only the obligation of the debtor to pay, but also the right of the creditor to receive and enforce payment.

And finally, The Shorter Oxford Dictionary, 3d ed. (1973), at p. 497:

> Debt 1. That which is owed or due; anything (as money, goods or service) which one person is under obligation to pay or render to another. 2. A liability to pay or render something; the being under such liability.

**36** I have no difficulty in finding that the claims of the appellants in the case under appeal fall within all of the above definitions. As will be discussed herein, concern was expressed in this case over whether or not the appellants as creditors were entitled to "receive and enforce payment" on the "debt" because of the insolvency of Central Capital on June 15, 1992. I will deal with the specific arguments relating to the effect of insolvency on this particular indebtedness in due course, but for the moment I am content to observe that the above definitions contemplate only that the creditor's right to recover is the reciprocal of the debtor's obligation to pay. For every debtor there must be a creditor. There may be cases where it is difficult to identify the person who in law may receive and enforce payment, but this is not such a one.

**37** With great respect to the judge of first instance and to the submissions of counsel for the unsecured creditors, I believe that the fundamental error that has been made in these proceedings arises from the conception that the preferred shares in question can either be debt instruments or

equity participation instruments, but they cannot have the attributes of both. Feldman J. had this to say at p. 48 of her judgment:

> Although the right of retraction at the option of the preferred shareholder may be less common than the usual right of the company to redeem at its option, that right is one of the incidents or provisions attaching to the preferred shares, but does not change the nature of those shares from equity to debt. The parties have characterized the transaction as a share transaction. The court would require strong evidence that they did not intend that characterization in order to hold that they rather intended a loan.
>
> In my view, this case turns on whether the right of retraction itself creates a debt on the date the company becomes obligated to redeem even if it cannot actually redeem by payment on that date, or a contingent future debt on the same analysis, not on whether the preferred shares themselves with the right of retraction are actually debt documents.
>
> Because the preferred shares remain in place as shares until the actual redemption, the appellants are not creditors and have no claim provable under the Bankruptcy Act (Canada), and the appeals are therefore dismissed.

**38** As I read these reasons, the learned judge is in effect stating that these instruments are preferred shares in the corporation because the parties have so described them. In the first place, I do not think that describing the documents as preferred shares is conclusive as to what instrument the parties thought they were creating. In the second place, it is not what the parties call the documents that is determinative of their identity, but rather it is what the facts require the court to call them. The character of the instrument is revealed by the language creating it and the circumstances of its creation. Although these instruments may "remain in place as shares" until they are actually redeemed, they also contain a specific promise to pay at a specified date. This is the language of debt. I cannot accept the proposition that a corporate share certificate cannot create a corporate debt in addition to the certificate holder's rights as a shareholder.

**39** The rules relating to the competing rights of shareholders and creditors of an insolvent corporation have become so regulated by governmental action that one can readily lose sight of the common law basis for making a distinction. To understand the difference in treatment, we must re-examine what a share of a corporation represents. Initially, a share is issued by the corporation to raise share capital. The price of the share is money or the promise of money. Accordingly, an individual share is one of a number of separate but integral parts of the authorized capital of a corporation. Even though it is the shareholders who contribute to the capital of the corporation, the capital remains the property of the corporation. The shareholders, however, as owners of the shares of capital, effectively control the corporation. They have the responsibility of managing its affairs through their control over the board of directors and in popular terminology are considered to be the owners of the corporation. However, the corporation is a separate entity in law, and if in the course of carrying out its business it incurs debts to third parties, those debts are those of the corporation. A corporation is an intangible and its capital therefore represents its substance to third parties having business dealings with the corporation. A preferred share is simply a share of a class of issued

shares which contains a preference over other classes of shares, whether preferred or common: see Sutherland, Fraser and Stewart on Company Law of Canada, 6th ed. (1993), at pp. 157 and 195 for further discussion.

**40** The rights of shareholders are conveniently summarized by R.M. Bryden in his chapter, "The Law of Dividends", contained in Ziegel ed., Studies in Canadian Company Law (1967), at p. 270:

> The purchaser of a share in a business corporation acquires three basic rights: he is entitled to vote at shareholders' meetings; he is entitled to share in the profits of the company when these are declared as dividends in respect of the shares of the class of which his share forms a part; and he is entitled, upon the winding-up of the corporation, to participate in the distribution of the assets of the company that remain after creditors are paid. A fourth right which should be noted is the right to transfer ownership in his share, whereby the owner for the time being may realize upon the increase in value of the company's assets, or its favourable prospects, by selling his share at a price reflecting the buyer's estimation of the value of the rights he will acquire. Unless the shareholder chooses to sell his share, he can realize a return upon his investment only through receipt of dividends or by the return of his capital upon an authorized reduction of capital or winding up.

**41** Shareholders are variously characterized as entrepreneurs, investors or risk-takers and as such they have the opportunities of benefitting from the successes of the corporation and suffering from its failures. While the corporation is an operating entity, the shareholders receive their rewards, if there are any, through the payment of dividends declared from time to time by the board of directors. While the source of these dividends is not restricted to surplus funds, the result of the payment of the dividend must not result in a return of capital to the shareholders. The classic justification for this rule was stated by Sir George Jessel, Master of the Rolls, in Flitcroft's Case (1882), 21 Ch. D. 519 at pp. 533-34, 52 L.J. Ch. 217 (C.A.):

> The creditor has no debtor but that impalpable thing the corporation, which has no property except the assets of the business. The creditor ... gives credit to that capital, gives credit to the company on the faith of the representation that the capital shall be applied only for the purposes of the business, and he has therefore a right to say that the corporation shall keep its capital and not return it to the shareholders ...

**42** Creditors, on the other hand, do not have an ownership or equity interest in the corporation. They are third parties who have loaned money or otherwise advanced credit to the corporation. They look to the company for payment in accordance with the terms of the contract creating the indebtedness. They are also restricted in their recovery to the amounts stipulated in the terms of indebtedness. They are entitled to payment regardless of the financial circumstances of the debtor corporation and accordingly are not restricted to receiving payment of the debt from surplus. They can be paid out of assets or through the creation of further indebtedness. It is immaterial how the corporation records this indebtedness in its internal books. In some circumstances the indebtedness could properly reflect the acquisition of property from a creditor as a capital asset. This does not,

however, convert the creditor into an investor. The vendor of the property remains a creditor and retains priority over shareholders in the event of a bankruptcy or insolvency.

**43** In my view, the reasons under appeal do not reflect a sensitivity to the circumstances which gave rise to the issuance of the preference shares. The shares were not issued by Central Capital to the general public in order to raise capital and do not represent an investment by the public in the capital of the corporation. They were issued to specific persons as payment for the acquisition of specified assets. While the corporation was authorized by its articles of incorporation to issue preferred shares generally, the shares issued to the appellants were structured to meet the requirements of the appellants as vendors of the controlling interest in the operating companies that Central Capital was acquiring. In my view, these preference shares are the equivalent of vendor shares in that the appellants received them in exchange for the transfer of assets to Central Capital.

**44** In the case of McCutcheon, the retraction provision in the preferred shares represented only partial payment of an agreed value for the assets, but in the case of SYH, they represented the full value. In both cases, the agreed value as reflected in the retraction price was guaranteed by Central Capital to be retractable at a fixed price at a predetermined date. By postponing the obligation to pay the purchase price in this way, Central Capital was using the retraction provisions of the preference shares as a vehicle for the financing of its expanding asset base. The appellants, for their part, deferred the realization of the purchase price of their assets to the agreed dates and thereby extended credit to the corporation. In return for extending credit for some or all of the selling price, the appellants agreed to receive dividends calculated in advance but payable as and when declared by the board of directors.

**45** Thus, in looking at the substance of the transaction that led to the issuance of the preference shares, it appears to me that the retraction clauses were promises by Central Capital to pay fixed amounts on definite dates to the appellants. They evidenced a debt to the appellants. The fact that the appellants as holders of the preference shares had rights as shareholders in the corporation up to the time when the retraction clauses were exercisable did not affect their right to enforce payment of the retraction price when it became due.

**46** The validity of an analysis directed to the substance of the transaction is supported by Canada Deposit Insurance Corp. v. Canadian Commercial Bank, [1992] 3 S.C.R. 558, 97 D.L.R. (4th) 385, a judgment of the Supreme Court of Canada delivered by Iacobucci J. The case involved a number of corporations constituting a support group which entered into an arrangement to provide emergency financial assistance to Canadian Commercial Bank ("CCB"). On the ultimate failure of the bank, the issue arose as to whether the moneys advanced to CCB under this support arrangement were in the nature of a loan or in the nature of a capital investment. I find instructive to our situation Iacobucci J.'s observation at pp. 590-91:

> As I see it, the fact that the transaction contains both debt and equity features does not, in itself, pose an insurmountable obstacle to characterizing the advance of $255 million. Instead of trying to pigeonhole the entire agreement between the Participants and CCB in one of two categories, I see nothing wrong in recognizing the arrangement for what it is, namely, one of a hybrid nature, combining elements of both debt and equity but which, in substance, reflects a debtor-creditor relationship. Financial and capital markets have been most creative in the variety of investments and securities that have been fashioned to meet

> the needs and interests of those who participate in those markets. It is not because an agreement has certain equity features that a court must either ignore these features as if they did not exist or characterize the transaction on the whole as an investment. There is an alternative. It is permissible, and often required, or desirable, for debt and equity to co-exist in a given financial transaction without altering the substance of the agreement. Furthermore, it does not follow that each and every aspect of such an agreement must be given the exact same weight when addressing a characterization issue. Again, it is not because there are equity features that it is necessarily an investment in capital. This is particularly true when, as here, the equity features are nothing more than supplementary to and not definitive of the essence of the transaction. When a court is searching for the substance of a particular transaction, it should not too easily be distracted by aspects which are, in reality, only incidental or secondary in nature to the main thrust of the agreement.

(Emphasis in original)

**47** I have no difficulty in finding that the appellants' preferred shares with their retraction clauses are of "a hybrid nature, combining elements of both debt and equity". As to the equity component, the appellants are shareholders prior to exercising their retraction rights in that they have the right to vote in certain circumstances and have a right to receive dividends when and if they are declared by the board of directors. The debt component is more significant however. The shares were not issued to investors, but to vendors of property. The vendors were entitled to receive a fixed sum at a specified time in payment therefor. Pending payment, the vendors were entitled to receive dividends which were the equivalent of interest on the unpaid balance.

**48** I can think of no reason why the holders of these preferred shares should not be treated as both shareholders and creditors. It does not concern me that these appellants act as shareholders before their retraction rights are exercisable. Nor do I see any hardship to other creditors of Central Capital arising from the ability of these appellants to claim as creditors in the restructuring of the company given that the appellants are unpaid with respect to substantial assets sold to the corporation and now transferred on the restructuring to CIGL.

**49** Much was made in argument of the fact that the retraction amounts could not be paid on the retraction dates. In the case of McCutcheon, the corporation was insolvent and subject to court administration on the due date of July 1, 1992. In the case of SYH, the retraction date did not arrive before the reorganization was complete.

**50** The narrow issue of the effect of insolvency on a debt has been dealt with by the British Columbia Court of Appeal in Re East Chilliwack Agricultural Co-Operative (1989), 74 C.B.R. (N.S.) 1, 58 D.L.R. (4th) 11. In this case, the appellants were one-time members of three co-operative associations. The rules of the co-operatives permitted a member to withdraw upon written notice to the board of directors to that effect. The member was entitled to elect to have his shares redeemed either in equal instalments over five years or in one payment with interest at the end of five years. In April of 1987, the superintendent of co-operatives, under the authority of the Cooperative Association Act, R.S.B.C. 1979, c. 66, suspended the co-operatives' right to redeem their shares until their financial situation was no longer impaired. The three co-operatives subsequently went bankrupt and a two-fold issue came before the bankruptcy court: (1) whether those members whose notices of withdrawal had been accepted by the board of directors but who had not

yet received the value of the shares were entitled to rank as unsecured creditors, and (2) whether those who had delivered notices that had not been accepted were to be treated as unsecured creditors. The court of first instance found that the members were shareholders and answered both questions in the negative. That judge was reversed on appeal with the majority of the court deciding that the answer to both questions was yes. Hutcheon J.A. for the majority stated at p. 13:

> I shall use Mr. Neels [a co-operative member] as my example. According to R. 3.06 he ceased to be a shareholder in May 1983. In May 1984 the Agricultural Co-operative owed him the first of five payments, or $686.40. I know of no principle of law that would support the proposition that Neels could not sue for that amount if the Agricultural Co-operative failed to pay in May 1984. Of course, the superintendent of co-operatives has power under s. 15(2) to suspend payments if, in his opinion, the financial position of the co-operative was impaired. Subject to that power, the position of Neels and the Agricultural Co-operative would be that of ordinary creditor and debtor. In my opinion, the order made by the judge cannot be sustained on the first ground.

From this case, I extract the proposition that the fact of an insolvency, whether declared or not, does not change the nature of the relationship between debtor and creditor. It continues notwithstanding the inability of the debtor to pay or the creditor to collect.

**51** It appears to me, with deference, that the issue of the effect of Central Capital's insolvency on the character of the retraction payments is something of a red herring. The contest in this appeal is between those who are conceded to be unsecured creditors and those whose claim to such status is contested. In both cases, any right to payment was suspended by Central Capital's announcement in December of 1991 that it was insolvent and that it had suspended all payments of principal and interest to unsecured creditors. This course of action was not freely chosen but was required by law. Any payments to creditors after the date of insolvency would be voidable at the instance of creditors on the basis that they were fraudulent preferences. In addition to ss. 95 and 96 of the Bankruptcy Act dealing with fraudulent preferences generally, there is provincial legislation in the form of the Fraudulent Conveyances Act, R.S.O. 1990, c. F-29, and the Assignments and Preferences Act, R.S.O. 1990, c. A-33, that would be applicable. Counsel for the unsecured creditors maintains that the right to redeem shares, including preference shares, was postponed by s. 36(2) of the CBCA, supra. I am not certain that s. 36(2) applies to the retraction provisions of the appellants' preference shares as opposed to the redemption privileges of Central Capital, but in my opinion the point is irrelevant to this appeal. Once Central Capital acknowledged its insolvency, it could neither redeem its shares nor honour its retraction obligations. The whole purpose for the creditors applying to the court for a stay of Central Capital's obligations, including those of the acknowledged unsecured creditors, was to arrange for a scheme of payments to all creditors that could not be subject to attack as preferences. There is no suggestion on the evidence before us that the claims of unsecured creditors accepted by the Administrator were claims that had crystallized prior to the insolvency of Central Capital. Nor is it suggested that any creditors were rejected because some or all of their claims were not payable until after the date of the insolvency. The fact of insolvency, by itself, does not provide a rational basis for distinguishing the claims of the appellants from those of other unsecured creditors.

**52** Much also was made of the provision in the Articles authorizing the shares in question, which states that if the obligation to redeem "would be contrary to applicable law", then Central Capital "shall redeem only the maximum number of [shares] it is then permitted to redeem". Counsel for the unsecured creditors submits that the reference to "applicable law" is to s. 36 of the CBCA. The reference certainly embraces the CBCA, but it is not restricted by its terms to that statute. For example, "applicable law" would also capture s. 101 of the Bankruptcy and Insolvency Act, which provides for penalties against directors and shareholders where insolvent companies redeem shares or pay dividends.

**53** There was no evidence led as to why this provision was placed in the articles and the share certificates. It appears to be a standard clause in all the preference shares issued by the corporation and not just those that were adapted to the appellants' situations where specific retraction clauses were drafted to satisfy the particular asset acquisitions. For my part, I have difficulty in understanding how a consideration of this provision assists the process of determining the underlying character of the retraction obligations. The statement is so self-evident that it is almost banal. I can only assume that the statement was included in the share provisions of a corporation marketing its securities world-wide so as to inform purchasers that legal restrictions in this jurisdiction apply to the company's right to redeem shares.

**54** In summary then regarding the insolvency argument, these various statutes prohibit payments of any kind to shareholders by an insolvent company. As I understand it, counsel does not question that when a dividend has been lawfully declared by a corporation, it is a debt of the corporation and each shareholder is entitled to sue the corporation for his proportion: see Fraser and Stewart, supra, at p. 220 for a list of authorities. However, once a company is insolvent it cannot make payments to shareholders or creditors so long as it continues to be insolvent. On the other hand, nowhere in the CBCA or elsewhere will we find authority for the proposition that once a corporation is insolvent, it is no longer obliged to pay its debts. The obligation is postponed until the insolvency is corrected or the corporation makes an accommodation with its creditors and obtains a release with or without the assistance of the various statutes dealing with insolvency.

**55** The existence of provisions prohibiting payment to shareholders and creditors on insolvency does not in any way assist the determination of whether the retraction obligations at issue in this appeal constitute a debt or a return of capital at the time they are payable. Speaking of the obligation to honour the retraction in terms of the corporation redeeming its shares also introduces the wrong emphasis. The corporation is not redeeming the shares at its option as contemplated by most redemptions. It is being forced to redeem them because of a prior contractual obligation for which the preferred shareholder gave good consideration. It is for this reason that I question whether s. 36 of the CBCA is the appropriate reference point. This is not the type of payment which concerned Jessel M.R. in Flitcroft's Case, supra.

**56** At the risk of oversimplifying this case, it appears to me that many of the arguments made against the appellants' claims to be creditors of Central Capital are impermissible in the context of the agreed statement of facts. The issue in appeal is frozen in time by the stipulation that the court is to determine if these retraction clauses created a debt within the meaning of the Bankruptcy and Insolvency Act on June 15, 1992. The arguments against the appellants' claims also ignore that debts under s. 121(1) of the Bankruptcy Act need not be payable at the date of the bankruptcy (or June 15, 1992 in our scenario). They need only come beneath the broad umbrella of "debts and liabilities, present and future, to which [Central Capital] is subject" on June 15, 1992. The fact that the debts

could not be paid after June 15, 1992, does not mean that they were not provable claims pursuant to s. 121 of the Bankruptcy and Insolvency Act. Moreover, assuming the retraction clauses created a debt payable on a future date, neither the order of Houlden J. nor the restrictions in the articles creating the shares themselves purported to extinguish that debt.

**57** There is nothing in either the articles of Central Capital or in the law that excuses the obligation to pay the retraction amounts. Rather, discharge of the obligation is simply postponed until the cessation of the disabling event of insolvency. Article 4.3 of the Senior Series B Provisions provides the mechanism for future redemption of tendered shares that are not redeemed because such redemption would be contrary to law. Article 4.5 provides that the inability to effect a redemption does not affect the obligation to pay dividends accrued or accruing on the unredeemed shares.

**58** So far as SYH is concerned, the retraction price was not payable until the fifth anniversary of the June 1989 sale of assets. Therefore, no issue of the effect of insolvency arose in 1992. The orders of Houlden J. of June 15 and July 9, 1992 changed the rules of the game. If this appellant is a creditor, it does not have to wait until the retraction date. It can claim as a creditor now. It did and the claim was disallowed. However, if this court holds that the claim should have been allowed, then in accordance with the narrow issue put to us, SYH is entitled to be accepted as a full creditor in the entire reorganization of Central Capital.

**59** An additional factor raised by counsel during argument was that art. 7, supra, provides that in the event of the liquidation, dissolution or winding-up of Central Capital, whether voluntary or involuntary, or any other distribution of assets among its shareholders for the purpose of winding up its affairs, the holders of these preferred shares are entitled to recover "from the assets of Central Capital" the retraction price plus all accrued and unpaid dividends thereon. Such amount is to be paid prior to payment to junior ranking shareholders. The article further provides that "[u]pon payment of such amounts, the holders of [the preferred shares] shall not be entitled to share in any further distribution of assets of [Central Capital]". Because it is trite law that shareholders are entitled to recover from assets only after all ordinary creditors have been paid in full, counsel for the unsecured creditors submits that the fact that the clause contemplates priorities between shareholders on a winding-up or a liquidation of assets is clear evidence that they were shareholders only.

**60** I have two responses to this submission. The first is the obvious, that we are not dealing with this contemplated event. We are dealing with a reorganization in which the parties have put a single question to the court: are the appellants creditors? Consideration of issues of priority or the valuation of claims have been taken away by the narrow scope of the agreed question. If the answer to the question posed is yes, then in accordance with the agreed statement of facts, the appellants are entitled to have their claims as creditors allowed under the subscription and escrow agreement and to participate in the amended plan of arrangement as senior creditors. If the answer is no, they are to be treated as the Administrator has treated them: they are not creditors at all and are restricted to receiving Central New Common Shares under the amended plan of arrangement.

**61** My second response is that counsel for the unsecured creditors misses the significance of the clause. He assumes that there will be a deficiency in all circumstances leading up to a liquidation, dissolution or winding-up that will necessitate a pro rata distribution, first to creditors and then to shareholders of all classes. However, the clause does not say that those with retraction rights are not creditors. It says that the retraction amounts are to be paid out of assets, not surplus. Once the retraction amounts have been paid in full, the appellants are not entitled to share in any further distribution. This contemplates a surplus after all creditors, including the appellants, have been paid in

full. Accordingly, far from classifying the appellants as shareholders, the clause provides that they are not entitled to be treated as shareholders under a winding-up or liquidation but only as creditors.

**62** Finally, with respect to SYH's claims, it was submitted that these claims were so contingent as to be virtually non-existent. The claims anticipate a retraction date that as of June 15, 1992 was some two years into the future. Upon approval of the amended plan of arrangement on December 18, 1992, the shares of SYH were cancelled and replaced by a new issue of shares, the Central New Common Shares. Counsel relied upon the finding of Feldman J. that there was then no discernable basis upon which the retraction could occur. Once again, with respect, this conclusion misses the point. Following the final order of Houlden J. approving the amended plan of arrangement, all the shares and all the debts of Central Capital disappeared. There was thereafter no discernable basis upon which any event contemplated by any debt or share instruments could occur. We are only concerned with the status of shareholders and creditors as of June 15, 1992.

**63** Based on the reasons set out above, I have concluded that the retraction amounts do fall within the definition of debts and liabilities, present or future, to which Central Capital was subject on June 15, 1992. This does not apply to undeclared dividends, however, because until a dividend is declared no action on behalf of a shareholder lies to enforce its payment: see Fairhall v. Butler, [1928] S.C.R. 369 at p. 374, [1928] 3 D.L.R. 161. If undeclared dividends have been claimed by any of the appellants they should be disallowed. In all other respects the claims should be allowed.

**64** Accordingly, I would allow the appeals, set aside the order of Feldman J. and order that the appellants have provable claims that are to be allowed by the Administrator. The record does not disclose what order if any Feldman J. made as to costs. Certainly the appellants are entitled to their costs of this appeal. If the parties are unable to agree with respect to any other disposition of costs, I would suggest that they submit their positions to the court in writing.

**65** WEILER J.A.: -- I have had the benefit of reading the reasons of Finlayson J.A. and for the reasons which follow I respectfully disagree with his conclusion that the appellants are entitled to prove a claim pursuant to the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 (the "CCAA").

**66** Section 12(1) of the CCAA requires that persons wishing to participate in a reorganization have claims which would be provable in bankruptcy. Section 121(1) of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, states that "[a]ll debts and liabilities, present or future ... shall be deemed to be claims provable in proceedings under this Act".

**67** In order to decide whether the obligation of Central Capital to redeem the preferred shares of the appellants is a claim provable in bankruptcy, it is necessary to characterize the true nature of the transaction. The court must look to the surrounding circumstances to determine whether the true nature of the relationship is that of a shareholder who has equity in the company or whether it is that of a creditor owed a debt or liability by the company: Canada Deposit Insurance Corp. v. Canadian Commercial Bank, [1992] 3 S.C.R. 558, 97 D.L.R. (4th) 385. In this case, the decision is not an easy one. Where, as here, the agreements between the parties are reflected in the articles of the corporation, it is necessary to examine them carefully to characterize the true relationship. It is not disputed that if the true nature of the relationship is that of a shareholder-equity relationship after the retraction date and at the time of the reorganization, then the appellants do not have a claim provable in bankruptcy. Consequently, they will not have a claim under the CCAA.

**68** As I see it, three main questions need to be addressed:

(1) Was Feldman J. correct in characterizing the relationship between Central Capital and the companies owned by James McCutcheon ("McCutcheon"), and between Central Capital and Scottish and York Holdings Limited (the predecessor to S.Y.H., hereinafter referred to as "SYH"), as a shareholder relationship?

(2) Did the nature of the relationship change after the retraction date for redeeming the shares of McCutcheon or, in the case of SYH, at the time of the reorganization?

(3) If the nature of the relationship is not a shareholder-equity relationship, are the appellants entitled to prove a claim under the CCAA?

**69** In addition, the appellants raise the question of whether they have a right to prove a claim for dividends, which have accrued but have not yet been declared payable. The price to be paid by Central Capital to McCutcheon on the retraction date, July 1, 1992, was $25 per share plus all accrued and unpaid dividends thereon. The dividends are therefore part of the retraction price. Similar provisions apply to SYH.

**70** The reasons of Finlayson J.A. contain a comprehensive statement of the background to the litigation and I will therefore only refer to the facts in a summary fashion.

**71** James McCutcheon and his brother sold their shares in Central Guarantee Trust Company to Central Capital Corporation ("Central Capital"), a trust company, for $575 a share. They received $400 per share in cash. The balance of $175 owing on each share was paid through the issue of seven preferred shares in Central Capital, with each share having a par value of $25. Following this transaction, McCutcheon purchased his brother's shares. These preferred shares, known as Senior Series B Preferred Shares, were to be listed on the Toronto Stock Exchange. These shares carried with them a retraction privilege. The shareholder had the right to have his shares redeemed by Central Capital on July 1, 1992, for $25 a share, provided that such redemption would not be "contrary to law in the context of the Corporation's current financial position". McCutcheon chose not to sell his shares.

**72** Scottish & York Holdings Limited (the predecessor to SYH) sold its shares in certain insurance companies which it owned to Central Capital. Central Capital paid for these shares by the issue of Series A Junior Preferred Shares. These shares were not posted on a stock exchange. SYH had the right to have its shares redeemed by Central Capital on or after September 1994 at a price of $1.00 per share, subject to the provisions of the Canada Business Corporations Act, R.S.C. 1985, c. C-44 (the "CBCA").

**73** It should be noted that the right of retraction was not unique to these two classes of shareholders. Even common shareholders had the right to have their shares retracted under certain circumstances.

**74** By December 1991, Central Capital was unable to pay its liabilities as they became due and its total liabilities greatly exceeded the value of its assets. As a result, the various banks and subordinated debtholders, collectively referred to as the lenders, had a choice to make. Inasmuch as the definition of a corporation in s. 2 of the Bankruptcy and Insolvency Act precludes a creditor from bringing a petition against a trust company, they could either wind up Central Capital under the Winding-up Act, R.S.C. 1985, c. W-11, or they could try to restructure Central Capital under the

CCAA. In a winding-up or liquidation, the trustee would sell the company's assets, either piecemeal or as a going concern, to third parties. The proceeds from the sale would then be distributed to those who proved a claim according to set priority rules. In a reorganization, existing fixed amounts owed to Central Capital's creditors would be traded for new claims and ownership interests in the reorganized corporation which would remain a going concern. The lenders chose to reorganize.

**75** Two transactions were involved. In the Consolidated Insurance Group Limited transaction, or "CIGL transaction", Central Capital transferred some of its significant assets to a newly incorporated company, CIGL. Thirty-nine creditors of Central Capital then elected to exchange a portion of Central Capital's debt owing to them for equity in this newly incorporated company. In the second transaction, common shares were issued for the remaining assets of Central Capital. The creditors of Central Capital were given 90 per cent of the common shares of the reorganized company. The balance of 10 per cent was allocated to the shareholders of Central Capital. All of the preferred, common and subordinate voting shares in Central Capital were then converted into these "new" common shares. The reorganization was subsequently approved by the creditors and sanctioned by the court as required by the Act, but this approval was given without prejudice to any claims that McCutcheon and SYH might have.

**76** McCutcheon's position was that the right to have his shares retracted accrued before the reorganization, and that his exercise of this right of retraction in May 1992 constituted a present debt or liability entitling him to rank as a creditor in the CIGL transaction and in the reorganized Central Capital. SYH's position was that the right to have its shares retracted in 1994 created a future debt or liability and thus a provable claim. The administrator of Central Capital disallowed both claims. McCutcheon and SYH appealed the administrator's decision to Feldman J. In dismissing their appeals, she held that the appellants were shareholders and that the right of retraction attaching to the shares did not change the nature of the shares from equity into debt.

1. Was Feldman J. correct in characterizing the agreement between Central Capital and the companies owned by McCutcheon, and between Central Capital and SYH, as creating a shareholder relationship between the parties?

**77** Feldman J. analyzed the transaction and came to the conclusion that it was an equity transaction.

**78** Finlayson J.A. is of the opinion that the nature of this transaction is different and that Feldman J. erred in not showing sensitivity to the fact that she was dealing with the sale of a business by its owners. He is of the opinion that the shares issued by Central Capital are the equivalent to "vendor shares" in that the appellants received them in exchange for the transfer of assets to Central Capital. He does not see the transaction as being either a contribution to capital by McCutcheon and SYH or as a return of capital. Although the transaction has debt and equity features, Finlayson J.A. is of the opinion that the true nature of the transaction is that of a debt owing by Central Capital to McCutcheon and SYH for the shares in their companies.

**79** My analysis of the transaction is that when McCutcheon sold his shares in Central Guaranty and took back preferred shares in Central Capital as part payment, he transferred part of his capital investment from a smaller entity to a larger entity. Similarly, SYH transferred its investment in the shares of the insurance companies for shares in the larger entity of Central Capital. Both appellants could look to a larger asset base than before to generate a return on their capital. Until the retraction

date, McCutcheon chose to take the risk of continuing his investment in Central Capital, which offered the prospect of a stable, yet relatively high, annual return through the receipt of 7 5/8 per cent dividends. Because the shares traded on the Toronto Stock Exchange, he would have had the option of realizing upon his investment by selling his shares for what they would bring on the open market, but he did not do so. In the case of SYH, although these shares were not required to be publicly listed, the corporation's articles did not restrict their transfer. The corporation's articles indicate that these shares had some preference over other shares with respect to the right to receive dividends and in the distribution of assets after creditors are paid on a liquidation. As preferred shareholders, McCutcheon and SYH did not have a voice in company affairs unless the company failed to pay the dividends it had promised to pay. This is quite typical: see Welling, Corporate Law in Canada, 2d ed. (1991) at p. 604; Ziegel et al., Cases and Materials on Partnership and Canadian Business Corporations, 2d ed. (1989) at p. 1198. Risk-taking, profit-sharing, transferability of investment, and the right to participate in a share of the assets on a liquidation after the creditors have been paid are the hallmarks of a shareholder: see R.M. Bryden, "The Law of Dividends," contained in Ziegel ed., Studies in Canadian Company Law (1967) at p. 270. In my opinion, Feldman J. was correct that the true nature of the relationship between the parties initially was that of an equity transaction.

2. Did the nature of the relationship change after the retraction date for McCutcheon's shares and did the reorganization trigger a right of redemption respecting SYH's shares?

**80** Ordinarily, shareholders cannot realize on their investment in a company except by transferring their shares. The retraction privilege attaching to the shares gives the preferred shareholders the option of realizing on their investment other than by transferring their shares to a third party.

**81** Feldman J. found that McCutcheon continued to be a shareholder after the retraction date and that he remained a shareholder at the time of the reorganization. She found SYH's claim to be too remote inasmuch as the retraction date had not yet arrived at the time of the reorganization.

**82** The appellants argue that Feldman J. erred in this conclusion. They submit that although McCutcheon and SYH may have been shareholders initially, this relationship changed. Upon McCutcheon's exercise of his right to have the corporation pay him the retraction price of his shares, he ceased to be a shareholder. When Central Capital failed to pay him, he became a creditor of the corporation. In the case of SYH, it is submitted that when the lenders opted to reorganize the company, they, in effect, triggered the obligation to redeem SYH's shares.

(a) Nature of the transaction's relationship to the capital structure of the corporation

**83** Section 25(3) of the CBCA states that shares shall not be issued until the consideration for the shares is fully paid either in cash or with property having a fair market value equivalent to the shares issued. Therefore, by issuing preferred shares with a fixed par value, Central Capital paid McCutcheon for his shares of Central Guaranty and paid SYH for the shares of the insurance companies that Central Capital received. Central Capital could not issue preferred shares except as full payment for the shares it received. The preferred shares were part of the capital of Central Capital and the preferred shares were always shown as shareholders' equity on Central Capital's books. The capital of the corporation is representative of the assets available to pay creditors. If, on the date for redemption of McCutcheon's shares, or on the date of reorganization in the case of SYH, the shares

are redeemed, the amount paid must be deducted from the stated capital of the corporation: s. 39 CBCA. Consequently, the total assets that Central Capital will have available to pay the lenders and other creditors outside the corporation will be reduced. A reduction of capital by the redemption of redeemable shares is permitted under the CBCA but only where the requirements of s. 36 are met.

(b) Section 36 of the CBCA

**84** Section 36 of the CBCA makes the ability of a corporation to redeem its redeemable shares subject to (1) its articles and (2) a solvency requirement. For ease of reference s. 36 is reproduced below.

> 36(1) Notwithstanding subsection 34(2) or 35(3) [both of which deal with a corporation's acquisition of its own shares in other circumstances], but subject to subsection (2) and to its articles, a corporation may purchase or redeem any redeemable shares issued by it at prices not exceeding the redemption price thereof stated in the articles or calculated according to a formula stated in the articles.
>
> (2) A corporation shall not make any payment to purchase or redeem any redeemable shares issued by it if there are reasonable grounds for believing that
>
> (a) the corporation is, or would after the payment be, unable to pay its liabilities as they become due; or
> (b) the realizable value of the corporation's assets would after the payment be less than the aggregate of
>
> (i) its liabilities, and
> (ii) the amount that would be required to pay the holders of shares that have a right to be paid, on a redemption or in a liquidation, rateably with or prior to the holders of shares to be purchased or redeemed.

(Emphasis added)

**85** There is no dispute that Central Capital was unable to redeem McCutcheon's shares on the retraction date. Nor could it redeem SYH's shares on the date of the reorganization. The appellants agree that the effect of s. 36 renders the agreement between themselves and Central Capital unenforceable. It is the position of the appellants, however, that s. 36 does not extinguish a debt or liability which they say has been created. The appellants rely on the decision in Re East Chilliwack Agricultural Co-operative (1989), 74 C.B.R. (N.S.) 1, 58 D.L.R. (4th) 11 (B.C.C.A.), in support of their position that a debt or liability is created notwithstanding the solvency requirements of s. 36 respecting payment. The appellants' submission does not take into consideration the major differences between the decision in East Chilliwack and the present situation relating to the timing, effect of the solvency requirements and the provisions in the articles governing the relationship of the parties.

**86** (1) In East Chilliwack, farmers who owned shares in an agricultural co-operative gave notice to the co-op of their intention to have their shares redeemed. After the notices had been given,

the superintendent of co-operatives suspended the right of the co-op to redeem its shares. Here, the request to redeem the shares by McCutcheon and the retraction date occurred after Central Capital had sent out a notice that it would not be able to redeem the shares due to its financial position. SYH had no right to demand that its shares be retracted until the retraction date, which was some two years after the date of Central Capital's insolvency.

**87** As in the instant case, the issue in East Chilliwack was whether the farmers were entitled to rank with the creditors of the co-op. Hutcheon J.A., with Toy J.A. concurring, held that they were entitled to be treated as creditors.

**88** At the outset of his reasons, Hutcheon J.A. noted, at p. 11, that the effect of the superintendent's suspension on the farmers' rights was not argued on appeal and that the court had been asked to determine the status of the farmers without regard to the suspension.

**89** Here, the effect of Central Capital's inability to redeem its shares due to insolvency is very much in issue and cannot be ignored. Although the articles provide for the redemption of all of the shares held by McCutcheon and SYH on or after the retraction date, the articles also state that Central Capital will only redeem so many of its shares as would not be "contrary to law". Pursuant to s. 36(1) of the CBCA, a corporation may purchase or redeem redeemable shares, but the corporation is prohibited from doing so if the corporation is unable to pay its liabilities as they become due or if the assets of the corporation are less than the total of its liabilities and the amount required for the redemption. Because Central Capital could not comply with the solvency requirements, redemption would be "contrary to law".

**90** (2) In East Chilliwack, supra, at p. 13, the rules of the co-op provided that upon the giving of a notice of redemption, the farmer giving it ceased to be a shareholder. Central Capital's articles do not state that a request for redemption of the holder's shares terminates his status as a shareholder. McCutcheon continued to have the right to receive dividends pursuant to art. 4.5 while his shares were not redeemed. In effect, so long as Central Capital was unable to redeem the shares but had profits, McCutcheon continued to be entitled to a share of the profits through the declaration of dividends. If the dividends remained unpaid for eight consecutive quarters then, pursuant to art. 8, McCutcheon had the right to receive notice of, and to attend, each meeting of shareholders at which directors were to be elected and was entitled to vote for the election of two directors. The articles relating to the preferred shares held by SYH contain a similar provision. The result of insolvency as envisaged by the articles was that McCutcheon and SYH would continue as shareholders.

**91** (3) In East Chilliwack, supra, Hutcheon J.A. held, at p. 13, that, subject to the power of the superintendent of co-operatives, the farmer's position would be that of an ordinary creditor.

**92** Here, the terms attaching to McCutcheon's shares do not give him that right. Instead, he is given the right to continue to receive dividends so long as the company cannot pay him. The articles relating to the shares held by SYH contain a similar provision. In addition, art. 4.3(b), respecting the retraction of the shares, indicates that if the directors have acted in good faith in making a determination that the number of shares the corporation is permitted to redeem is zero, then the corporation is not liable in the event this determination proves inaccurate. This would hardly be the position vis-à-vis an ordinary creditor.

**93** (4) Article 8 and a similar provision in the articles relating to the shares held by SYH provide that upon a sale of all or a substantial part of the company's undertaking, the preferred share-

holders have a right to receive notice of and to be present at the meeting called to consider this sale. The farmers in East Chilliwack do not appear to have had any similar right.

**94** (5) Article 7 provides that in the event of a liquidation, dissolution or winding-up of the corporation the preferred shareholders have a right to receive $25 per Series B Senior Preferred Shares before the corporation pays any money or distributes assets to shareholders in any class subordinate or junior to the Series B Senior Preferred Shares. Similarly, SYH, as the holder of Series A and B Junior Preferred shares, has the right, upon the dissolution or winding-up of the corporation, to receive a sum equivalent to the redemption amount for each series junior preferred share. This right is subject to the rights of shares ranking in priority to the shares of these series, but is ahead of the rights of the holders of common shares.

**95** Nothing in the articles concerning the retraction date affects the right of McCutcheon and SYH to participate in Central Capital's liquidation. The participation of the farmer in East Chilliwack ceased once he had given notice to redeem. Article 4.4 of Central Capital provides that once the shares have been tendered for retraction this election is irrevocable on the part of the holder. In the event that payment of the retraction price was not made, however, the holder had the right to have all deposited share certificates returned. Central Capital offered to return McCutcheon's shares to him, but he refused. Because McCutcheon retained all the rights and privileges of a preferred shareholder after the retraction date, the fact that he refused to take back his share certificates cannot alter the true nature of the relationship. The refusal was merely evidence of a dispute concerning what the relationship was. SYH also retained its full status as a shareholder until the date of the reorganization. This was not the situation in East Chilliwack.

**96** By way of summary, on the date of the reorganization McCutcheon and SYH had not ceased to be preferred shareholders of Central Capital. The rights attaching to their retractable preferred shares entitled them to continue to share in the profits of the company when these were declared as dividends, to vote at shareholders meetings to elect directors so long as dividends remained unpaid for a specified period of time, and, on a winding-up of the company, to participate in the distribution of assets that remained after the creditors were paid according to the ranking of the series of their shares. The company's obligation to redeem its shares was not absolute. Instead, the articles provided for what was realistically a "best efforts" buy-back based on solvency and continuation as a shareholder to the extent a buy-back could not take place. In East Chilliwack, because the farmer ceased to be a shareholder, the articles do not appear to make any provision for continued participation or for the postponement of payment depending on the solvency of the co-op.

(c) Evidence of a debtor-creditor relationship is lacking in the articles

**97** Looked at another way, after the retraction date and at the time of the reorganization, the common features of a debtor-creditor relationship are not in evidence in Central Capital's articles. The agreements between the parties contain no express provision that the redemption of the shares is in repayment of a loan. The corporation was not obliged to create any fund or debt instrument to ensure that it could redeem the shares on the retraction date. There is no indemnity in the event that the money is not repaid on the retraction date. There is no provision for the payment of any interest after the retraction date in the event that the money is not repaid on the retraction date. There is no provision that after the retraction date and in the event of insolvency, the appellants would have the right to have the company wound up. (See R. v. Imperial General Properties Ltd., [1985] 2 S.C.R. 288, 21 D.L.R. (4th) 741, for a case where the articles of the company contained this right.) There is

no provision that upon a winding-up or insolvency the parties are entitled to rank pari passu with the creditors as was the case in Canada Deposit Insurance Corp. v. Canadian Commercial Bank, supra.

(d) The effect of the reorganization

**98** Finlayson J.A. is of the view that it is immaterial that the articles provide, in the event of the liquidation, dissolution or winding-up of the company, that the appellants are only entitled to rank after the creditors but ahead of the junior ranking shareholders. In his view, this provision is irrelevant because we are not dealing with a liquidation but with a reorganization. He finds it significant that, like debtors, the preferred shareholders are not entitled to participate in any surplus once they have been paid. I am of the view that this provision in the articles is significant. It represents a clear indication that the holders of the retractable shares were not to be dealt with on the same footing as ordinary creditors even after the retraction date. Instead, they were to be dealt with as shareholders, albeit an elevated class. Under the CBCA all shares carry equal rights. Words used in the articles to differentiate a class of shares are nothing more than authorized deviations from this statutory position of equality: Welling, supra, at p. 683.

**99** The appellants submit that a winding-up or liquidation is not the same as a reorganization. This is true. Both, however, are methods of dealing with insolvency. Both are methods for secured creditors to enforce their claims by seizing the assets in which they hold security interests. If the value of the corporation as a going concern exceeds the liquidation value of the assets, it is in the interest of all the debt holders that the corporation be preserved as a going concern. The purpose of both a liquidation and a reorganization is to permit the rehabilitation of the insolvent person unfettered by debt: Vachon v. Canada Employment & Immigration Commission, [1985] 2 S.C.R. 417, 23 D.L.R. (4th) 641. By virtue of s. 20 of the CCAA, arrangements under the Act mesh with the reorganization provisions of the CBCA so as to affect the company's relations with its shareholders. Shareholders have no right to dissent to a reorganization: s. 191(7), CBCA. On a reorganization, among other things, the articles may be amended to alter or remove rights and privileges attaching to a class of shares and to create new classes of shares: s. 173, CBCA. These statutory provisions provide a clear indication that, on a reorganization, the interests of all shareholders, including shareholders with a right of redemption, are subordinated to the interests of the creditors. Where the debts exceed the assets of the company, a sound commercial result militates in favour of resolving this problem in a manner that allows creditors to obtain repayment of their debt in the manner which is most advantageous to them.

**100** The similarities between a liquidation and a reorganization, together with the express statement in the articles of Central Capital with respect to what is to happen on a winding-up, dictate that the interests of the holders of retractable shares, McCutcheon and SYH, are subordinated to the creditors and they are not entitled to claim under the CCAA equally with the creditors. This position is also consistent with the provisions of the Bankruptcy and Insolvency Act and the Winding-up Act. In the case of an insolvency where the debts to creditors clearly exceed the assets of the company, the policy of federal insolvency legislation appears to be clear that shareholders do not have the right to look to the assets of the corporation until the creditors have been paid.

Dividends

**101** Although dividends were payable on the shares of McCutcheon and SYH, no dividends were in fact declared. The appellants contend that the dividends, which have accrued but which

were not declared, are a debt or liability because they were stipulated to be part of the retraction price.

**102** Article 7 of Central Capital respecting McCutcheon's shares states that in the event of a liquidation, dissolution or winding-up of the corporation, the shareholders are entitled to receive not only the $25 per Series B preferred share, but "all accrued and unpaid dividends thereon, whether or not declared ... before any amount is paid by the Corporation or any assets of the Corporation are distributed to the holders of any shares ... ranking as to capital junior to the Series B Senior preferred Shares".

**103** It is trite law that a dividend may only be declared if a company is solvent. For corporations governed by the CBCA, it appears that the common law tests for solvency have all been subsumed or overruled: R. v. McClurg, [1990] 3 S.C.R. 1020 at pp. 1039-40, [1991] 2 W.W.R. 244 at pp. 259-60.

**104** Section 42 of the CBCA provides:

> 42. A corporation shall not declare or pay a dividend if there are reasonable grounds for believing that
>
> (a) the corporation is, or would after the payment be, unable to pay its liabilities as they become due; or
> (b) the realizable value of the corporation's assets would thereby be less than the aggregate of its liabilities and stated capital of all classes.

**105** Section 42 prevents the corporation from declaring or paying a dividend when it does not meet certain solvency requirements. There was no declaration of a dividend in the present case. Any obligation to pay a dividend as part of the retraction price cannot therefore be enforced when the company is insolvent. Dividends which have accrued but which are unpaid are not considered to be a debt because, on reading the articles as a whole, the provision for payment is not one which is made independent of the ability to pay: see Welling, supra, at p. 689, citing International Power Co. v. McMaster University, [1946] S.C.R. 178, [1946] 2 D.L.R. 81, where it was held there was no guarantee of payment and hence the accrued but unpaid dividends were not a debt. Instead, accrued but unpaid dividends are considered to be akin to a return of capital. Making these accrued dividends part of the retraction price does not alter this.

**106** By way of analogy to the treatment of dividends, it could be said that until the company has declared it will redeem the shares which are tendered to it the obligation to redeem them is not a debt or liability. The promise to pay in the articles of Central Capital is not made independent of any ability to pay.

**107** In the event that I am wrong in my conclusion that the true nature of the relationship is one of equity, I shall now consider the position in the event that a debt has been created.

> 3. If the nature of the relationship is not an equity relationship are the appellants entitled to be claimants under the CCAA?

**108** The parties agree that the effect of s. 36 renders the agreement to redeem their preferred shares unenforceable. It is the position of the appellants, however, that s. 36 does not extinguish

Central Capital's obligation to repay them. Their position is that Central Capital's obligation to repay them is a contingent liability and therefore gives them a claim provable in bankruptcy, bringing them under s. 12(1) of the CCAA.

The Meaning of Debt

**109** Debt is defined in a very broad manner in Black's Law Dictionary, 6th ed. (1990) at p. 403. It is the position of the appellants that this definition of "debt" is broad enough to include McCutcheon's right to have Central Capital redeem his shares. In the case of SYH, it is submitted that the right to redemption constitutes a future liability. It is the appellants' position that Feldman J. erred in holding that to have a provable claim, McCutcheon and Central Capital must be able to obtain a judgment against Central Capital for the retraction price and be entitled to seek payment on the judgment. Finlayson J.A. agrees with the appellant's position.

**110** Debt is defined in Black's Law Dictionary, supra, as:

> A sum of money due by certain and express agreement. A specified sum of money owing to one person from another, including not only obligation of debtor to pay but right of creditor to receive and enforce payment ...
>
> A fixed and certain obligation to pay money or some other valuable thing or things, either in the present or in the future. In a still more general sense, that which is due from one person to another, whether money, goods, or services. In a broad sense, any duty to respond to another in money, labor, or service; it may even mean a moral or honorary obligation, unenforceable by legal action. Also, sometimes an aggregate of separate debts, or the total sum of the existing claims against person or company. Thus we speak of the "national debt", the "bonded debt" of a corporation, etc.

**111** It will be readily apparent that in Black's the term "debt" is defined in two distinct ways. In order to constitute a debt as defined in the first paragraph, the obligation must be enforceable. In the second paragraph debt is defined more broadly as any duty or obligation even if unenforceable by legal action. Feldman J. considered the first portion of the definition in her reasons. If the first portion of the definition applies, no debt is created because the obligation is not enforceable under the CBCA. The appellants rely on the second portion of the definition. They also rely on the definition of the word "liability" in Black's which is also defined very broadly.

**112** In one sense, support for the position of the appellants is found in s. 40 of the CBCA. Section 40 states that a contract with a corporation providing for the purchase of shares of the corporation is specifically enforceable against the corporation except to the extent that the corporation cannot perform the contract without being in breach of ss. 34 or 35. Section 34 contains the solvency requirements concerning the redemption by a company of its own shares other than those carrying a right of redemption. Section 35 deals with shares which have been issued to settle or compromise a debt. In s. 2, "lability" is defined as including "a debt of a corporation arising under section 40".

**113** Section 40 does not include any reference to the obligation of a company to repurchase redeemable shares under s. 36. As a result s. 36 is not incorporated by reference into the definition of liability. While it might be suggested that this is a legislative oversight, the omission is also consistent with the position that only the articles of the corporation govern the relationships between

the company and the holders of the retractable shares under s. 36. I have already stated my opinion that the articles of Central Capital do not make the obligation to redeem the shares a debt or, for that matter, a liability. Moreover, even if a provision like s. 40 is implied with respect to redeemable preferred shares, it would also be necessary to imply a provision like s. 40(3) which states that in the event of liquidation where the company has not performed its contract to redeem, the other party is entitled to be ranked subordinate to the rights of creditors but in priority to the shareholders. This is a clear expression of legislative intention that on insolvency the claim of those entitled to have their shares redeemed should not be placed on the same footing with the claims of creditors but should rank subordinate to them: see Nelson v. Rentown Enterprises Inc., [1994] 4 W.W.R. 579, 16 Alta. L.R. (3d) 212 (C.A.), adopting the reasons of Hunt J. at 96 D.L.R. (4th) 586, 5 Alta. L.R. (3d) 149 (Q.B.). Policy reasons would again militate in favour of the result being the same on a reorganization.

Claims in Bankruptcy

**114** Even if the broader definitions of a debt or liability in Black's are adopted, the appellants still do not have a claim provable in bankruptcy.

**115** Persuasive authority already exists to the effect that in order to be a provable claim within the meaning of s. 121 of the Bankruptcy and Insolvency Act the claim must be one recoverable by legal process: Farm Credit Corp. v. Holowach (Trustee of), [1988] 5 W.W.R. 87 at p. 90, 51 D.L.R. (4th) 501 (Alta. C.A.), leave to appeal to the Supreme Court of Canada dismissed at [1989] 4 W.W.R. lxx.

**116** In Holowach, the seven members of the court were dealing with a situation in which some persons borrowed money from a mortgagee and mortgaged certain lands as security for repayment of the loan. The mortgagors then made an assignment in bankruptcy. The mortgagee filed a proof of claim for the full amount of the deficiency, that is, the amount of the indebtedness less the value of the land which the mortgagee was permitted to purchase. The Alberta Law of Property Act, R.S.A. 1980, c. L-8, precluded deficiency claims against individuals in foreclosure actions, although the effect of the legislation was not to extinguish or satisfy the debt. The mortgagee argued that it had a claim provable in bankruptcy under s. 95(1) of the Bankruptcy Act, R.S.O. 1970, c. B-3, now s. 121(1) of the Bankruptcy and Insolvency Act. The court rejected this argument, holding that a provable claim must be one recoverable by legal process. In coming to its conclusion, the court relied on Reference re Debt Adjustment Act, 1937, [1943] 1 All E.R. 240, [1943] 1 W.W.R. 378 (P.C.), and a number of decisions at the trial level which are collected at p. 91 of the decision.

**117** Here, the contract to repurchase the shares, while perfectly valid, is without effect to the extent that there is a conflict between the corporation's promise to redeem the shares and its statutory obligation under s. 36 of the CBCA not to reduce its capital where it is insolvent. As was the case in the Holowach decision, this statutory overlay renders Central Capital's promise to redeem the appellants' preferred shares unenforceable. Although there is a right to receive payment, the effect of the solvency provision of the CBCA means that there is no right to enforce payment. Inasmuch as there is no right to enforce payment, the promise is not one which can be proved as a claim.

**118** It could be suggested that the decision in Holowach can be distinguished from the instant case on the basis that in Holowach the claim is made unenforceable forever by statute whereas under the CCAA the claim is unenforceable only so long as the corporation does not meet the solven-

cy requirements of s. 36 of the CBCA. I do not believe this is a valid distinction for three reasons. First, the relevant date for determining any contingent liability is not the future but the past, namely, September 8, 1992, the date by which proofs of claim had to be submitted. On that date, Central Capital was insolvent. Second, it is only because the lenders were willing to convert their debt obligations into equity in the reorganization that Central Capital is now solvent. Central Capital is not the same company and its liabilities are not the same. The redeemable shares no longer exist. Third, in order to be profitable, the assets of a company must be managed. Any value in the assets after the insolvency of the company is, in this case, due to the new management and not to the preferred shareholders extending credit to the company by having their claim for redemption postponed.

**119** Even if Central Capital's obligation to redeem the shares of the appellants created a debt or liability, the appellants do not have a claim provable within the meaning of s. 121 of the Bankruptcy and Insolvency Act.

CONCLUSION

**120** I would dismiss the appeal. For the reasons I have given, the retraction amounts do not constitute a debt or liability within the meaning of s. 121 of the Bankruptcy and Insolvency Act. Even if I am wrong in my conclusion and a debt or liability is created, it is not a claim within the meaning of the CCAA. This is a case of first impression. For these reasons, I would not award any costs of this appeal.

**121** LASKIN J.A. (concurring): -- I have read the reasons of my colleagues Justice Finlayson and Justice Weiler. Like Justice Weiler, I would affirm the decision of the motions judge, Feldman J., and dismiss these appeals. I prefer, however, to state my own reasons for upholding the position of the unsecured creditors of Central Capital Corporation.

The Issue

**122** The application was argued before Madam Justice Feldman on an agreed statement of facts. My colleagues have summarized the relevant facts and important provisions of the documents. Each appellant holds preferred shares of Central Capital and each appellant's shares contain a right of retraction -- a right to require Central Capital to redeem the shares on a fixed date and for a fixed price. The retraction date for the appellants James McCutcheon and Central Guarantee Trust Company (collectively McCutcheon) was July 1, 1992, and before that date McCutcheon exercised his right of retraction and tendered his shares for redemption. The retraction date for the appellant SYH Corporation was September 1994 and although it could not tender its shares for redemption, it did file a proof of claim with the Administrator of Central Capital. The Administrator disallowed each appellant's claim and Feldman J. dismissed appeals from the Administrator's decisions.

**123** The issue on these appeals is whether McCutcheon and SYH Corporation "have claims provable against Central Capital Corporation within the meaning of the Bankruptcy Act (Canada) as amended as of the date of the Restated Subscription and Escrow Agreement". Under the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, s. 2, a claim provable "includes any claim or liability provable in proceedings under this Act by a creditor" and a creditor "means a person having a claim, preferred, secured or unsecured, provable as a claim under this Act". Section 121(1) of the Bankruptcy Act further defines claims provable as follows:

> 121(1) All debts and liabilities, present or future, to which the bankrupt is subject at the date of the bankruptcy or to which he may become subject before his discharge by reason of any obligation incurred before the date of the bankruptcy shall be deemed to be claims provable in proceedings under this Act.

**124** The date of the restated subscription and escrow agreement is May 1992.[1] at end of document.] By then, and indeed since December 1991, Central Capital had been insolvent and therefore was prohibited by s. 36(2) of the Canada Business Corporations Act, R.S.C. 1985, c. C-44, from making any payment to redeem the appellants' shares.

**125** On June 15, 1992, Houlden J. provided that Central Capital could be reorganized under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, and he stayed proceedings against it. Houlden J.'s order of July 9, 1992, which approved the restructuring of Central Capital, was made without prejudice to the right of the appellants to assert claims as creditors. Thus the question for this court is whether the appellants' retraction rights created debts of Central Capital in May 1992. In other words were McCutcheon and SYH Corporation creditors of Central Capital in May 1992? If they were creditors, then like the other unsecured creditors of Central Capital, they can elect to take shares in the newly incorporated company, Canadian Insurance Group Limited; if they were not creditors, then they remain shareholders of Central Capital under the restructuring plan.

**126** This is a question of characterization. I will address the question first, by considering the "substance" of the relationship between each appellant and the company; and second by considering s. 36(2) of the Canada Business Corporations Act, supra. In brief I conclude:

> (1) Although the relationship between each appellant and the company has characteristics of debt and equity, in substance both McCutcheon and SYH Corporation are shareholders, not creditors of Central Capital. Neither the existence of their retraction rights nor the exercise of those rights converts them into creditors;
> (2) Finding that the appellants were creditors of Central Capital would defeat the purpose of s. 36(2) of the statute.

I. The Relationship Between the Appellants and Central Capital

**127** Preferred shares have been called "compromise securities" and even "financial mongrels": Grover and Ross, Materials and Corporate Finance (1975), at p. 49. Invariably the conditions attaching to preferred shares contain attributes of equity and, at least in an economic sense, attributes of debt. Over the years financiers and corporate lawyers have blurred the distinction between equity and debt by endowing preferred shareholders with rights analogous to the rights of creditors. One example is the right of redemption -- the right of the corporation to compel preferred shareholders to sell their shares back to the corporation. Another example, and it is the case before us, is the right of retraction -- the right of shareholders to compel the corporation to buy back their shares on a specific date for a specific price.

**128** I acknowledge, therefore, that redeemable or retractable preferred shares are somewhat different from conventional equity capital. What makes the appeals before us difficult is that although the appellants appear to hold equity, their right of retraction appears to be a basic characteristic of a debtor-creditor relationship: see Grover and Ross, supra, at pp. 47-49; Buckley, Gillen and Yalden, Corporations: Principles and Policies, 3d ed. (1995), at pp. 938-40.

**129** If the certificate or instrument contains features of both equity and debt -- in other words if it is hybrid in character -- then the court must determine the "substance" of the relationship between the holder of the certificate and the company. This is the lesson of Justice Iacobucci's judgment in Canada Deposit Insurance Corp. v. Canadian Commercial Bank, [1992] 3 S.C.R. 558, 97 D.L.R. (4th) 385. In that case the Supreme Court of Canada had to determine whether the financial assistance given by several lending institutions to try to rescue the Canadian Commercial Bank was "in the nature of a loan" or "in the nature of a capital investment". Justice Iacobucci discussed his approach to the problem at pp. 590-91 of his judgment:

> As I see it, the fact that the transaction contains both debt and equity features does not, in itself, pose an insurmountable obstacle to characterizing the advance of $255 million. Instead of trying to pigeonhole the entire agreement between the Participants and CCB in one of two categories, I see nothing wrong in recognizing the arrangement for what it is, namely, one of a hybrid nature, combining elements of both debt and equity but which, in substance, reflects a debtor-creditor relationship. Financial and capital markets have been most creative in the variety of investments and securities that have been fashioned to meet the needs and interests of those who participate in those markets. It is not because an agreement has certain equity features that a court must either ignore these features as if they did not exist or characterize the transaction on the whole as an investment. There is an alternative. It is permissible, and often required, or desirable, for debt and equity to co-exist in a given financial transaction without altering the substance of the agreement. Furthermore, it does not follow that each and every aspect of such an agreement must be given the exact same weight when addressing a characterization issue. Again, it is not because there are equity features that it is necessarily an investment in capital. This is particularly true when, as here, the equity features are nothing more than supplementary to and not definitive of the essence of the transaction. When a court is searching for the substance of a particular transaction, it should not too easily be distracted by aspects which are, in reality, only incidental or secondary in nature to the main thrust of the agreement.

**130** In determining the substance of the relationship, as in any other case of contract interpretation, the court looks to what the parties intended. In CDIC v. CCB, supra, Iacobucci J. put this proposition as follows at p. 588:

> As in any case involving contractual interpretation, the characterization issue facing this Court must be decided by determining the intention of the parties to the support agreements. This task, perplexing as it sometimes proves to be, depends primarily on the meaning of the words chosen by the parties to reflect their intention. When the words alone are insufficient to reach a conclusion as to the true nature of the agreement, or when outside support for a particular characterization is required, a consideration of admissible surrounding circumstances may be appropriate.

**131** In these appeals what the parties intended is reflected mainly in the share purchase agreements and the conditions attaching to the appellants' shares, but also in the articles of incorporation and in the way Central Capital recorded the appellants' shares in its financial statements. These documents indicate that in substance the appellants are shareholders of Central Capital, not creditors. I rely on the following considerations to support my conclusion:

(i) Both appellants agreed to take preferred shares instead of some other instrument -- for example, a bond or debenture -- that would obviously have made them creditors. The appellant McCutcheon sold shares of one corporation (Canadian General Securities Limited) for cash and for shares of another corporation (Central Capital). Neither the share purchase agreements nor the share conditions support McCutcheon's contention that in taking preferred shares he was extending credit to Central Capital by deferring payment of the purchase price. He made an investment in the capital of Central Capital, no doubt because of the attractive dividend rate, the income tax advantages of preferred shares and "sweeteners" such as conversion privileges. Unlike Finlayson J.A., I place little weight on what he termed "the unique nature of the transaction". McCutcheon transferred assets to acquire his preferred shares rather than acquiring them with cash. But he nonetheless decided to invest in Central Capital and to take the risk and the profits (through dividends) of his investment.

Similarly, SYH Corporation exchanged its equity investment in four insurance companies for an equity investment in Central Capital. It too chose equity not debt. None of the contractual documents indicates that the appellants' retraction rights were intended to trigger an obligation on the part of Central Capital to repay a loan. Moreover, as Weiler J.A. points out, neither the share purchase agreements nor the share conditions provides for interest if Central Capital fails to honour its retraction obligations.

(ii) The senior preferred shares and junior preferred shares that the appellants own were part of the authorized capital of Central Capital before the appellants acquired them.

(iii) The appellants' shares were recorded in the financial statements of Central Capital as "capital stock", along with the company's issued and outstanding common shares, class "A" shares and warrants. The amount Central Capital might be obligated to pay the appellants if they exercised their retraction rights was not recorded as debt (even contingent debt) in the company's financial statements.

(iv) Both appellants had the right to receive dividends on their shares and McCutcheon had the right to vote his shares for the election of directors of Central Capital if dividends remained unpaid for a specified time. These rights -- to receive dividends and to vote -- are well recognized rights of shareholders. And these rights continue, even after the retraction dates, until the appellants' shares are redeemed.

(v) The preferred share conditions provide that on a liquidation, dissolution or winding-up, the holders rank with other shareholders and therefore, implicitly, behind creditors. The appellant McCutcheon, who holds senior preferred shares, would rank behind creditors but ahead of the holders of subordinate classes of shares; the appellant SYH Corporation, which holds junior preferred shares, would rank behind senior preferred shareholders but ahead of common shareholders.

**132** These provisions in the preferred share conditions also state that on payment of the amount owing to them the appellants "shall not be entitled to share in any further distribution of assets of the corporation". Finlayson J.A. interprets this to mean that the appellants "are not entitled to be treated as shareholders under a winding-up or liquidation but only as creditors". I disagree. These are typical preferred share provisions, which limit the recovery of the holders but do not treat them as creditors: Sutherland, Fraser and Stewart on Company Law of Canada, 6th ed. (1993), at p. 198. At least on a liquidation, dissolution or winding-up, the preferred share conditions evidence that the appellants would be treated not as creditors but as shareholders. In CDIC v. CCB, supra, Iacobucci J. placed considerable weight on a provision in the participation agreement stating that each participant "shall rank pari passu with the rights of the depositors". No such provision exists in this case. Indeed the share conditions I have referred to state the opposite.

**133** Of course, Central Capital was reorganized, not liquidated, dissolved or wound up and the preferred share conditions are silent about what occurs on a reorganization. Still these conditions shed light on what the parties intended on the reorganization. Section 12(1) of the Companies' Creditors Arrangement Act, supra, defines claim as "any indebtedness, liability or obligation of any kind that, if unsecured, would be a debt provable in bankruptcy within the meaning of the Bankruptcy Act". The question the court has been asked to answer is the same question that would arise on a liquidation. It is illogical to conclude that the appellants could claim only as shareholders on a liquidation and yet can claim as creditors on the reorganization. Whether Central Capital's financial difficulties led to a liquidation or a reorganization, the issue is the same and the analysis and the result should also be the same.

**134** The appellants argue, however, that they are shareholders only until they exercise their retraction rights but once they exercise these rights they become creditors. I do not agree with this argument. The share conditions provide that even after exercising their retraction rights, the appellants continue to be entitled to dividends and to vote until their shares are redeemed. In other words, they continue to enjoy the rights of shareholders. Moreover, if when the appellants exercised their retraction rights the company were insolvent and were to be subsequently liquidated (or dissolved or wound up), the appellants would rank as shareholders on the liquidation. And as I have indicated above the result should be no different on the reorganization.

**135** It seems to me that these appellants must be either shareholders or creditors. Except for declared dividends, they cannot be both. Once they are characterized as shareholders, their rights of retraction do not create a debtor-creditor relationship. These rights enable them to call for the repayment of their capital on a specific date (and at an agreed-upon price) provided the company is solvent. Ordinarily shareholders have to recoup their investment by selling their shares to third parties. If they have retraction rights, however, they can compel the company (if solvent) to repay their investment at a given time for a given price. But the right of retraction provides for the return of capital not for the repayment of a loan. Certainly the Canada Business Corporations Act treats a re-

demption of shares as a return of capital because s. 39 of the statute requires a company on a redemption to deduct from its stated capital account an amount equal to the value of the shares redeemed. The shares redeemed are then either cancelled or returned to the status of authorized but unissued shares.

**136** Putting it differently, a preferred shareholder exercising a right of retraction on the terms that exist here must rank behind the company's creditors. Grover and Ross make this point more generally in their Materials and Corporate Finance, supra, at pp. 48-49:

> On the other hand, the company cannot issue "secured" preferred shares in the sense that shares cannot have a right to a return of capital which is equal or superior to the rights of creditors. Preferred shareholders are risk-takers who are required to invest capital in the business and who can look only to what is left after creditors are fully provided for. Thus, in the absence of statutory authorization, the claims of shareholders cannot be secured by a lien on the corporate assets. They rank behind creditors but before common shareholders (if specified) on a voluntary or involuntary dissolution of the company.

**137** Admittedly there is little authority in Canada on the issue confronting this court. Some of the cases that the respondent relies on -- for example, Re Patricia Appliance Shops Ltd. (1922), 52 O.L.R. 215, [1923] 3 D.L.R. 1160 (S.C.), Laronge Realty Ltd. v. Golconda Investments Ltd. (1986), 63 C.B.R. (N.S.) 74, 7 B.C.L.R. (2d) 90 (C.A.), and even Re Meade, [1951] 2 All E.R. 168, [1951] Ch. 774 (D.C.) -- are of limited assistance because the shareholders in those cases did not have retraction rights.

**138** Perhaps the closest case -- and the appellants rely heavily on it -- is the judgment of the British Columbia Court of Appeal in Re East Chilliwack Agricultural Co-operative (1989), 74 C.B.R. (N.S.) 1, 58 D.L.R. (4th) 11. In that case a majority of the court (Craig J.A. dissenting) held that a withdrawing member of a co-operative association who elected to have his shares redeemed in instalments over a five-year period should be treated on the subsequent bankruptcy of the association as an ordinary creditor rather than as a shareholder. I decline to apply East Chilliwack for three reasons. First, because the case was decided in 1989, the British Columbia Court of Appeal did not have the benefit of the Supreme Court of Canada's reasons in CDIC v. CCB, supra. In East Chilliwack Hutcheon J.A., writing for the majority, did not focus on what the parties intended when the member contracted with the co- operative. Instead he only considered the relationship between the member and the co-operative after the member had withdrawn. I do not think his approach is consistent with Justice Iacobucci's judgment in CDIC v. CCB, supra.

**139** Second, there are important factual differences between East Chilliwack and the appeals before us. Justice Weiler has referred to these factual differences in her reasons. The most important of these differences are the following: in East Chilliwack the rules of the association provided that a member had to withdraw from the association to trigger the right of redemption, whereas the appellants' share conditions provide that they continue to be shareholders of Central Capital until their shares are redeemed; in East Chilliwack the member elected to withdraw and redeem his shares when the association was solvent whereas when the appellant McCutcheon exercised his right of retraction Central Capital was insolvent; and in East Chilliwack Hutcheon J.A. expressly stated that he was not considering the effect of the superintendent's power to suspend payments if the financial position of the co-operative was impaired, whereas the effect of the statutory prohibition against

Central Capital making payment, found in s. 36(2) of the Canada Business Corporations Act, is in issue in these appeals.

**140** Third, the decision in East Chilliwack is at odds with most of the American case-law and I favour the American approach. When a company repurchases shares by instalment and bankruptcy intervenes, the prevailing American position is that the shareholder's claim is deferred to the claims of ordinary creditors. The decision of the Fifth Circuit Court of Appeals in Robinson v. Wangemann, 75 F. 2d 756 (1935), is frequently cited. The facts of that case are virtually identical to the facts in East Chilliwack. A company had agreed to repurchase a stockholder's stock by instalments. Although the company was solvent when the agreement was made it went bankrupt before the repurchase was completed. The stockholder sought to prove as an ordinary creditor for the unpaid purchase price. Foster, Circuit Judge, writing for a unanimous court, rejected the stockholder's claim at p. 757:

> A transaction by which a corporation acquires its own stock from a stockholder for a sum of money is not really a sale. The corporation does not acquire anything of value equivalent to the depletion of its assets, if the stock is held in the treasury, as in this case. It is simply a method of distributing a proportion of the assets to the stockholder. The assets of a corporation are the common pledge of its creditors, and stockholders are not entitled to receive any part of them unless creditors are paid in full. When such a transaction is had, regardless of the good faith of the parties, it is essential to its validity that there be sufficient surplus to retire the stock, without prejudice to creditors, at the time payment is made out of assets.

**141** At the heart of Robinson v. Wangemann is the finding that the selling stockholder is not a creditor in the sense of a person who loans money to a corporation, and therefore is not entitled to parity with the general creditors. The principle in Robinson v. Wangemann seeks to protect creditors by refusing to permit selling stockholders, who were risk investors, to withdraw their capital on the same terms as general creditors in the event of insolvency. Section 40(3) of the Canada Business Corporations Act -- a section to which I shall return when considering s. 36(2) of the same statute -- codifies the principle in Robinson v. Wangemann for share repurchases, though not for share redemptions. See also Blumberg, The Law of Corporate Groups (1987), at pp. 205-10 and see contra Wolff v. Heidritter Lumber Co., 163 A. 140 (N.J.Ch., 1932).

**142** Quite apart from the instalment purchase price cases, American courts have often grappled with the question whether preferred stockholders can claim as creditors of the corporation. Although there are cases going both ways, most appear to come to the same conclusion as I do. The American cases are collected in Bjor and Solheim, Fletcher Cyclopedia of the Law of Private Corporations (1995), revised, vol. 11, and in Bjor and Reinholtz, Fletcher Cyclopedia of the Law of Private Corporations (1990), revised, vol. 15A. In volume 11 the authors of the text indicate -- as did the Supreme Court of Canada in CDIC v. CCB -- that "[w]hether or not the holder of a particular instrument or certificate is to be regarded as a shareholder or a creditor is a question of interpretation, and depends on the terms of the contract as evidenced by the instrument, the articles of incorporation, and the statutes of the state. The nature of the transaction is to be determined by the real substance and effect of the contract rather than by the name given to the obligations or its form" (at p. 566).

**143** And in volume 15A the authors state at pp. 290 and 292 that even the arrival of a fixed redemption date does not change a preferred stockholder into a creditor:

> Holders of preferred stock of a corporation, in the absence of express provision to the contrary, are stockholders and not creditors of the corporation, except for dividends declared. They have no lien upon, and are not entitled to, any of the assets of the corporation when it becomes insolvent, until all debts are paid. Furthermore, there is authority that the status of a preferred stockholder is not changed to that of creditor, even though a dividend is guaranteed. Indeed it is beyond the power of a corporation to issue a class of stock, the holders of which are entitled to preference over general creditors.
>
> ...
>
> Even where preferred stock has a fixed redemption date, arrival of that date does not change the status of a preferred stockholder to that of a creditor.

**144** I agree with these statements. I therefore conclude first that the appellants, in substance, were shareholders of Central Capital, not creditors; and second that neither the existence nor the exercise of their retraction rights turned them into creditors.

II. Provable Claims and Section 36(2) of the Canada Business Corporations Act

**145** In May 1992 Central Capital was insolvent. It was unable to pay its liabilities as they became due and the realizable value of its assets was less than the aggregate of its liabilities. Because it was insolvent it was prohibited by s. 36(2) of the Canada Business Corporations Act from redeeming the appellants' shares. Section 36(2) of the statute provides:

> 36(2) A corporation shall not make any payment to purchase or redeem any redeemable shares issued by it if there are reasonable grounds for believing that
>
> (a) the corporation is, or would after the payment be, unable to pay its liabilities as they become due; or
> (b) the realizable value of the corporation's assets would after the payment be less than the aggregate of
>
> (i) its liabilities, and
> (ii) the amount that would be required to pay the holders of shares that have a right to be paid, on a redemption or in a liquidation, rateably with or prior to the holders of the shares to be purchased or redeemed.

**146** As well, the appellants' share conditions provide that they are not permitted to redeem their shares if to do so would be "contrary to applicable law", in this case s. 36(2) of the statute.

**147** To hold that the appellants have provable claims would defeat the purpose of s. 36(2) of the Canada Business Corporations Act. At common law a company could not repurchase its own

shares on the open market or in the language of Trevor v. Whitworth (1887), 12 App. Cas. 409, [1886-90] All E.R. Rep. 46 (H.L.), a company could not "traffick in its own shares". The obvious reason was to prevent companies from using their assets to destroy the claims of their creditors. Modern corporate statutes, such as the Canada Business Corporations Act, modified the rule in Trevor v. Whitworth to permit repurchases provided the company's creditors would not be prejudiced. Thus the legislation insisted that the company could not repurchase its own shares unless it satisfied stated solvency tests. And so, s. 34(2) of the Canada Business Corporations Act provides:

> 34(2) A corporation shall not make any payment to purchase or otherwise acquire shares issued by it if there are reasonable grounds for believing that
>
> (a) the corporation is, or would after the payment be, unable to pay its liabilities as they become due; or
> (b) the realizable value of the corporation's assets would after the payment be less than the aggregate of its liabilities and stated capital of all classes.

**148** In Nelson v. Rentown Enterprises Inc. (1993), 96 D.L.R. (4th) 586 at p. 589, 5 Alta. L.R. (3d) 149, affirmed (1994), 109 D.L.R. (4th) 608n, 16 Alta. L.R. (3d) 212 (C.A.), Hunt J. of the Alberta Queen's Bench wrote:

> The policy behind the s. 34(2) limitation upon a corporation's power to purchase its own shares seems obvious. It is intended to ensure that one or more shareholders in a corporation do not recoup their investments to the detriment of creditors and other shareholders. It has been observed that:
>
> > Corporate power to purchase its own stock has been frequently abused. Done by corporations conducting faltering businesses, it has been employed to create preferences to the detriment of creditors and of the other stockholders.
> >
> > (Mountain State Steel Foundries, Inc. v. C.I.R., supra, at p. 741 [284 F.2d 737 (1960)].)
>
> Modern business statutes permit these share purchases to take place provided that the position of creditors and other shareholders is protected, by virtue of the application of the s. 34(2) tests.

**149** Redemptions of preferred shares, unlike repurchases, were always permitted at common law as long as they were not made in contemplation of bankruptcy. But the solvency test in s. 36(2) of the Canada Business Corporations Act has the same purpose as the solvency test in s. 34(2): to prevent redemptions if they would allow the company to prejudice the claims of creditors. See Buckley et al., Corporations: Principles and Policies, supra, at pp. 968-71. To hold that the appellants' retraction rights gave rise to provable claims in the face of s. 36(2), thereby allowing the appellants to rank equally with the unsecured creditors, would undermine the purpose of the section. If a claim in a bankruptcy or reorganization proceeding is unenforceable under the statute, the claim is not entitled to recognition on a parity with the claims of unsecured creditors: see Blumberg, supra,

at pp. 205-06; and Farm Credit Corp. v. Holowach (Trustee of) (1988), 68 C.B.R. (N.S.) 255, 51 D.L.R. (4th) 501 (Alta. C.A.).

**150** I draw comfort in this conclusion from s. 40 of the Canada Business Corporations Act. Section 40(1) provides that a contract with a corporation for the purchase of its shares is specifically enforceable against the corporation "except to the extent that the corporation cannot perform the contract without thereby being in breach of s. 34". Section 40(3) then states:

> 40(3) Until the corporation has fully performed a contract referred to in subsection (1), the other party retains the status of a claimant entitled to be paid as soon as the corporation is lawfully able to do so or, in a liquidation, to be ranked subordinate to the rights of creditors but in priority to the shareholders.

**151** In other words, the section recognizes that if a company contracts to repurchase its shares but is prohibited from doing so because it is insolvent, the vendor of the shares is not a creditor and on a liquidation ranks subordinate to the rights of creditors. The shareholder cannot be repaid at the expense of the company's creditors. Although s. 40 does not expressly apply to s. 36, I think that the rationale for s. 40(3) applies to redemptions as well as to repurchases. Whether a repurchase or a redemption, the shareholder is not a creditor and is subordinate to the rights of creditors. More simply the shareholder does not have a provable claim.

**152** The appellants rely on The Custodian v. Blucher, [1927] S.C.R. 420, [1927] 3 D.L.R. 40, but in my view this case does not assist them. In Blucher dividends were declared on stock but payment of the dividends was suspended during World War I. The Supreme Court of Canada held at p. 425 S.C.R., p. 43 D.L.R. that "[t]he right of recovery was in suspense during the war; but the debt nevertheless existed". In that case, however, the dividend was declared before the suspension of payment took place. Moreover, as Justice Finlayson points out in his reasons, courts have always accepted the proposition that when a dividend is declared it is a debt on which each shareholder can sue the corporation.

**153** Holding that the appellants do not have provable claims accords with sound corporate policy. On the insolvency of a company the claims of creditors have always ranked ahead of the claims of shareholders for the return of their capital. Case-law and statute law protect creditors by preventing companies from using their funds to prejudice creditors' chances of repayment. Creditors rely on these protections in making loans to companies. Permitting preferred shareholders to be turned into creditors by endowing their shares with retraction rights runs contrary to this policy of creditor protection.

**154** I would dismiss these appeals. I would not make any cost order. I am grateful to all counsel for their assistance on this interesting and difficult problem.

Order accordingly.

* * * * *

Note 1: There is a discrepancy in the materials before this court on the relevant date for establishing a claim provable against Central Capital: SYH Corporation used May 1992, the date of the

restated subscription and escrow agreement whereas McCutcheon and the unsecured creditors of Central Capital Corporation used June 15, 1992, the date of the court-ordered stay of proceedings against Central Capital. I have used the May 1992 date but nothing turns on the use of this date as opposed to the June 15, 1992 date.

qp/e/qlgxc/qlbxr

# Tab 8

*Case Name:*

# Nelson Financial Group Ltd. (Re)

**IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, C-36, as amended**
**AND IN THE MATTER OF a Plan of Compromise or Arrangement of Nelson Financial Group Ltd.**

[2010] O.J. No. 4903

2010 ONSC 6229

75 B.L.R. (4th) 302

71 C.B.R. (5th) 153

2010 CarswellOnt 8655

Court File No. 10-8630-00CL

Ontario Superior Court of Justice
Commercial List

**S.E. Pepall J.**

November 16, 2010.

(36 paras.)

*Bankruptcy and insolvency law -- Companies' Creditors' Arrangement Act (CCAA) -- Compromises and arrangements -- Claims -- Priority -- Motion by the holders of promissory notes from the debtor company for an order that all claims and potential claims of the preferred shareholders against the company be classified as equity claims within the meaning of the Companies' Creditors Arrangement Act allowed -- Claims of preferred shareholders for unpaid dividends, redemption, compensatory damages and rescission fell within s. 2 of the Companies' Creditors Arrangement Act and were thus equity claims.*

Motion by the holders of promissory notes from the debtor company for an order that all claims and potential claims of the preferred shareholders against the company be classified as equity claims within the meaning of the Companies' Creditors Arrangement Act. The company raised money from

investors and then used those funds to extend credit to customers in vendor assisted financing programmes. It issued promissory notes or preference shares to the investors. The preferred shareholders were entered on the share register and received share certificates. They were treated as equity in the company's financial statements. The claims of the preferred shareholders against the company were for declared but unpaid dividends, unperformed requests for redemption, compensatory damages for negligent or fraudulent misrepresentation and payment of the amounts due upon the rescission or annulment of the purchase or subscription for preferred shares.

HELD: Motion allowed. The preferred shareholders were shareholders of the company, not creditors. The substance of the arrangement between the preferred shareholders and the company was a relationship based on equity and not debt. The claims of the preferred shareholder in the present case did not constitute a claim provable for the purposes of the Companies' Creditors Arrangement Act. The language of s. 2 of the Act was clear and unambiguous and equity claims included a claim in respect of an equity interest and a claim for a dividend or similar payment and a claim for rescission. This encompassed the claims of all of the preferred shareholders.

**Statutes, Regulations and Rules Cited:**

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, s. 2, s. 121(1)

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 2, s. 6(8), s. 22.1

**Counsel:**

Richard B. Jones and Douglas Turner, Q.C., Representative Counsel for Noteholders/Moving Party.

J.H. Grout and S. Aggarwal, for the Monitor.

Pamela Foy, for the Ontario Securities Commission.

Frank Lamie, for Nelson Financial Group Ltd.

Robert Benjamin Mills and Harold Van Winssen for Clifford Styles, Jackie Styles and Play Investments Ltd., Respondents.

Michael Beardsley, Self Represented Respondent.

Clifford Holland, Self Represented Respondent.

Arnold Bolliger, Self Represented Respondent.

John McVey, Self Represented Respondent.

Joan Frederick, Self Represented Respondent.

Rakesh Sharma, Self Represented Respondent.

Larry Debono, Self Represented Respondent.

Keith McClear, Self Represented Respondent.

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## REASONS FOR DECISION

1 **S.E. PEPALL J.**:-- This motion addresses the legal characterization of claims of holders of preferred shares in the capital stock of the applicant, Nelson Financial Group Ltd. ("Nelson"). The issue before me is to determine whether such claims constitute equity claims for the purposes of sections 6(8) and 22.1 of the *Companies' Creditors Arrangement Act* ("*CCAA*").

Background Facts

2 Nelson was incorporated pursuant to the *Business Corporations Act* of Ontario in September, 1990. Nelson raised money from investors and then used those funds to extend credit to customers in vendor assisted financing programmes. It raised money in two ways. It issued promissory notes bearing a rate of return of 12% per annum and also issued preference shares typically with an annual dividend of 10%.[1] The funds were then lent out at significantly higher rates of interest.

3 The Monitor reported that Nelson placed ads in selected publications. The ads outlined the nature of the various investment options. Term sheets for the promissory notes or the preferred shares were then provided to the investors by Nelson together with an outline of the proposed tax treatment for the investment. No funds have been raised from investors since January 29, 2010.

(a) Noteholders

4 As of the date of the *CCAA* filing on March 23, 2010, Nelson had issued 685 promissory notes in the aggregate principal amount of $36,583,422.89. The notes are held by approximately 321 people.

(b) Preferred Shareholders

5 Nelson was authorized to issue two classes of common shares and 2,800,000 Series A preferred shares and 2,000,000 Series B preferred shares, each with a stated capital of $25.00. The president and sole director of Nelson, Marc Boutet, is the owner of all of the issued and outstanding common shares. By July 31, 2007, Nelson had issued to investors 176,675 Series A preferred shares for an aggregate consideration of $4,416,925. During the subsequent fiscal year ended July 31, 2008, Nelson issued a further 172,545 Series A preferred shares and 27,080 Series B preferred shares. These shares were issued for an aggregate consideration of $4,672,383 net of share issue costs.

6 The preferred shares are non-voting and take priority over the common shares. The company's articles of amendment provide that the preferred shareholders are entitled to receive fixed preferential cumulative cash dividends at the rate of 10% per annum. Nelson had the unilateral right to redeem the shares on payment of the purchase price plus accrued dividends. At least one investor negotiated a right of redemption. Two redemption requests were outstanding as of the *CCAA* filing date.

7 As of the *CCAA* filing date of March 23, 2010, Nelson had issued and outstanding 585,916.6 Series A and Series B preferred shares with an aggregate stated capital of $14,647,914. The preferred shares are held by approximately 82 people. As of the date of filing of these *CCAA* proceedings, there were approximately $53,632 of declared but unpaid dividends outstanding with respect to the preferred shares and $73,652.51 of accumulated dividends.

8 Investors subscribing for preferred shares entered into subscription agreements described as term sheets. These were executed by the investor and by Nelson. Nelson issued share certificates to

the investors and maintained a share register recording the name of each preferred shareholder and the number of shares held by each shareholder.

**9** As reported by the Monitor, notwithstanding that Nelson issued two different series of preferred shares, the principal terms of the term sheets signed by the investors were almost identical and generally provided as follows:

- the issuer was Nelson;
- the par value was fixed at $25.00;
- the purpose was to finance Nelson's business operations;
- the dividend was 10% per annum, payable monthly, commencing one month after the investment was made;
- preferred shareholders were eligible for a dividend tax credit;
- Nelson issued annual T-3 slips on account of dividend income to the preferred shareholders;
- the preferred shares were non-voting (except where voting as a class was required), redeemable at the option of Nelson and ranked ahead of common shares; and
- dividends were cumulative and no dividends were to be paid on common shares if preferred share dividends were in arrears.

**10** In addition, the Series B term sheet provided that the monthly dividend could be reinvested pursuant to a Dividend Reinvestment Plan ("DRIP").

**11** The preferred shareholders were entered on the share register and received share certificates. They were treated as equity in the company's financial statements. Dividends were received by the preferred shareholders and they took the benefit of the advantageous tax treatment.

(c) Insolvency

**12** Mr. Boutet knew that Nelson was insolvent since at least its financial year ended July 31, 2007. Nelson did not provide financial statements to any of the preferred shareholders prior to, or subsequent to, the making of the investment.

(d) Ontario Securities Commission

**13** On May 12, 2010, the Ontario Securities Commission ("OSC") issued a Notice of Hearing and Statement of Allegations alleging that Nelson and its affiliate, Nelson Investment Group Ltd., and various officers and directors of those corporations committed breaches of the *Ontario Securities Act* in the course of selling preferred shares. The allegations include non-compliance with the prospectus requirements, the sale of shares in reliance upon exemptions that were inapplicable, the sale of shares to persons who were not accredited investors, and fraudulent and negligent misrepresentations made in the course of the sale of shares. The OSC hearing has been scheduled for the end of February, 2011.

(e) Legal Opinion

**14** Based on the Monitor's review, the preferred shareholders were documented as equity on Nelson's books and records and financial statements. Pursuant to court order, the Monitor retained

Stikeman Elliott LLP as independent counsel to provide an opinion on the characterization of the claims and potential claims of the preferred shareholders. The opinion concluded that the claims were equity claims. The Monitor posted the opinion on its website and also advised the preferred shareholders of the opinion and conclusions by letter. The opinion was not to constitute evidence, issue estoppel or res judicata with respect to any matters of fact or law referred to therein. The opinion, at least in part, informed Nelson's position which was supported by the Monitor, that independent counsel for the preferred shareholders was unwarranted in the circumstances.

(f) Development of Plan

**15** The Monitor reported in its Eighth Report that a plan is in the process of being developed and that preferred shareholders would have their existing preference shares cancelled and would then be able to claim a tax loss on their investment or be given a new form of preference shares with rights to be determined.

Motion

**16** The holders of promissory notes are represented by Representative Counsel appointed pursuant to my order of June 15, 2010. Representative Counsel wishes to have some clarity as to the characterization of the preferred shareholders' claims. Accordingly, Representative Counsel has brought a motion for an order that all claims and potential claims of the preferred shareholders against Nelson be classified as equity claims within the meaning of the *CCAA*. In addition, Representative Counsel requests that the unsecured creditors, which include the noteholders, be entitled to be paid in full before any claim of a preferred shareholder and that the preferred shareholders form a separate class that is not entitled to vote at any meeting of creditors. Nelson and the Monitor support the position of Representative Counsel. The OSC is unopposed.

**17** On the return of the motion, some preferred shareholders were represented by counsel from Templeman Menninga LLP and some were self-represented. It was agreed that the letters and affidavits of preferred shareholders that were filed with the court would constitute their evidence. Oral submissions were made by legal counsel and by approximately eight individuals. They had many complaints. Their allegations against Nelson and Mr. Boutet range from theft, fraud, misrepresentation including promises that their funds would be secured, operation of a Ponzi scheme, breach of trust, dividend payments to some that exceeded the rate set forth in Nelson's articles, conversion of notes into preferred shares at a time when Nelson was insolvent, non-disclosure, absence of a prospectus or offering memorandum disclosure, oppression, violation of section 23(3) of the *OBCA* and of the *Securities Act* such that the issuance of the preferred shares was a nullity, and breach of fiduciary duties.

**18** The stories described by the investors are most unfortunate. Many are seniors and pensioners who have invested their savings with Nelson. Some investors had notes that were rolled over and replaced with preference shares. Mr. McVey alleges that he made an original promissory note investment which was then converted arbitrarily and without his knowledge into preference shares. He alleges that the documents effecting the conversion did not contain his authentic signature.

**19** Mr. Styles states that he and his company invested approximately $4.5 million in Nelson. He states that Mr. Boutet persuaded him to convert his promissory notes into preference shares by promising a 13.75% dividend rate, assuring him that the obligation of Nelson to repay would be treated the same or better than the promissory notes, and that they would have the same or a priority

position to the promissory notes. He then received dividends at the 13.75% rate contrary to the 10% rate found in the company's articles. In addition, at the time of the conversion, Nelson was insolvent.

**20** In brief, Mr. Styles submits that:

(a) the investment transactions were void because there was no prospectus contrary to the provisions of the *Securities Act* and the Styles were not accredited investors; the preferred shares were issued contrary to section 23(3) of the *OBCA* in that Nelson was insolvent at the relevant time and as such, the issuance was a nullity; and the conduct of the company and its principal was oppressive contrary to section 248 of the *OBCA*; and that

(b) the Styles' claim is in respect of an undisputed agreement relating to the conversion of their promissory notes into preferred shares which agreement is enforceable separate and apart from any claim relating to the preferred shares.

The Issue

**21** Are any of the claims advanced by the preferred shareholders equity claims within section 2 of the *CCAA* such that they are to be placed in a separate class and are subordinated to the full recovery of all other creditors?

The Law

**22** The relevant provisions of the *CCAA* are as follows.

Section 2 of the *CCAA* states:

> In this Act,
>
> "Claim" means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the *Bankruptcy and Insolvency Act*;
>
> "Equity Claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
> (b) a return of capital,
> (c) a redemption or retraction obligation,
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (*a*) to (*d*);"
>
> "Equity Interest" means

(a) in the case of a corporation other than an income trust, a share in the corporation -- or a warrant or option or another right to acquire a share in the corporation -- other than one that is derived from a convertible debt, and

(b) in the case of an income trust, a unit in the income trust -- or a warrant or option or another right to acquire a unit in the income trust -- other than one that is derived from a convertible debt;

Section 6(8) states:

> No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

Section 22.1 states:

> Despite subsection 22(1) creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise.

**23** Section 2 of the *Bankruptcy and Insolvency Act* ("*BIA*") which is referenced in section 2 of the *CCAA* provides that a claim provable includes any claim or liability provable in proceedings under the Act by a creditor. Creditor is then defined as a person having a claim provable as a claim under the Act.

**24** Section 121(1) of the *BIA* describes claims provable. It states:

> All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

**25** Historically, the claims and rights of shareholders were not treated as provable claims and ranked after creditors of an insolvent corporation in a liquidation. As noted by Laskin J.A. in *Re Central Capital Corporation*[2], on the insolvency of a company, the claims of creditors have always ranked ahead of the claims of shareholders for the return of their capital. This principle is premised on the notion that shareholders are understood to be higher risk participants who have chosen to tie their investment to the fortunes of the corporation. In contrast, creditors choose a lower level of exposure, the assumption being that they will rank ahead of shareholders in an insolvency. Put differently, amongst other things, equity investors bear the risk relating to the integrity and character of management.

**26** This treatment also has been held to encompass fraudulent misrepresentation claims advanced by a shareholder seeking to recover his investment: *Re Blue Range Resource Corp.*[3] In that case, Romaine J. held that the alleged loss derived from and was inextricably intertwined with the shareholder interest. Similarly, in the United States, the Second Circuit Court of Appeal in *Re Stirling Homex Corp.*[4] concluded that shareholders, including those who had allegedly been defrauded, were subordinate to the general creditors when the company was insolvent. The Court stated that

"the real party against which [the shareholders] are seeking relief is the body of general creditors of their corporation. Whatever relief may be granted to them in this case will reduce the percentage which the general creditors will ultimately realize upon their claims." *National Bank of Canada v. Merit Energy Ltd.*[5] and *Earthfirst Canada Inc.*[6] both treated claims relating to agreements that were collateral to equity claims as equity claims. These cases dealt with separate indemnification agreements and the issuance of flow through shares. The separate agreements and the ensuing claims were treated as part of one integrated transaction in respect of an equity interest. The case law has also recognized the complications and delay that would ensue if *CCAA* proceedings were mired in shareholder claims.

**27** The amendments to the *CCAA* came into force on September 18, 2009. It is clear that the amendments incorporated the historical treatment of equity claims. The language of section 2 is clear and broad. Equity claim means a claim in respect of an equity interest and includes, amongst other things, a claim for rescission of a purchase or sale of an equity interest. Pursuant to sections 6(8) and 22.1, equity claims are rendered subordinate to those of creditors.

**28** The Nelson filing took place after the amendments and therefore the new provisions apply to this case. Therefore, if the claims of the preferred shareholders are properly characterized as equity claims, the relief requested by Representative Counsel in his notice of motion should be granted.

**29** Guidance on the appropriate approach to the issue of characterization was provided by the Ontario Court of Appeal in *Re Central Capital Corporation*[7]. Central Capital was insolvent and sought protection pursuant to the provisions of the *CCAA*. The appellants held preferred shares of Central Capital. The shares each contained a right of retraction, that is, a right to require Central Capital to redeem the shares on a fixed date and for a fixed price. One shareholder exercised his right of retraction and the other shareholder did not but both filed proofs of claim in the *CCAA* proceedings. In considering whether the two shareholders had provable debt claims, Laskin J.A. considered the substance of the relationship between the company and the shareholders. If the governing instrument contained features of both debt and equity, that is, it was hybrid in character, the court must determine the substance of the relationship between the company and the holder of the certificate. The Court examined the parties' intentions.

**30** In *Central Capital*, Laskin J.A. looked to the share purchase agreements, the conditions attaching to the shares, the articles of incorporation and the treatment given to the shares in the company's financial statements to ascertain the parties' intentions and determined that the claims were equity and not debt claims.

**31** In this case, there are characteristics that are suggestive of a debt claim and of an equity claim. That said, in my view, the preferred shareholders are, as their description implies, shareholders of Nelson and not creditors. In this regard, I note the following.

(a) Investors were given the option of investing in promissory notes or preference shares and opted to invest in shares. Had they taken promissory notes, they obviously would have been creditors. The preference shares carried many attractions including income tax advantages.

(b) The investors had the right to receive dividends, a well recognized right of a shareholder.

(c) The preference share conditions provided that on a liquidation, dissolution or winding up, the preferred shareholders ranked ahead of common share-

holders. As in *Central Capital*, it is implicit that they therefore would rank behind creditors.

(d) Although I acknowledge that the preferred shareholders did not receive copies of the financial statements, nonetheless, the shares were treated as equity in Nelson's financial statements and in its books and records.

**32** The substance of the arrangement between the preferred shareholders and Nelson was a relationship based on equity and not debt. Having said that, as I observed in *I. Waxman & Sons.*[8], there is support in the case law for the proposition that equity may become debt. For instance, in that case, I held that a judgment obtained at the suit of a shareholder constituted debt. An analysis of the nature of the claims is therefore required. If the claims fall within the parameters of section 2 of the *CCAA*, clearly they are to be treated as equity claims and not as debt claims.

**33** In this case, in essence the claims of the preferred shareholders are for one or a combination of the following:

(a) declared but unpaid dividends;
(b) unperformed requests for redemption;
(c) compensatory damages for the loss resulting in the purchased preferred shares now being worthless and claimed to have been caused by the negligent or fraudulent misrepresentation of Nelson or of persons for whom Nelson is legally responsible; and
(d) payment of the amounts due upon the rescission or annulment of the purchase or subscription for preferred shares.

**34** In my view, all of these claims fall within the ambit of section 2, are governed by sections 6(8) and 22.1 of the *CCAA,* and therefore do not constitute a claim provable for the purposes of the statute. The language of section 2 is clear and unambiguous and equity claims include "a claim that is in respect of an equity interest" and a claim for a dividend or similar payment and a claim for rescission. This encompasses the claims of all of the preferred shareholders including the Styles whose claim largely amounts to a request for rescission or is in respect of an equity interest. The case of *National Bank of Canada v. Merit Energy Ltd.*[9] is applicable in regard to the latter. In substance, the Styles' claim is for an equity obligation. At a minimum, it is a claim in respect of an equity interest as described in section 2 of the CCAA. Parliament's intention is clear and the types of claims advanced in this case by the preferred shareholders are captured by the language of the amended statute. While some, and most notably Professor Janis Sarra[10], advocated a statutory amendment that provided for some judicial flexibility in cases involving damages arising from egregious conduct on the part of a debtor corporation and its officers, Parliament opted not to include such a provision. Sections 6(8) and 22.1 allow for little if any flexibility. That said, they do provide for greater certainty in the appropriate treatment to be accorded equity claims.

**35** There are two possible exceptions. Mr. McVey claims that his promissory note should never have been converted into preference shares, the conversion was unauthorized and that the signatures on the term sheets are not his own. If Mr. McVey's evidence is accepted, his claim would be qua creditor and not preferred shareholder. Secondly, it is possible that monthly dividends that may have been lent to Nelson by Larry Debono constitute debt claims. The factual record on these two possible exceptions is incomplete. The Monitor is to investigate both scenarios, consider a resolution of same, and report back to the court on notice to any affected parties.

**36** Additionally, the claims procedure will have to be amended. The Monitor should consider an appropriate approach and make a recommendation to the court to accommodate the needs of the stakeholders. The relief requested in the notice of motion is therefore granted subject to the two aforesaid possible exceptions.

S.E. PEPALL J.

cp/e/qlafr/qlvxw/qlana

1 The Monitor is aware of six preferred shareholders with dividends that ranged from 10.5% to 13.75% per annum.

2 (1996), 38 C.B.R. (3d) 1 (Ont. C.A.).

3 (2000), 15 C.B.R. (4th) 169.

4 (1978) 579 F. 2d 206 (2nd Cir. Ct. of App.).

5 [2001] A.J. No. 918, (2001), 2001 CarswellAlta 913, aff'd [2002] A.J. no. 6, 2002 CarswellAlta 23 (Alta C.A.).

6 [2009] A.J. No. 749, (2009) 2009 CarswellAlta 1069.

7 Supra, note 2.

8 [2008] O.J. No. 885, (2008), 2008 CarswellOnt 1245.

9 Supra, note 5.

10 "From Subordination to Parity: An International Comparison of Equity Securities Law Claims in Insolvency Proceedings" (2007) 16 Int. Insolv. Re., 181.

# Tab 9

*Case Name:*

# Earthfirst Canada 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 Plan of Compromise or Arrangement of Earthfirst Canada Inc.**

[2009] A.J. No. 749

2009 ABQB 316

56 C.B.R. (5th) 102

2009 CarswellAlta 1069

Docket: 0801 13559

Registry: Calgary

Alberta Court of Queen's Bench
Judicial District of Calgary

**B.E.C. Romaine J.**

Heard: May 13, 2009.
Judgment: May 27, 2009.

(5 paras.)

**Counsel:**

Kelly J. Bourassa and Scott Kurie, for Indemnity Claimants of Earthfirst Canada Inc.

Howard A. Gorman, for Earthfirst Canada Inc.

A. Robert Anderson, Q.C. and Eric D. Stearns, for the Monitor, Ernst & Young Inc.

[Editor's note: A corrigendum was released by the Court on July 8, 2009; the corrections have been made to the text and the corrigendum is appended to this document.]

## Reasons for Judgment

B.E.C. ROMAINE J.:--

## INTRODUCTION

**1** Earthfirst Canada Inc. seeks a declaration as the proper characterization of potential claims of holders of its flow-through common shares for the purpose of a proposed plan of arrangement under the *Companies' Creditors Arrangement Act,* R.S.C. 1985, c. C-36, as amended. The issue is whether contingent claims that the flow-through subscribers may have are, at their core, equity obligations rather than debt or creditor obligations and, as such, necessarily rank behind claims made by the creditors of Earthfirst. I decided that the potential claims are in substance equity obligations and these are my reasons.

## FACTS

**2** The flow-through shares at issue were distributed in December, 2007 as part of an initial public offering of common shares and flow-through shares. The common shares plus one-half of a warrant were offered at a price of $2.25 per unit. The flow-through shares were offered at a price of $2.60 per share. Investors who wished to purchase flow-through shares were required to execute a subscription agreement which included the following covenants of Earthfirst:

> 6.(b) to incur, during the Expenditure Period, Qualifying Expenditures in such amount as enables the Corporation to renounce to each Subscriber, Qualifying Expenditures in an amount equal to the Commitment Amount of such Subscriber;
>
> (c) to renounce to each Subscriber, pursuant to subsection 66(12.6) and 66(12.66) of the Tax Act and this Subscription Agreement, effective on or before December 31, 2007, Qualifying Expenditures incurred during the Expenditure Period in an amount equal to the Commitment Amount of such Subscriber;
>
> ...
>
> (g) if the Corporation does not renounce to the Subscriber, Qualifying Expenditures equal to the Commitment Amount of such Subscriber effective on or before December 31, 2007 and as the sole recourse to the Subscriber for such failure, the Corporation shall indemnify the Subscriber as to, and pay to the Subscriber, an amount equal to the amount of any tax payable under the Tax Act (and under any corresponding provincial legislation) by the Subscriber (or if the Subscriber is a partnership, by the partners thereof) as a consequence of such failure, such payment to be made on a timely basis once the amount is definitively determined, provided that for certainty the limitation of the Corporation's obligation to indemnify the Subscriber pursuant to this Section shall not apply to limit the Corporation's liability in the event of a breach by the Corporation of any other covenant, representation or warranty pursuant to this Agreement or the Underwriting Agreement;

3 Certain conditions were required to be satisfied before expenditures made by Earthfirst would qualify as "Qualifying Expenditures" pursuant to the *Income Tax Act* and the associated regulations. Because construction of Earthfirst's Dokie 1 wind power project was interrupted by events triggered by the CCAA filing, it may be that Earthfirst will not be able to satisfy some of these conditions. While Earthfirst is seeking a purchaser of the Dokie 1 project assets, and that purchaser may complete the necessary requirements for expenditures to be considered "Qualifying Expenditures", there is presently no guarantee that the necessary conditions will be met. The subscribers for flow-through shares may therefore have a claim under the indemnity set out in the subscription agreement.

**ISSUE**

Are the claims under the indemnity debt claims or claims for the return of an equity investment?

**ANALYSIS**

The flow-through share subscribers submit that their indemnity claims are not claims for the return of capital. Counsel for the flow-through share subscribers makes some persuasive arguments in that regard, including:

(a) that the underlying rights that form the basis of the claims are severable and distinct from the status of subscribers as shareholders of Earthfirst, in that the flow-through shares are composed of two distinct components, being common shares and the subscriber's right to the renunciation of a certain amount of tax credit or the right to be indemnified for tax credit not so renounced. It is submitted that further evidence of the distinct and severable nature of the indemnity claim can be found in the fact that, while the common share component of the flow-through shares can be transferred, the flow-through benefits accrue only to original subscribers;

(b) that the claimants in advancing a claim under the indemnity are not advancing a claim for the return of their investment in common shares;

(c) that the rights and obligations that form the basis of the indemnity claim are set out in the subscription agreement, which indicates an intention to create a debt obligation in the indemnity provisions; and

(d) that the claim under the indemnity is limited to a specific amount as compared to the unlimited upside potential of any equity investment, and that thus one of the policy reasons for drawing a distinction between debt and equity in the context of insolvency does not apply to an indemnity claim.

4 On the other side of the argument, it is clear that the indemnity claim derives from the original status of the subscribers as subscribers of shares, that the claim was acquired as part of an investment in shares, and that any recovery on the indemnity would serve to recoup a portion of what the subscriber originally invested, primarily qua shareholder. While it may be true that equity may become debt, as, for instance, in the case of declared dividends or a claim reduced to a judgment debt (Re I. Waxman & Sons Ltd. [2008] O.J. No. 885 at para 24 and 25), the indemnity claim has not undergone a transformation from its original purpose as a "sweetener" to the offering of common shares, even if individual subscribers have since sold the shares to which it was attached. The renunciation of flow-through tax credits, despite the payment of a premium for this feature, can be characterized as incidental or secondary to the equity features of the investment, a marketing feature

that provided an alternative to the share plus warrant tranche of the public offering for investors who found the feature attractive: *Canada Deposit Insurance Corp. v. Canadian Commercial Bank* [1992] S.C.J. No. 96 at para. 54.

**5** This type of indemnity skirts close to the line that courts are attempting to draw with respect to the characterization and ranking of equity and equity-type investments in the insolvency context. In Alberta, that line is drawn by the decision of LoVecchio, J. in *National Bank of Canada v. Merit Energy Ltd.*, [2001] A.J. No. 918, upheld by the Court of Appeal at [2002] A.J. No. 6. The indemnity at issue in Merit Energy was substantially identical to the one at issue in this case. While Lovecchio, J. appeared to refer to elements of misrepresentation arising from prospectus disclosure with respect to the Merit indemnity claim at para. 29 of the decision, it is clear that he considered the debt features of the indemnity in his later analysis, and noted at para. 54 that:

> While the Flow-Through Shareholders paid a premium for the shares (albeit to get the deductions), in my view the debt features associated with the CEE indemnity from Merit do not "transform' that part of the relationship from a shareholder relationship into a debt relationship. That part of the relationship remains "incidental" to being a shareholder.

The Court of Appeal in dismissing the appeal commented:

> Counsel for the appellant stresses the express indemnity covenant here, but in our view, it is ancillary to the underlying right, as found by the chambers judge. Characterization flows from the underlying right, not from the mechanism for its enforcement, nor from its non-performance.

The decision in Merit Energy thus determines the issue in this case, which is not distinguishable on any basis that is relevant to the issue. I also note that, while it is not determinative of the issue as the legislation has not yet been proclaimed, section 49 of Bill C-12, *An Act to amend the Bankruptcy and Insolvency Act,* the *Companies' Creditors Act*, the *Wage Protection Program Act* and Chapter 47 of the *Statues of Canada*, 2005, 2nd Sess., 39th Parl., 2007, ss. 49, 71 [Statute c.36] provides that a creditor is not entitled to a dividend in respect of any equity claim until all other claims are satisfied. Equity Claims are defined as including:

> (a) a dividend or similar payment,
> (b) a return of capital,
> (c) a redemption or retraction obligation,
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
> (e) contribution or indemnity in respect of a claim referred to in any paragraphs (a) to (d) [emphasis added].

**CONCLUSION**

I therefore grant:

> a) a declaration that potential claims that holders of flow-through common shares in Earthfirst may have against Earthfirst, if any, are at their core eq-

uity obligations rather than debt or creditor obligations, and, as such, necessarily rank behind in priority to claims made by creditors of Earthfirst and will not participate in any creditor plan or distribution; and

b) an order permitting Earthfirst to make certain payment to its creditors pursuant to a Plan of Arrangement in an amount and upon such terms to be determined by this Honourable Court at the date of this application without regard to any contingent or other claims of the flow-through shareholders or subscribers.

B.E.C. ROMAINE J.

* * * * *

**Corrigendum**
Released: July 8, 2009

The citation "Earthfirst Canada Inc. *(Companies' Creditors Arrangement Act)* 2009 ABQB 316" was corrected to read "Earthfirst Canada Inc. (Re) 2009 ABQB 316"

cp/e/qlcct/qlpwb/qlltl/qlaxr

# Tab 10

*Case Name:*

# ROI Fund Inc. v. Gandi Innovations Ltd.

**Between**
**Return On Innovation Capital Ltd. as agent for ROI Fund Inc., ROI Sceptre Canadian Retirement Fund, ROI Global Retirement Fund, and ROI High Yield Private Placement Fund and Any Other Fund Managed By ROI from time to time, Applicants, and Gandi Innovations Limited, Gandi Innovations Holdings LLC, Gandi Innovations LLC, Gandi Innovations Hold Co., and Gandi Special Holdings LLC., Respondents**

[2011] O.J. No. 3827

2011 ONSC 5018

83 C.B.R. (5th) 123

2011 CarswellOnt 8590

206 A.C.W.S. (3d) 464

Court File No. 09-CL-8172

Ontario Superior Court of Justice
Commercial List

**F.J.C. Newbould J.**

Heard: August 18, 2011.
Judgment: August 25, 2011.

(62 paras.)

*Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Compromises and arrangements -- Directions -- Motion by Monitor for directions allowed -- Gandi Group was under creditor protection and assets were sold with court approval -- Lender claimed repayment of debt and equity advance to Group -- Three claimants were party to advance in personal capacities -- Lender commenced arbitration proceeding against claimants -- Claimants sought indemnity of related costs from Group -- Monitor sought directions -- No evidence existed*

*that Group entities gave indemnities or otherwise acknowledged claimants' entitlement to indemnities -- For purpose of CCAA proceedings, lender's claim and indemnity claims constituted equity claims -- Companies' Creditors Arrangement Act, s. 2(1).*

Motion by the Monitor for the Gandi Group for advice and directions regarding indemnity claims made against the Group. The Gandi Group was under creditor protection. The Monitor was appointed in May 2009. The business and assets of the Group were sold with court approval. The Monitor held the proceeds for eventual distribution to unsecured creditors pursuant to a plan of compromise and arrangement. The indemnity claims arose from the 2007 reorganization of the Group's business structure. The claimants were officers and board members of Gandi Holdings. A lender advanced $75 million by way of debt and equity to the Group. The indemnity claimants were party to the advance in their personal capacities. In 2009, the lender commenced arbitration proceedings against the claimants for the total of the advance. The claimants asserted an entitlement to indemnification by the Group in respect of any award of damages which may be made against them in the arbitration together with all legal fees incurred in defending the arbitration. The claimants' proofs of claim relied on indemnity provisions set out in the limited liability company agreement and a separate indemnification made by Gandi Holdings at the time of the lender's advance. In 2011, the Monitor disallowed the claims on the basis that any claim would be made solely against Gandi Holdings rather than against other entities in the Group.

HELD: Motion allowed. There was no evidence that any indemnities from any other Gandi Group entities were made at the time of the advance. There were no corporate records supporting the contention that two of the claimants were an officer or director of Gandi Innovations. Thus, the third claimant was the only claimant entitled to identification from Gandi Innovations pursuant to the indemnity in the company's articles. Such claim was subject to a subordination agreement in respect of the debt portion of the advance, and thus the third claimant had no right to receive payment from Gandi Innovations in respect of his claim. There was no basis for inferring that the articles of the other Group entities contained the same indemnity as contained in the articles of Gandi Innovations. There was no prior acknowledgment of liability for indemnity by the Group. The claims of both the lender and the claimants were to be treated as equity claims for the purpose of the CCAA proceeding.

**Statutes, Regulations and Rules Cited:**

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 2(1), s. 6(8)

**Counsel:**

Harvey Chaiton and Maya Poliak, for the Monitor, BDO Canada Limited.

Mathew Halpin and Evan Cobb, for TA Associates Inc.

Christopher J. Cosgriffe, for Harry Gandy, James Gandy and Trent Garmoe.

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**ENDORSEMENT**

1 **F.J.C. NEWBOULD J.**:-- This is a motion brought by BDO Canada Limited in its capacity as the Court-appointed Monitor of Gandi Innovations Limited, Gandi Innovations Holdings LLC, Gandi Innovations LLC, Gandi Innovations Hold Co, and Gandi Special Holdings LLC (the "Gandi Group") for advice and directions, and particularly to determine preliminary issues in connection with the indemnity claims made by Hary Gandy, James Gandy and Trent Garmoe (the "Claimants") against all of the Gandi Group.

2 The Gandi Group is under CCAA protection. The Monitor was appointed in the Initial Order on May 8, 2009.

3 The business and assets of the Gandi Group have been sold with court approval. The proceeds from the sale are being held by the Monitor for eventual distribution to unsecured creditors pursuant to a plan of compromise and arrangement.

**Arbitration proceedings and indemnity claims**

4 Gandi Innovations Holdings LLC ("Gandi Holdings") was incorporated pursuant to the laws of the State of Delaware on August 24, 2007. On September 12, 2007, the Gandi Group re-organized their business structure so that Gandi Holdings became the direct or indirect parent of the other various entities comprising the Gandi Group.

5 TA Associates Inc. is a general partner for a number of TA partners. In conjunction with the reorganization of Gandi Holdings, it advanced approximately US $75 million on September 12, 2007 by way of debt and equity to the Gandi Group. The advance consisted of:

(i) an equity investment in the amount of US $50 million made pursuant to the terms of a Membership Interest Purchase Agreement in respect of Gandi Holdings dated as of September 12, 2007 made between, among others, Gandi Holdings, TA Associates and the Claimants in their personal capacities; and

(ii) an unsecured loan in the amount of US $25 million which amount was guaranteed by other members of the Gandi Group.

6 In January 2009, TA Associates commenced an arbitration proceeding against the Claimants. In the arbitration TA Associates claim damages against the Claimants in an amount of US $75 million with interest, being the total amount of TA Associates' investment in the Gandi Group. The arbitration has not yet been heard on its merits.

7 On December 20, 2010, the Monitor received proofs of claim of Hary Gandy and James Gandy against the Gandi Group in the approximate amount of $76 million and a proof of claim of Trent Garmoe against the Gandi Group in an approximate amount of $88 million. The Claimants assert an entitlement to indemnification by the Gandi Group in respect of any award of damages which may be made against them in the arbitration together with all legal fees incurred by the Claimants in defending the arbitration.

8 The proofs of claim filed by the Claimants rely on indemnity provisions set out in the Amended and Restated Limited Liability Company Agreement of Gandi Holdings and a separate Indemnification Agreement made by Gandi Holdings entered into in connection with the Membership Agreement made at the time of the TA Associates investment with Gandi Holdings. Gandi Holdings is the only Gandi entity that is a party to these indemnity agreements.

**9** On March 11, 2011 the Monitor disallowed the indemnity claims and advised the Claimants that based on the evidence filed in support of the indemnity claims, any indemnity claim would be solely against Gandi Holdings.

**10** The Claimants have served notices of dispute and have provided to the Monitor a memorandum of articles of Association of Gandi Canada which provides an indemnity in favour of directors and officers of Gandi Canada in certain circumstances.

**11** There is also an indemnity of Gandi Innovations Hold Co ("Gandi Hold Co"). At the relevant times James Gandy was the sole director of the company.

**12** There has been an extensive search for corporate documents. The Monitor made inquiries of Jaffe Raitt Heuer & Weiss Inc., former corporate counsel of the Gandi Group, and learned that all of corporate governance documents of the Gandi Group, at Hary Gandy's request, had been sent to Stikeman Elliot LLP, insolvency counsel for the Gandi Group, following the CCAA filing date. Counsel for the Monitor attended at the offices of Stikeman Elliott and reviewed the corporate governance documents in its possession.

**13** In addition the Monitor contacted counsel for Agfa, the purchaser of the assets of the Gandi Group, to inquire if it has in its possession copies of the Gandi Group's corporate governance records. The Monitor was advised by counsel for Agfa that Agfa was not able to find any corporate governance documents of the Gandi Group entities.

**14** The Monitor also reviewed the books and records of the Gandi Group in storage. In addition, the Monitor advised the Claimants that should they wish to undertake a review of the Gandi Group's records in storage, the Claimants were invited to contact the Monitor and arrange for such review. The review was arranged and conducted by the Claimants on June 3, 2011.

**15** It is a fact that there are not in existence documents that support the Claimants all being entitled to indemnities from each corporate entity in the Gaudi Group.

**Issues**

**16** Whether the Claimants will ever be with held liable in the arbitration is not yet known. However, whether the Claimants have rights to indemnification against all of the Gandi Group or against only Gandi Holdings and Gandi Hold Co will assist the Monitor in determining whether to proceed with a consolidated plan of arrangement or file an alternative plan excluding Gandi Holdings and/or Gandi Hold Co which would enable the Monitor to make a meaningful distribution to unsecured creditors prior to the completion of the arbitration.

**17** There is another preliminary issue. In the arbitration, TA Associates seeks to recover against the Claimants their equity investment of US $50 million, for which the Claimants in turn have sought indemnification from the Gandi Group. The Monitor seeks a preliminary determination as to whether these claims for indemnification relating to the claim by TA Associates for its equity investment constitute "equity claims" under the CCAA. A determination of this issue will assist the Monitor in determining the maximum amount which can be claimed by the Claimants and may facilitate an earlier distribution of funds available to unsecured creditors.

**Discussion**

**(a) Indemnity agreements**

**18** An Amended and Restated Limited Liability Company Agreement of Gandi Holdings dated September 12, 2007 provides for an indemnity by Gandi Holdings in section 6.8(a) for board members and officers. There is no dispute that the Claimants were officers and board members of Gandi Holdings. It also contains in section 7.6 an indemnity for Members as follows:

> (a) Without limitation of any other provision of this Agreement executed in connection herewith, the Company agrees to defend, indemnify and hold each Member, its affiliates and their respective direct and indirect partners (including partners of partners and stockholders and members of partners), members, stockholders, directors, officers, employees and agents and each person who controls any of them...

**19** Superwide Limited Partnership is a Member and the Claimants are partners of Superwide. Thus the Claimants are indemnified by Gandi Holdings by that provision as well.

**20** There is a form on indemnity agreement made between Gandi Holdings and indemnitees. The form in the record is an unsigned copy dated September 11, 2007. Neither the monitor nor any of the parties have been able to locate any of these agreements signed in favour of the Claimants. Hary Gandi, who swore an affidavit for the Claimants, said that a copy of this agreement was signed between Gandi Holdings and each of the Claimants on September 12, 2007. It contains the following:

> WHEREAS, the Company desires to provide Indemnitee with specific contractual assurance of Indemnitee's rights to full indemnification against litigation risks and related expenses (regardless, among other things, of any amendment to or revocation of the Company's LLC Agreement or any change in the ownership of the Company or the composition of its Board of Managers) ...
>
> ...
>
> 3. Agreement to indemnify... if Indemnitee was or is a party or is threatened to be made a party to any Proceeding by reason of Indemnitee's Corporate Status, Indemnitee shall be indemnified by the Company against all Expenses and Liabilities incurred . . . ."

**21** Assuming that this form of indemnity agreement was signed by Gandi Holdings and the Claimants, they would be covered by it.

**22** The Claimants contend that each of the corporate entities in the Gandi Group signed an indemnity in favour of each of them. This is based on a statement in the affidavit of Hary Gandy that Gandi Holdings and the other CCAA Respondents provided additional indemnities to him, James Gandy and Trent Garmoe dated September 12, 2007. He attached to his affidavit a form of the indemnification agreement to be signed by Gandi Holdings. No affidavit was filed from James Gandy or Trent Garmoe.

**23** There is no form of indemnity agreement in existence which names an indemnifier other than Gandi Holdings.

**24** The date of September 12, 2007, said to be the date that all of the entities in the Gandi Group signed indemnities in favour of each of the claimants, was the date of the investment by TA Associates in which it purchased a membership interest in Gandi Holdings only. Representatives of TA Associates received identical indemnities from Gandi Holdings. There is no evidence that any indemnities from any of the other Gandi Group entities were made at that time. To the contrary, the Membership Interest Purchase Agreement under which TA Associates purchased its membership interest in Gandi Holdings contained as a condition to closing a requirement that Gandi Holdings sign an indemnification agreement. The indemnification was only to be given by Gandi Holdings. There was no requirement for an indemnity to be given by any other entity in the Gandi Group,.

**25** I do not accept the bald statement of Hary Gandy that all of the entities in the Gandi Group gave indemnities at the time. The only indemnities that were given were by Gaudi Holdings.

**(b) Memorandum and articles of Gandi Hold Co**

**26** In the course of its investigation, the Monitor did locate an indemnity granted by Gandi Hold Co in its Memorandum and Articles in favour of its directors and officers. Those articles contain an indemnity in the same terms as the indemnity in the Gandi Innovations Limited articles, as discussed below. As the Monitor does not seek a determination regarding indemnities given by Gandi Hold Co, I need not discuss whether one or more of the Claimants is entitled to be indemnified by these articles.

**(c) Articles of Association of Gandi Innovations Limited (Gandi Canada)**

**27** The articles of this company contain an indemnity as follows:

> Every director or officer, former director or officer, or person who acts or acted at the Company's request, as a director or officer of the Company, a body corporate, partnership or other association of which the Company is or was a shareholder, partner, member or creditor and the heirs and legal representatives of such person, in absence of any dishonesty on the part of such persons shall be indemnified by the Company...in respect of any claim made against such person ... by reason of being or having been a director or officer of the Company. [emphasis added]

**28** The corporate records sent to the Monitor by the corporate solicitors who incorporated the company name James Gandy as the president, treasurer and secretary and as the sole director. Hary Gandy stated at the outset of his affidavit filed on behalf of the claimants that he was the president and chief executive officer and chairman of the board of the companies that made up the Gandi Group. There are no corporate records that support that assertion and on his cross-examination he acknowledged he had no documents, including board resolutions, contracts or appointment letters to show that he was ever a director or officer of Gandi Innovations Limited. He said that he was directing the business of all of the entities. On his cross-examination, he said that as far as he was concerned, James Handy and Trent Garmoe were directors and officers of the company.

**29** James Gandy did not file any affidavit to say that he was not the president, treasurer and secretary of the company, as shown in the corporate records. Trent Garmoe did not file any affidavit. I think it fair to draw an adverse inference that their evidence would not have been helpful to their case.

**30** The affidavit of Bruce Johnston filed on behalf of TA Associates states that Hary Gandy and Trent Garmoe were not directors or officers of Gandi Innovations Limited and that a document printed from the Nova Scotia Registry of Joint Stock Companies which was included in the closing documents for TA Associates' investment showed that James Gandy was the only director and officer of Gandi Innovations Limited.

**31** There has been an extensive search for corporate documents but none have been found that would support Hary Gundy or Trent Garmoe as being an officer or director of Gandi Innovations Limited.

**32** It is argued that the indemnity in the articles of Gandi Innovations Limited is in favour not only of officers and directors, but also "persons who acted at the Company's request as a director or officer of the Company", and that Hary Gandy and Trent Garmoe acted as directors and officers at the Company's request. There is certainly no documentary evidence of that. Presumably the request would have had to come from James Gandy, who is the sole officer and director according to the corporate records. There is no evidence from any of the Claimants that any request was made to Hary Gandy or Trent Garmoe to act as an officer or director of Gandi Innovations Limited, which one would have expected if the assertion was to be made.

**33** It is also argued that the board of managers (the Delaware concept of a board of directors) of Gandi Holdings operated the subsidiaries as if they were officers and directors of the subsidiaries. Again, there is no documentary evidence of that and no evidence from any of the Claimants to support the assertion. While Hary Gandy may have operated the business in a functional sense, that does not mean that he was acting as an officer or director of any subsidiary in the corporate sense. This is not mere semantics. TA Associates made a large investment, and one of the corporate documents provided on closing was the Nova Scotia Registry of Joint Stock Companies that showed only James Gandy as an officer and director. If all of the Claimants are entitled to be indemnified by Gandi Innovations Limited, it will impact the claim of TA Associates in the CCAA proceedings.

**34** In the circumstances, I find that the only person entitled to indemnification from Gandi Innovations Limited is James Gandy.

**35** However, in connection with the financing provided by TA Associates, James Gandy executed a Subordination Agreement dated as of September, 12, 2007 under which he agreed that any liability or obligations of Gandi Canada to him, present or in the future, would be deferred, postponed and subordinated in all respects to the repayment in full by Gandi Innovations of all indebtedness, liabilities and obligations owing to TA Associates in connection with the purchase by TA Associates of US $25 million in notes. Until that obligation to pay the notes in full with interest has been fulfilled, any claim by James Gandy under the indemnity from Gandi Innovations Limited is subordinated to the claim of TA Associates.

**36** The debt claim of TA Associates of $46,733,145 has been accepted by the Monitor. Assuming that the purchase price on the sale of the assets to Agfa is received in full, the monitor expects a distribution to unsecured creditors of approximately 27% of the value of their claims. In such circumstances, James Gundy will have no right to receive any payment from Gandi Innovations Limited in respect of his indemnity claim.

### (d) Other Gaudi Group entities

**37** It was asserted by the Claimants that because the Gandi companies operated essentially as one integrated company, it should be inferred that the constating documents of the other entities in the Gandi Group contained the same indemnity as contained in the bylaws of Gandi Innovations Limited and Gandi Hold Co. I do not agree.

**38** Gandi Innovations LLC is a Texas company. Its Amended and Restated Operating Agreement contains the types of things normally contained in a general bylaw of an Ontario corporation. It contains no provision for indemnities. It was argued that as no articles were obtained from Texas, it could be assumed that the articles contained an indemnity provision similar to that contained in the bylaws of Gandi Innovations Limited and Gandi Hold Co. I asked counsel to obtain whatever documentation was available in Texas, and subsequently the Monitor received from its US counsel, Vinson & Elkins LLP, a copy of articles of organization for Gandi Innovations LLC dated August 2, 2004. There is nothing in these articles dealing with indemnities. Vinson & Elkins LLP advised that these articles, together with amending articles already in the possession of the Monitor, are the only corporate governance documents on file with the State of Texas.

**39** Gandi Special Holdings LLC is a Delaware corporation. The Limited Liability Company Agreement of Gandi Special Holdings LLC, like the Texas company, contains the types of things normally contained in a general bylaw of an Ontario corporation. It contains no provision for indemnities. Following the hearing, the Monitor obtained through Vinson & Elkins LLP a Delaware Certificate of Formation of Gandi Special Holdings LLC. This document contains no provision for indemnities. A certificate of the Secretary of State of Delaware confirms that there were no other relevant documents on file and this was confirmed by Vinson & Elkins LLP.

**40** I find that there is no indemnity in favour of the Claimants in the corporate documentation of Gandi Innovations LLC and Gandi Special Holdings LLC.

**41** It is also argued on behalf of the Claimants that the Gandi Group have acknowledged an obligation to indemnify the Claimants and it is said that this arises from a meeting of the board of Gandi Holdings. It is argued that the Gandi Group through the Monitor is thus estopped from denying an indemnity for all of the Gandi Group companies. A document said to be minutes of a meeting of the board of managers of Gandi Holdings held on March 4, 2009 is relied on. That document contains the following paragraph:

> The next item on the agenda was the indemnification of the officers. It was generally agreed that all parties would follow the Purchase Agreement between Gandi Innovations and TA Resources dated September 12, 2007: Counsel for TA had previously expressed the opinion that indemnification was not allowed under the purchase agreement. Counsel for James Gandy, Hary Gandy and Trent Garmoe together with the Corporate Counsel, Matthew Murphy had previously expressed verbal opinions that the indemnification of the officers was permitted under the Purchase Agreement. Lydia Garay, as the only member not involved in the dispute between TA and the key holders, voted to follow the advice of Corporate Counsel, Matthew Murphy. To avoid any misunderstanding, Corporate Counsel would be requested to express that opinion in writing.

**42** I do not see this paragraph in the informal minutes as assisting the Claimants. It is a meeting of the board of Gandi Holdings. It says that it was generally agreed that all parties would follow the purchase agreement between Gandi Holdings and TA resources dated September 12, 2007. That

purchase agreement provides for an indemnity by only Gandi Holdings. Assuming that the minutes reflect a desire of some board members to indemnify officers of subsidiary corporations, and assuming that the Claimants thought they were officers of all of the subsidiary corporations, it is quite clear from the paragraph that there was a difference of view. The minute states that counsel for TA Associates had previously expressed the opinion that indemnification was not allowed under the purchase agreement and that counsel for the Claimants together with corporate counsel, Matthew Murphy, expressed the opposite opinion. The minute states that Lydia Garay, the only member not involved in the dispute between TA Associates and the key holders, voted to follow the advice of Corporate Counsel Terry Murphy and to avoid any misunderstanding, corporate counsel would be requested to express that opinion in writing.

**43** The affidavit of Bruce Johnston on behalf of TA Associates, who attended that meeting of the board of managers of Gandi Holdings swears that the Claimants voted to place Lydia Garay, a longtime employee and officer of Gandi Holdings, on the board despite a verbal agreement that he had with the Claimants to leave that board seat vacant and to work with him to appoint an outside independent board member. He stated Ms. Garay was completely reliant on the Gandy family for her job security and compensation.

**44** Mr. Johnston also states in his affidavit that the indemnification of the Claimants was discussed and that he and Mr. Taylor took the position that indemnification was not permitted. He said the Claimants took the position that indemnification was permitted, despite the language of the purchase agreement, and took the position that corporate counsel for Gandi Holdings had previously given a verbal opinion that indemnification was permitted under the purchase agreement. After hearing that, and during the meeting, Mr. Johnston sent an e-mail to Mr. Murphy who two minutes later responded that he had not advised on the question of an indemnity under the purchase agreement. Mr. Johnson states that he then read that e-mail at the meeting. I accept his evidence on this.

**45** Whether or not Ms. Garay was a disinterested or proper member of the board of management of Gandi Holdings, the minute states that she voted to follow the advice of corporate counsel. At the next board meeting on May 4, 2009, Ms. Garay said that she had sought the written opinion of corporate counsel but had not received it. To date no opinion from Mr. Murphy has surfaced. On the face of those minutes from March 4, 2009, there has been no approval of any indemnities in favour of the Claimants for other corporations. I cannot find on the evidence that there was any agreement that the Claimants would be indemnified by subsidiary corporations, nor is there any evidence that any subsidiary corporation ever enacted any documentation of any kind to provide such indemnities. The opposite is the case, as has been discussed.

**46** Finally, the Claimants allege that the Gandi Group has previously acknowledged their liability to indemnify the Claimants for any damage, award or legal costs incurred by the following actions:

(i) certain Gandi entities made payments of defence costs in connection with the arbitration both pre-and post the CCAA filing; and
(ii) the Monitor allegedly approved payment of post-filing defence costs.

**47** Until the sale of the Gandi Group to Agfa was completed, this CCAA proceeding was a debtor in possession restructuring with the business and affairs of the Gandi Group being managed by their officers and directors, specifically Hary Gundy and Trent Garmoe. Payments of legal fees

to Langley and Banack Inc., U.S. lawyers for the Gandi Group and the Claimants, were made by or on authorization of Trent Garmoe.

**48** Pursuant to the terms of the Initial Order, the Monitor was required to approve all expenditures over $10,000 before payment was made. The Monitor approved payment of legal fees to counsel for the Gandi Group on the general understanding that such fees were incurred by the Gandi Group in connection with the Gandi Group's insolvency proceeding and for general corporate work for the Gandi Group.

**49** I accept the statement of the Monitor that it did not knowingly approve the payment of the Claimants' defence costs in connection with the arbitration.

**50** Subsequent to the completion of the sale to Agfa, the Monitor learned that a nominal amount of the legal fees approved by the Monitor was subsequently allocated to cover the costs of the arbitration. I accept the statement of the Monitor that it had no input, knowledge or control over such allocation, and had it been consulted, would have been opposed to such allocation as it did not involve any member of the Gandi Group.

**51** In the circumstances there is no basis for the assertion that the Monitor is somehow estopped by reason of the payment of legal fees from denying that there are other indemnities in favour of the Claimants.

### (e) Are the Claimants claims debt or equity claims?

**52** This involves the application of provisions of the CCAA to the claims asserted by TA Associates in the arbitration.

**53** Section 6(8) of the CCAA provides:

> No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

**54** In s. 2(1) of the CCAA, equity claims are defined as follows:

> "equity claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
> (b) a return of capital,
> (c) a redemption or retraction obligation,
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);

**55** This definition of equity claim came into force on September 18, 2009. Although this provision does not apply to the Gandi Group's CCAA proceedings which commenced shortly prior to the legislative amendments, courts have noted that the amendments codified existing case law relating

to the treatment of equity claims in insolvency proceedings. In *Re Nelson Financial Group Ltd.*, (2010) 75 B.L.R. (4th) 302, Pepall J. stated:

> The amendments to the CCAA came into force on September 18, 2009. It is clear that the amendments incorporated the historical treatment of equity claims. The language of section 2 is clear and broad. Equity claim means a claim in respect of an equity interest and includes, amongst other things, a claim for rescission of a purchase or sale of an equity interest. Pursuant to sections 6(8) and 22.1, equity claims are rendered subordinate to those of creditors.

**56** If the claims in the arbitration commenced by TA Associates against the Claimants are equity claims, the claims by the Claimants in the CCAA process for contribution or indemnity in respect of those claims would be equity claims. The Claimants contend that the claims in the arbitration are not equity claims.

**57** The claims in the arbitration by TA Associates against the creditors include claims for various breaches of contract, fraud, rescission, or in the alternative, rescissory damages, negligent misrepresentation, breach of fiduciary duty and tortious interference with advantageous business relationships and prospective economic advantage.

**58** In the arbitration TA Associates seeks to recover the investment that it made in Gandi Holdings, including the US $25 million debt secured by promissory notes and the US $50 million equity investment made by way of a membership subscription in Gandi Holdings.

**59** The Claimants assert that the claim for US $50 million by TA Associates cannot be an equity claim because it is based on breaches of contract, torts and equity. I do not see that as being the deciding factor. TA Associates seeks the return of its US $50 million equity investment because of various wrongdoings alleged against the Claimants and the fact that the claim is based on these causes of action does not make it any less a claim in equity. The legal tools that are used is not the important thing. It is the fact that they are being used to recover an equity investment that is important.

**60** In *Re Nelson Financial Group Lrd.*, *supra*, at Peppall J. stated that historically, the claims and rights of shareholders were not treated as provable claims and ranked after creditors of an insolvent corporation in a liquidation. She also stated:

> This treatment also has been held to encompass fraudulent misrepresentation claims advanced by a shareholder seeking to recover his investment: *Re Blue Range Resource Corp.*, [2000] A.J. No. 14. In that case, Romaine J. held that the alleged loss derived from and was inextricably intertwined with the shareholder interest. Similarly, in the United States, the Second Circuit Court of Appeal in *Re Stirling Homex Corp.* concluded that shareholders, including those who had allegedly been defrauded, were subordinate to the general creditors when the company was insolvent.

**61** As the amendments to the CCAA incorporated the historical treatment of equity claims, in my view the claims of TA Associates in the arbitration to be compensated for the loss of its equity interest of US $50 million is to be treated as an equity claim and that the claims of the Claimants for indemnity against that claim is also to be treated as an equity claim in this CCAA proceeding.

**Order**

**62** An order in the form of a declaration shall go in accordance with these reasons.

F.J.C. NEWBOULD J.

cp/e/qlcct/qlvxw/qlced/qlhcs

# Tab 11

*Case Name:*

# ROI Fund Inc. v. Gandi Innovations Ltd.

**Between**
**Return on Innovation Capital Ltd. as agent for ROI Fund Inc., ROI Sceptre Canadian Retirement Fund, ROI Global Retirement Fund and ROI high Yield Private Placement Fund and Any Other Fund Managed by ROI from time to time, Applicants/Respondents, and**
**Gandi Innovations Limited, Gandi Innovations Holdings LLC and Gandi Innovations LLC, Respondents/Appellants**

[2012] O.J. No. 31

2012 ONCA 10

90 C.B.R. (5th) 141

2012 CarswellOnt 103

211 A.C.W.S. (3d) 264

Docket: M40553

Ontario Court of Appeal
Toronto, Ontario

**R.J. Sharpe, R.A. Blair and P.S. Rouleau JJ.A.**

Heard: January 3, 2012 by written submissions.
Judgment: January 9, 2012.

(13 paras.)

*Bankruptcy and insolvency law -- Companies' Creditors Arrangement Act (CCAA) matters -- Compromises and arrangements -- Claims -- Claims against directors -- Motion by officers, directors and shareholders in Gandi Group for leave to appeal from order determining their entitlement to indemnity from Gandi Group companies arising out of arbitration proceedings brought against them by TA Associates dismissed -- TA Associates was major unsecured creditor in CCAA proceed-*

*ings -- Issues raised by appeal were of no significance to practice -- Further, appeal with respect to these issues had little merit.*

Motion by the officers, directors and shareholders in the Gandi Group for leave to appeal from an order determining their entitlement to indemnity from the Gandi Group companies arising out of arbitration proceedings brought against them by TA Associates, the major unsecured creditor in the CCAA proceedings. The Gandi Group companies were under CCAA protection. The order provided that the claimants were only entitled to indemnity from the direct and indirect parent company, that any claim of James Gandy was subordinated to the claim of TA Associates because of an earlier existing Subordination Agreement, and that the claims for indemnification in respect of the TA Associates claim in the arbitration were equity claims for purposes of the CCAA and therefore subsequent in priority to the claims of unsecured creditors.

HELD: Motion dismissed. The indemnification issue and subordination issues raised by the appeal were of no significance to the practice and the appeal with respect to these issues had little merit. The application judge's determination of the claimants' indemnity claims as equity claims was also not of significance to the practice since all insolvency proceedings commenced after the new provisions of the CCAA came into effect in September 2009 would be governed by those provisions, not by the prior jurisprudence.

**Statutes, Regulations and Rules Cited:**

Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 2(1), s. 6(8)

**Counsel:**

Christopher J. Cosgriffe and Natasha S. Danson, for James Gandy, Hary Gandy and Trent Garmoe.

Matthew J. Halpin and Evan Cobb, for TA Associates Inc.

Harvey Chaiton and Maya Poliak, for the Monitor.

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ENDORSEMENT

The following judgment was delivered by

THE COURT:--

**Overview**

**1** The moving parties (James Gandy, Hary Gandy and Trent Garmoe) are officers, directors and shareholders in the Gandi Group, a series of related companies currently under CCAA protection. In those proceedings they assert indemnity claims in the range of $75 - 80 million against each of the companies in the Gandi Group. The indemnity claims arise out of arbitration proceedings brought against them individually, as officers and directors, by TA Associates, a disgruntled investor in the Gandi Group. TA Associates is the major unsecured creditor in the CCAA proceedings.

2 The assets of the Gandi Group have been sold and what remains to be done in the CCAA process is the finalization of a plan of compromise and arrangement for the distribution of the proceeds among the various creditors. Before settling on the most effective type of plan for such a distribution - a consolidated plan, a partial consolidation plan, or individual corporate plans - the Monitor and the creditors sought to have two preliminary issues determined by the Court:

a) whether the moving parties (the Claimants) are entitled to indemnity from all of the entities which comprise the Gandi Group, and, if so,
b) whether those indemnification claims are "equity" or "non-equity" claims for purposes of the CCAA (non-equity claims have priority).

3 On August 25, 2011, Justice Newbould, sitting on the Commercial List, ruled:

a) that the Claimants were only entitled to indemnity from the direct and indirect parent company, Gandi Holdings (except that the Claimant, James Gandy only was also entitled to indemnification from a second entity in the Group, Gandi Canada);
b) that any claim of James Gandy was subordinated to the claim of TA Associates because of an earlier existing Subordination Agreement; and
c) that the claims for indemnification in respect of the TA Associates claim in the arbitration were equity claims for purposes of the CCAA and therefore subsequent in priority to the claims of unsecured creditors.

4 The Claimants seek leave to appeal from that order.

5 We deny the request.

**Analysis**

The Test

6 Leave to appeal is granted sparingly in CCAA proceedings and only when there are serious and arguable grounds that are of real and significant interest to the parties. The Court considers four factors:

(1) Whether the point on the proposed appeal is of significance to the practice;
(2) Whether the point is of significance to the action;
(3) Whether the appeal is prima facie meritorious or frivolous; and
(4) Whether the appeal will unduly hinder the progress of the action.

See *Re Stelco (Re)*, (2005), 75 O.R. (3d) 5, at para. 24 (C.A.).

7 The Claimants do not meet this stringent test here.

The Indemnification Issue

8 Whether the Claimants are entitled to indemnification from all or just one or some of the entities in the Gandi Group was essentially a factual determination by the motion judge, is of no significance to the practice as a whole, and the proposed appeal on that issue is of doubtful merit in our view. We would not grant leave to appeal on that issue.

The Subordination Issue

**9** The same may be said for the Subordination Agreement issue. The Claimants argue that by declaring that the indemnity claim of James Gandy is subordinate to the CCAA claim of TA Associates, the motion judge usurped the role of the pending arbitration. We do not agree. The subordination issue needed to be clarified for purposes of the CCAA proceedings. None of the criteria respecting the granting of leave is met in relation to this proposed ground.

The "Equity Claim" Issue

**10** Nor do we see any basis for granting leave to appeal on the equity/non-equity claim issue.

**11** "Equity" claims are subsequent in priority to non-equity claims by virtue of s. 6(8) of the CCAA. What constitutes an "equity claim" is defined in s. 2(1) and would appear to encompass the indemnity claims asserted by the Claimants here. Those provisions of the Act did not come into force until shortly after the Gandi Group CCAA proceedings commenced, however, and therefore do not apply in this situation. Newbould J. relied upon previous case law suggesting that the new provisions simply incorporated the historical treatment of equity claims in such proceedings: see, for example, *Re Nelson Financial Group Ltd.*, 2010 ONSC 6229 (CanLII), (2010), 75 B.L.R. (4th) 302, at para. 27 (Pepall J.). He therefore concluded that TA Associates was in substance attempting to reclaim its equity investment in the Gandi Group through the arbitration proceedings and that the Claimants' indemnity claims arising from that claim must be equity claims for CCAA purposes as well.

**12** This issue in the proposed appeal is not of significance to the practice since all insolvency proceedings commenced after the new provisions of the CCAA came into effect in September 2009 will be governed by those provisions, not by the prior jurisprudence. The interpretation of sections 6(8) and 2(1) does not come into play on this appeal. To the extent that existing case law continues to govern whatever pre-September 2009 insolvency proceedings are still in the system, those cases will fall to be decided on their own facts. We see no error in the motion judge's analysis of the jurisprudence or in his application of it to the facts of this case, and therefore see no basis for granting leave to appeal from his disposition of the equity issue in these circumstances.

**Disposition**

**13** The motion for leave to appeal is therefore dismissed. Costs to the Monitor and to TA Associates fixed in the amount of $5,000 each, inclusive of disbursements and all applicable taxes.

R.J. SHARPE J.A.
R.A. BLAIR J.A.
P.S. ROULEAU J.A.

cp/e/qllxr/qljxr/qlmll/qlana/qlcas

# Tab 12

*Indexed as:*

# National Bank of Canada v. Merit Energy Inc.

**Between**
**National Bank of Canada, Bank One, NA and Bank One, Canada, respondents (plaintiffs), and Merit Energy Inc., respondent (defendant), and Dundee Securities Corporation, Peters & Co. Limited, Nesbitt Burns Inc., Newcrest Capital Inc., RBC Dominion Securities Inc. and Bunting Warburg Dillon Read Inc., appellants (applicants)**
**(Action No. 0001-04994)**
**And between**
**Magellan Aerospace Limited, not parties to the appeal, (plaintiff), and First Energy Capital Corp., Dundee Securities Corporation, Peters & Co. Limited, Nesbitt Burns Inc., Newcrest Capital Inc., RBC Securities Inc., and Bunting Warburg Dillon Read Inc., not parties to the appeal, (defendants) Merit Energy Ltd., Duncan A. Chisholm, Kent J. Edinga, John W. Ferguson, David D. Johnson, John P. Kaumeyer, Lawrence F. Walter, Richard A. Grafton and Barry Stobo, not parties to the appeal, (third parties)**
**(Action No. 0001-02529)**
**And between**
**Larry Delf, on behalf of himself, and all other members of a class having a claim against the defendants, Merit Energy Ltd., Duncan A. Chisholm, Kent J. Edinga, John W. Ferguson, David D. Johnson, John P. Kaumeyer, Lawrence F. Walter, First Energy Capital Corp., Dundee Securities Corporation, Peters & Co. Limited, Nesbitt Burns Inc., Newcrest Capital Inc., RBC Dominion Securities Inc., Bunting Warburg Dillon Read Inc. and PriceWaterHouseCoopers LLP, not parties to the appeal, (plaintiffs), and Merit Energy Ltd., Duncan A. Chisholm, Kent J. Edinga, John W. Ferguson, David D. Johnson, John P. Kaumeyer, Lawrence F. Walter, First Energy Capital Corp., Dundee Securities Corporation, Peters & Co. Limited, Nesbitt Burns Inc., Newcrest**

**Capital Inc., RBC Dominion Securities Inc., Bunting Warburg Dillon Read Inc. and PriceWaterHouseCoopers LLP, not parties to the appeal, (defendants), and Merit Energy Ltd., Duncan A. Chisholm, Kent J. Edinga, John W. Ferguson, David D. Johnson, John P. Kaumeyer, Lawrence F. Walter, Richard A. Grafton, and Barry Stobo, not parties to the appeal, (third parties)**
**(Action No. 001-01899)**
**And between**
**Law Investments Ltd., Debra Wollersheim, John Wollersheim, Urvashi Patel, Kent McDougall, Ron Sachkiw, Reginald Ball, Fred Claridge, Ben Dulley, Lawrence Fan, Glen Gibling, Ralph Gibson, Wayne Gillespie, T. Jack Hall, Jim Hinks, Alnoor Kassam, Gordon Kerr, Arif Kurji, Victor Luciak, Bill Mah, Wayne McNeill, Dennis Paddock, Dave Purcell, Roger Rodermound, Dalton Siebrasse, Shiraz Sumar, Salim Sumar, James Sachkiw, Michael Theilgaard, Astrid Theilgaard, Richard Walls, Alexandra Smith, Geoff Smith, and Ice Gate Holdings Inc., not parties to the appeal, (plaintiffs), and Merit Energy Ltd., Duncan Chisholm, Kent J. Edinga, John W. Ferguson, Richard A. Grafton, David D. Johnson, John P. Kaumeyer, PriceWaterHouseCoopers LLP, First Energy Capital Corp., Dundee Securities Corporation, Peters & Co. Ltd., Nesbitt Burns Inc., Newcrest Capital Inc., RBC Dominion Securities Inc., and Bunting Warburg Dillon Read Inc., not parties to the appeal, (defendants), and Merit Energy Ltd., Duncan A. Chisholm, Kent J. Edinga, John W. Ferguson, David D. Johnson, John P. Kaumeyer, Lawrence F. Walter, Richard A. Grafton, and Barry Stobo, not parties to the appeal (third parties)**
**(Action No. 0001-13166)**

[2001] A.J. No. 760

2001 ABCA 138

[2001] 8 W.W.R. 448

93 Alta. L.R. (3d) 43

281 A.R. 389

15 B.L.R. (3d) 172

2 P.P.S.A.C. (3d) 225

106 A.C.W.S. (3d) 74

2001 CarswellAlta 806

Dockets: 00-19028 and 00-19029

Alberta Court of Appeal
Calgary, Alberta

**Berger, Costigan and Paperny JJ.A.**

Heard: May 18, 2001.
Judgment: filed June 12, 2001.

(11 paras.)

On appeal from a portion of the Judgment and Order of Lovecchio J. Order dated the 31st day of August, 2000. Entered the 19th day of September, 2000. Order dated the 4th day of October, 2000. Entered the 5th day of October, 2000.

**Counsel:**

E.D.D. Tavender, Q.C. and M. Lindsay, for the appellants, Dundee Securities Corporation, Peters & Co. Limited, Nesbitt Burns Inc., Newcrest Capital Inc., RBC Dominion Securities Inc. and Bunting Warburg Dillon Read Inc.
H. Gorman and S. Leitl, for the respondents, National Bank of Canada, Bank One, NA and Bank One Canada.
F. Dearlove and C. Simard, for the respondent, Arthur Andersen, Inc., Receiver & Manager of Merit Energy Ltd.
G. McLennan, for PriceWaterhouseCoopers LLP.
J. Rooney, for Kent Edinga, John P. Kaumeyer, John W. Ferguson and Richard Grafton.
D.J. McDonald, Q.C., for Duncan A. Chisholm and Lawrence F. Walter.
T. Mallett, for First Energy Capital Corp.
W. McNally, for the plaintiffs, Larry Delf.
D. Klein, for Kitzul et al in a B.C. action and Larry Delf in an Ontario action.
P. Jervis, for Canada Dominion Resources Limited.

MEMORANDUM OF JUDGMENT

THE COURT:--

INTRODUCTION

**1** This appeal raises the question of whether underwriters who perform services for a corporation pursuant to an underwriting agreement containing indemnity rights are, by virtue of those rights, entitled to a declaration of an equitable lien or charge over the corporation's assets or the proceeds therefrom?

**2** This appeal was dismissed at the end of the hearing with reasons to follow. These are our reasons.

BACKGROUND

**3** The appellants are underwriters who agreed to participate in a public offering of flow-through common shares to the public of Merit Energy Ltd. ("Merit"). The underwriting agreement paragraph 16 provides:

> The Corporation shall indemnify and save each of the Indemnified Persons, harmless against and from all liabilities, claims, demands, losses (other than losses of profit in connection with the distribution of the Common Shares), costs, damages and expenses to which any of the Indemnified Persons may be subject or which any of the indemnified Persons may suffer or incur, whether under the provisions of any statute or otherwise, in any way caused by, or arising directly or indirectly from or in consequence of:
>
> (a) any information or statement contained in the Public Record (other than any information or statement relating solely to one or more of the Underwriters and furnished to the Corporation by the Underwriters for inclusion in the Public Record) which is or is alleged to be untrue or any omission or alleged omission to provide any information or state any fact the omission of which makes or is alleged to make any such information or statement untrue or misleading in light of the circumstances in which it was made;
>
> (b) any misrepresentation or alleged misrepresentation (except a misrepresentation or alleged misrepresentation which is based upon information relating solely to one or more of the Underwriters and furnished to the Corporation by the Underwriters for inclusion in the Public Record) in the Public Record;
>
> ...
>
> (e) any breach of, default under or non-compliance by the Corporation with any representation, warranty, term or condition of this agreement or any requirement of applicable Securities Laws in connection with or relating to the distribution of the Common Shares;

**4** Merit became insolvent and sought protection under the CCAA, although a plan of arrangement was not approved. The court appointed a receiver/manager of Merit on the application of Merit's lenders. At that time, Merit owed the lenders approximately $70 million dollars.

**5** On August 9, 2000, the receiver applied to approve the sale of Merit's assets for approximately $92 million dollars and to further approve an interim distribution of the sale proceeds to the lenders of up to $60 million dollars.

**6** The court accepted that the lenders security over Merit's assets was valid, enforceable and first in priority. The court approved the sale and ordered an interim distribution of $45 million dollars to the lenders. The court also ordered that any party claiming an equitable lien, constructive trust or other entitlement in priority to the lenders, file an application returnable August 31, 2000. This appeal results from the underwriters' unsuccessful application before the learned chambers justice. The application was opposed by the respondent lenders.

ANALYSIS

**7** The underwriters maintain their entitlement to an equitable lien over Merit's assets or the proceeds therefrom, in priority to the respondents on the following basis: The underwriters underwrote the share sale as agents for Merit, in reliance upon Merit's information and in consideration of express indemnity rights pursuant to their underwriting agreement. They submit that where an agent has performed valuable services for the benefit of others in reliance upon that party and upon a covenant to indemnify, an equitable charge should be created where the indemnifier is unable to respond to the claim.

**8** In support of this proposition, the appellants analogize their relationship to the indemnity rights of a trustee and the subrogation rights of an insurer, relationships which may give rise to an equitable lien. Further, the appellants point to circumstances in which trusts have been imposed on funds to protect officers and directors from liability arising from their rights of indemnity. In those relationships, the obligations of the indemnified are onerous, unique and, for separate and distinct policy reasons, are given a priority over certain specific assets in appropriate circumstances.

**9** The appellants submit here, that a special relationship akin to that of trustee or insurer with a subrogated claim exists such that the court should intervene to give resonance to the indemnity by granting an equitable lien over the proceeds in question. However, they have been unable to provide any authority to establish that a mere contract for a right of indemnity, without more, grants a security interest in the property of the indemnified.

**10** Assuming, without deciding, that this court has the jurisdiction to grant an equitable lien in priority to secured lenders, the appellants have been unable to persuade us of any equitable basis upon which to distinguish their relationship with Merit from any other of Merit's unsecured creditors, who also provided goods or services for which they expected to be paid, have not been and may never be as a result of the insolvency. The mere existence of a covenant to indemnify as partial consideration for services, is not a foundation for equitable relief in this case, nor does it assist the appellants to classify them as agents. Assuming special relationships can give rise to equitable liens on specific property, the blanket lien urged upon us in favor of the underwriters, in these circumstances, is not supportable.

**11** While the arguments advanced by the appellants are creative, we find, as did the learned chambers justice, that they are without merit and do not support a triable issue. As well, insolvency

proceedings by their very nature, are to be resolved in a summary fashion to the extent possible for the benefit of all creditors. In our view, the learned chambers justice was correct in summarily dismissing the underwriters' claim.

BERGER J.A.
COSTIGAN J.A.
PAPERNY J.A.

cp/i/qlrds

# Tab 13

*Indexed as:*

# Rizzo & Rizzo Shoes Ltd. (Re)

**Philippe Adrien, Emilia Berardi, Paul Creador, Lorenzo Abel Vasquez and Lindy Wagner on their own behalf and on behalf of the other former employees of Rizzo & Rizzo Shoes Limited, appellants;**

**v.**

**Zittrer, Siblin & Associates, Inc., Trustees in Bankruptcy of the Estate of Rizzo & Rizzo Shoes Limited, respondent, and The Ministry of Labour for the Province of Ontario, Employment Standards Branch, party.**

[1998] 1 S.C.R. 27

[1998] S.C.J. No. 2

File No.: 24711.

Supreme Court of Canada

1997: October 16 / 1998: January 22.

**Present: Gonthier, Cory, McLachlin, Iacobucci and Major JJ.**

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

*Employment law -- Bankruptcy -- Termination pay and severance available when employment terminated by the employer -- Whether bankruptcy can be said to be termination by the employer -- Employment Standards Act, R.S.O. 1980, c. 137, ss. 7(5), 40(1), (7), 40a -- Employment Standards Amendment Act, 1981, S.O. 1981, c. 22, s. 2(3) -- Bankruptcy Act, R.S.C., 1985, c. B-3, s. 121(1) -- Interpretation Act, R.S.O. 1990, c. I.11, ss. 10, 17.*

A bankrupt firm's employees lost their jobs when a receiving order was made with respect to the firm's property. All wages, salaries, commissions and vacation pay were paid to the date of the receiving order. The province's Ministry of Labour audited the firm's records to determine if any outstanding termination or severance pay was owing to former employees under the Employment Standards Act ("ESA") and delivered a proof of claim to the Trustee. The Trustee disallowed the claims on the ground that the bankruptcy of an employer does not constitute dismissal from em-

ployment and accordingly creates no entitlement to severance, termination or vacation pay under the ESA. The Ministry successfully appealed to the Ontario Court (General Division) but the Ontario Court of Appeal overturned that court's ruling and restored the Trustee's decision. The Ministry sought leave to appeal from the Court of Appeal judgment but discontinued its application. Following the discontinuance of the appeal, the Trustee paid a dividend to Rizzo's creditors, thereby leaving significantly less funds in the estate. Subsequently, the appellants, five former employees of Rizzo, moved to set aside the discontinuance, add themselves as parties to the proceedings, and requested and were granted an order granting them leave to appeal. At issue here is whether the termination of employment caused by the bankruptcy of an employer give rise to a claim provable in bankruptcy for termination pay and severance pay in accordance with the provisions of the ESA.

Held: The appeal should be allowed.

At the heart of this conflict is an issue of statutory interpretation. Although the plain language of ss. 40 and 40a of the ESA suggests that termination pay and severance pay are payable only when the employer terminates the employment, statutory interpretation cannot be founded on the wording of the legislation alone. 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. Moreover, s. 10 of Ontario's Interpretation Act provides that every Act "shall be deemed to be remedial" and directs that every Act shall "receive such fair, large and liberal construction and interpretation as will best ensure the attainment of the object of the Act according to its true intent, meaning and spirit".

The objects of the ESA and of the termination and severance pay provisions themselves are broadly premised upon the need to protect employees. Finding ss. 40 and 40a to be inapplicable in bankruptcy situations is incompatible with both the object of the ESA and the termination and severance pay provisions. The legislature does not intend to produce absurd consequences and such a consequence would result if employees dismissed before the bankruptcy were to be entitled to these benefits while those dismissed after a bankruptcy would not be so entitled. A distinction would be made between employees merely on the basis of the timing of their dismissal and such a result would arbitrarily deprive some of a means to cope with economic dislocation.

The use of legislative history as a tool for determining the intention of the legislature is an entirely appropriate exercise. Section 2(3) of the Employment Standards Amendment Act, 1981 exempted from severance pay obligations employers who became bankrupt and lost control of their assets between the coming into force of the amendment and its receipt of royal assent. Section 2(3) necessarily implies that the severance pay obligation does in fact extend to bankrupt employers. If this were not the case, no readily apparent purpose would be served by this transitional provision. Further, since the ESA is benefits-conferring legislation, it ought to be interpreted in a broad and generous manner. Any doubt arising from difficulties of language should be resolved in favour of the claimant.

When the express words of ss. 40 and 40a are examined in their entire context, the words "terminated by an employer" must be interpreted to include termination resulting from the bankruptcy of the employer. The impetus behind the termination of employment has no bearing upon the ability of the dismissed employee to cope with the sudden economic dislocation caused by unemployment. As all dismissed employees are equally in need of the protections provided by the ESA, any distinction

between employees whose termination resulted from the bankruptcy of their employer and those who have been terminated for some other reason would be arbitrary and inequitable. Such an interpretation would defeat the true meaning, intent and spirit of the ESA. Termination as a result of an employer's bankruptcy therefore does give rise to an unsecured claim provable in bankruptcy pursuant to s. 121 of the Bankruptcy Act for termination and severance pay in accordance with ss. 40 and 40a of the ESA. It was not necessary to address the applicability of s. 7(5) of the ESA.

**Cases Cited**

Distinguished: Re Malone Lynch Securities Ltd., [1972] 3 O.R. 725; Re Kemp Products Ltd. (1978), 27 C.B.R. (N.S.) 1; Mills-Hughes v. Raynor (1988), 63 O.R. (2d) 343; referred to: U.F.C.W., Loc. 617P v. Royal Dressed Meats Inc. (Trustee of) (1989), 76 C.B.R. (N.S.) 86; R. v. Hydro-Québec, [1997] 1 S.C.R. 213; Royal Bank of Canada v. Sparrow Electric Corp., [1997] 1 S.C.R. 411; Verdun v. Toronto-Dominion Bank, [1996] 3 S.C.R. 550; Friesen v. Canada, [1995] 3 S.C.R. 103; Machtinger v. HOJ Industries Ltd., [1992] 1 S.C.R. 986; Wallace v. United Grain Growers Ltd., [1997] 3 S.C.R. 701; R. v. TNT Canada Inc. (1996), 27 O.R. (3d) 546; Re Telegram Publishing Co. v. Zwelling (1972), 1 L.A.C. (2d) 1; R. v. Vasil, [1981] 1 S.C.R. 469; Paul v. The Queen, [1982] 1 S.C.R. 621; R. v. Morgentaler, [1993] 3 S.C.R. 463; Abrahams v. Attorney General of Canada, [1983] 1 S.C.R. 2; Hills v. Canada (Attorney General), [1988] 1 S.C.R. 513; British Columbia (Director of Employment Standards) v. Eland Distributors Ltd. (Trustee of) (1996), 40 C.B.R. (3d) 25; R. v. Z. (D.A.), [1992] 2 S.C.R. 1025.

**Statutes and Regulations Cited**

Bankruptcy Act, R.S.C., 1985, c. B-3 [now the Bankruptcy and Insolvency Act], s. 121(1).
Employment Standards Act, R.S.O. 1970, c. 147, s. 13(2).
Employment Standards Act, R.S.O. 1980, c. 137, ss. 7(5) [rep. & sub. 1986, c. 51, s. 2], 40(1) [rep. & sub. 1987, c. 30, s. 4(1)], (7), 40a(1) [rep. & sub. ibid., s. 5(1)].
Employment Standards Act, 1974, S.O. 1974, c. 112, s. 40(7).
Employment Standards Amendment Act, 1981, S.O. 1981, c. 22, s. 2.
Interpretation Act, R.S.O. 1980, c. 219 [now R.S.O. 1990, c. I.11], ss. 10, 17.
Labour Relations and Employment Statute Law Amendment Act, 1995, S.O. 1995, c. 1, ss. 74(1), 75(1).

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Sullivan, Ruth. Statutory Interpretation. Concord, Ont.: Irwin Law, 1997.

APPEAL from a judgment of the Ontario Court of Appeal (1995), 22 O.R. (3d) 385, 80 O.A.C. 201, 30 C.B.R. (3d) 1, 9 C.C.E.L. (2d) 264, 95 C.L.L.C. par. 210-020, [1995] O.J. No. 586 (QL), reversing a judgment of the Ontario Court (General Division) (1991), 6 O.R. (3d) 441, 11 C.B.R. (3d) 246, 92 C.L.L.C. par. 14,013, ruling that the Ministry of Labour could prove claims on behalf of employees of the bankrupt. Appeal allowed.

Steven M. Barrett and Kathleen Martin, for the appellants.
Raymond M. Slattery, for the respondent.
David Vickers, for the Ministry of Labour for the Province of Ontario, Employment Standards Branch.

Solicitors for the appellants: Sack, Goldblatt, Mitchell, Toronto.
Solicitors for the respondent: Minden, Gross, Grafstein & Greenstein, Toronto.
Solicitor for the Ministry of Labour for the Province of Ontario, Employment Standards Branch: The Attorney General for Ontario, Toronto.

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The judgment of the Court was delivered by

1 **IACOBUCCI J.**:-- This is an appeal by the former employees of a now bankrupt employer from an order disallowing their claims for termination pay (including vacation pay thereon) and severance pay. The case turns on an issue of statutory interpretation. Specifically, the appeal decides whether, under the relevant legislation in effect at the time of the bankruptcy, employees are entitled to claim termination and severance payments where their employment has been terminated by reason of their employer's bankruptcy.

1. Facts

2 Prior to its bankruptcy, Rizzo & Rizzo Shoes Limited ("Rizzo") owned and operated a chain of retail shoe stores across Canada. Approximately 65 percent of those stores were located in Ontario. On April 13, 1989, a petition in bankruptcy was filed against the chain. The following day, a receiving order was made on consent in respect of Rizzo's property. Upon the making of that order, the employment of Rizzo's employees came to an end.

3 Pursuant to the receiving order, the respondent, Zittrer, Siblin & Associates, Inc. (the "Trustee") was appointed as trustee in bankruptcy of Rizzo's estate. The Bank of Nova Scotia privately appointed Peat Marwick Limited ("PML") as receiver and manager. By the end of July 1989, PML had liquidated Rizzo's property and assets and closed the stores. PML paid all wages, salaries, commissions and vacation pay that had been earned by Rizzo's employees up to the date on which the receiving order was made.

4 In November 1989, the Ministry of Labour for the Province of Ontario, Employment Standards Branch (the "Ministry") audited Rizzo's records to determine if there was any outstanding termination or severance pay owing to former employees under the Employment Standards Act, R.S.O. 1980, c. 137, as amended (the "ESA"). On August 23, 1990, the Ministry delivered a proof of claim to the respondent Trustee on behalf of the former employees of Rizzo for termination pay

and vacation pay thereon in the amount of approximately $2.6 million and for severance pay totalling $14,215. The Trustee disallowed the claims, issuing a Notice of Disallowance on January 28, 1991. For the purposes of this appeal, the relevant ground for disallowing the claim was the Trustee's opinion that the bankruptcy of an employer does not constitute a dismissal from employment and thus, no entitlement to severance, termination or vacation pay is created under the ESA.

**5** The Ministry appealed the Trustee's decision to the Ontario Court (General Division) which reversed the Trustee's disallowance and allowed the claims as unsecured claims provable in bankruptcy. On appeal, the Ontario Court of Appeal overturned the trial court's ruling and restored the decision of the Trustee. The Ministry sought leave to appeal from the Court of Appeal judgment, but discontinued its application on August 30, 1993. Following the discontinuance of the appeal, the Trustee paid a dividend to Rizzo's creditors, thereby leaving significantly less funds in the estate. Subsequently, the appellants, five former employees of Rizzo, moved to set aside the discontinuance, add themselves as parties to the proceedings, and requested an order granting them leave to appeal. This Court's order granting those applications was issued on December 5, 1996.

2. Relevant Statutory Provisions

**6** The relevant versions of the Bankruptcy Act (now the Bankruptcy and Insolvency Act) and the Employment Standards Act for the purposes of this appeal are R.S.C., 1985, c. B-3 (the "BA"), and R.S.O. 1980, c. 137, as amended to April 14, 1989 (the "ESA") respectively.

Employment Standards Act, R.S.O. 1980, c. 137, as amended:

> 7. --
>
> (5) Every contract of employment shall be deemed to include the following provision:
>
> > All severance pay and termination pay become payable and shall be paid by the employer to the employee in two weekly instalments beginning with the first full week following termination of employment and shall be allocated to such weeks accordingly. This provision does not apply to severance pay if the employee has elected to maintain a right of recall as provided in subsection 40a (7) of the Employment Standards Act.
>
> 40. -- (1) No employer shall terminate the employment of an employee who has been employed for three months or more unless the employee gives,
>
> (a) one weeks notice in writing to the employee if his or her period of employment is less than one year;
> (b) two weeks notice in writing to the employee if his or her period of employment is one year or more but less than three years;
> (c) three weeks notice in writing to the employee if his or her period of employment is three years or more but less than four years;
> (d) four weeks notice in writing to the employee if his or her period of employment is four years or more but less than five years;

(e) five weeks notice in writing to the employee if his or her period of employment is five years or more but less than six years;
(f) six weeks notice in writing to the employee if his or her period of employment is six years or more but less than seven years;
(g) seven weeks notice in writing to the employee if his or her period of employment is seven years or more but less than eight years;
(h) eight weeks notice in writing to the employee if his or her period of employment is eight years or more,

and such notice has expired.

. . .

(7) Where the employment of an employee is terminated contrary to this section,

(a) the employer shall pay termination pay in an amount equal to the wages that the employee would have been entitled to receive at his regular rate for a regular non-overtime work week for the period of notice prescribed by subsection (1) or (2), and any wages to which he is entitled;

. . .

40a . . .

(1a) Where,

(a) fifty or more employees have their employment terminated by an employer in a period of six months or less and the terminations are caused by the permanent discontinuance of all or part of the business of the employer at an establishment; or
(b) one or more employees have their employment terminated by an employer with a payroll of $2.5 million or more,

the employer shall pay severance pay to each employee whose employment has been terminated and who has been employed by the employer for five or more years.

Employment Standards Amendment Act, 1981, S.O. 1981, c. 22

2.--(1) Part XII of the said Act is amended by adding thereto the following section:

. . .

(3) Section 40a of the said Act does not apply to an employer who became a bankrupt or an insolvent person within the meaning of the Bankruptcy Act (Canada) and whose assets have been distributed

among his creditors or to an employer whose proposal within the meaning of the Bankruptcy Act (Canada) has been accepted by his creditors in the period from and including the 1st day of January, 1981, to and including the day immediately before the day this Act receives Royal Assent.

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

121. (1) All debts and liabilities, present or future, to which the bankrupt is subject at the date of the bankruptcy or to which he may become subject before his discharge by reason of any obligation incurred before the date of the bankruptcy shall be deemed to be claims provable in proceedings under this Act.

Interpretation Act, R.S.O. 1990, c. I.11

10. Every Act shall be deemed to be remedial, whether its immediate purport is to direct the doing of anything that the Legislature deems to be for the public good or to prevent or punish the doing of any thing that it deems to be contrary to the public good, and shall accordingly receive such fair, large and liberal construction and interpretation as will best ensure the attainment of the object of the Act according to its true intent, meaning and spirit.

. . .

17. The repeal or amendment of an Act shall be deemed not to be or to involve any declaration as to the previous state of the law.

3. Judicial History

A. Ontario Court (General Division) (1991), 6 O.R. (3d) 441

**7** Having disposed of several issues which do not arise on this appeal, Farley J. turned to the question of whether termination pay and severance pay are provable claims under the BA. Relying on U.F.C.W., Loc. 617P v. Royal Dressed Meats Inc. (Trustee of) (1989), 76 C.B.R. (N.S.) 86 (Ont. S.C. in Bankruptcy), he found that it is clear that claims for termination and severance pay are provable in bankruptcy where the statutory obligation to provide such payments arose prior to the bankruptcy. Accordingly, he reasoned that the essential matter to be resolved in the case at bar was whether bankruptcy acted as a termination of employment thereby triggering the termination and severance pay provisions of the ESA such that liability for such payments would arise on bankruptcy as well.

**8** In addressing this question, Farley J. began by noting that the object and intent of the ESA is to provide minimum employment standards and to benefit and protect the interests of employees. Thus, he concluded that the ESA is remedial legislation and as such it should be interpreted in a fair, large and liberal manner to ensure that its object is attained according to its true meaning, spirit and intent.

**9** Farley J. then held that denying employees in this case the right to claim termination and severance pay would lead to the arbitrary and unfair result that an employee whose employment is ter-

minated just prior to a bankruptcy would be entitled to termination and severance pay, whereas one whose employment is terminated by the bankruptcy itself would not have that right. This result, he stated, would defeat the intended working of the ESA.

**10** Farley J. saw no reason why the claims of the employees in the present case would not generally be contemplated as wages or other claims under the BA. He emphasized that the former employees in the case at bar had not alleged that termination pay and severance pay should receive a priority in the distribution of the estate, but merely that they are provable (unsecured and unpreferred) claims in a bankruptcy. For this reason, he found it inappropriate to make reference to authorities whose focus was the interpretation of priority provisions in the BA.

**11** Even if bankruptcy does not terminate the employment relationship so as to trigger the ESA termination and severance pay provisions, Farley J. was of the view that the employees in the instant case would nevertheless be entitled to such payments as these were liabilities incurred prior to the date of the bankruptcy by virtue of s. 7(5) of the ESA. He found that s. 7(5) deems every employment contract to include a provision to provide termination and severance pay following the termination of employment and concluded that a contingent obligation is thereby created for a bankrupt employer to make such payments from the outset of the relationship, long before the bankruptcy.

**12** Farley J. also considered s. 2(3) of the Employment Standards Amendment Act, 1981, S.O. 1981, c. 22 (the "ESAA"), which is a transitional provision that exempted certain bankrupt employers from the newly introduced severance pay obligations until the amendments received royal assent. He was of the view that this provision would not have been necessary if the obligations of employers upon termination of employment had not been intended to apply to bankrupt employers under the ESA. Farley J. concluded that the claim by Rizzo's former employees for termination pay and severance pay could be provided as unsecured and unpreferred debts in a bankruptcy. Accordingly, he allowed the appeal from the decision of the Trustee.

B. Ontario Court of Appeal (1995), 22 O.R. (3d) 385

**13** Austin J.A., writing for a unanimous court, began his analysis of the principal issue in this appeal by focussing upon the language of the termination pay and severance pay provisions of the ESA. He noted, at p. 390, that the termination pay provisions use phrases such as "[n]o employer shall terminate the employment of an employee" (s. 40(1)), "the notice required by an employer to terminate the employment" (s. 40(2)), and "[a]n employer who has terminated or who proposes to terminate the employment of employees" (s. 40(5)). Turning to severance pay, he quoted s. 40a(1)(a) (at p. 391) which includes the phrase "employees have their employment terminated by an employer". Austin J.A. concluded that this language limits the obligation to provide termination and severance pay to situations in which the employer terminates the employment. The operation of the ESA, he stated, is not triggered by the termination of employment resulting from an act of law such as bankruptcy.

**14** In support of his conclusion, Austin J.A. reviewed the leading cases in this area of law. He cited Re Malone Lynch Securities Ltd., [1972] 3 O.R. 725 (S.C. in bankruptcy), wherein Houlden J. (as he then was) concluded that the ESA termination pay provisions were not designed to apply to a bankrupt employer. He also relied upon Re Kemp Products Ltd. (1978), 27 C.B.R. (N.S.) 1 (Ont. S.C. in bankruptcy), for the proposition that the bankruptcy of a company at the instance of a creditor does not constitute dismissal. He concluded as follows at p. 395:

> The plain language of ss. 40 and 40a does not give rise to any liability to pay termination or severance pay except where the employment is terminated by the employer. In our case, the employment was terminated, not by the employer, but by the making of a receiving order against Rizzo on April 14, 1989, following a petition by one of its creditors. No entitlement to either termination or severance pay ever arose.

**15** Regarding s. 7(5) of the ESA, Austin J.A. rejected the trial judge's interpretation and found that the section does not create a liability. Rather, in his opinion, it merely states when a liability otherwise created is to be paid and therefore it was not considered relevant to the issue before the court. Similarly, Austin J.A. did not accept the lower court's view of s. 2(3), the transitional provision in the ESAA. He found that that section had no effect upon the intention of the Legislature as evidenced by the terminology used in ss. 40 and 40a.

**16** Austin J.A. concluded that, because the employment of Rizzo's former employees was terminated by the order of bankruptcy and not by the act of the employer, no liability arose with respect to termination, severance or vacation pay. The order of the trial judge was set aside and the Trustee's disallowance of the claims was restored.

## 4. Issues

**17** This appeal raises one issue: does the termination of employment caused by the bankruptcy of an employer give rise to a claim provable in bankruptcy for termination pay and severance pay in accordance with the provisions of the ESA?

## 5. Analysis

**18** The statutory obligation upon employers to provide both termination pay and severance pay is governed by ss. 40 and 40a of the ESA, respectively. The Court of Appeal noted that the plain language of those provisions suggests that termination pay and severance pay are payable only when the employer terminates the employment. For example, the opening words of s. 40(1) are: "No employer shall terminate the employment of an employee. . . ." Similarly, s. 40a(1a) begins with the words, "Where . . . fifty or more employees have their employment terminated by an employer. . . ." Therefore, the question on which this appeal turns is whether, when bankruptcy occurs, the employment can be said to be terminated "by an employer".

**19** The Court of Appeal answered this question in the negative, holding that, where an employer is petitioned into bankruptcy by a creditor, the employment of its employees is not terminated "by an employer", but rather by operation of law. Thus, the Court of Appeal reasoned that, in the circumstances of the present case, the ESA termination pay and severance pay provisions were not applicable and no obligations arose. In answer, the appellants submit that the phrase "terminated by an employer" is best interpreted as reflecting a distinction between involuntary and voluntary termination of employment. It is their position that this language was intended to relieve employers of their obligation to pay termination and severance pay when employees leave their jobs voluntarily. However, the appellants maintain that where an employee's employment is involuntarily terminated by reason of their employer's bankruptcy, this constitutes termination "by an employer" for the purpose of triggering entitlement to termination and severance pay under the ESA.

**20** At the heart of this conflict is an issue of statutory interpretation. Consistent with the findings of the Court of Appeal, the plain meaning of the words of the provisions here in question appears to restrict the obligation to pay termination and severance pay to those employers who have actively terminated the employment of their employees. At first blush, bankruptcy does not fit comfortably into this interpretation. However, with respect, I believe this analysis is incomplete.

**21** Although much has been written about the interpretation of legislation (see, e.g., Ruth Sullivan, Statutory Interpretation (1997); Ruth Sullivan, Driedger on the Construction of Statutes (3rd ed. 1994) (hereinafter "Construction of Statutes"); Pierre-André Côté, The Interpretation of Legislation in Canada (2nd ed. 1991)), Elmer Driedger in Construction of Statutes (2nd ed. 1983) best encapsulates the approach upon which I prefer to rely. He recognizes that statutory interpretation cannot be founded on the wording of the legislation alone. At p. 87 he states:

> 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.

Recent cases which have cited the above passage with approval include: R. v. Hydro-Québec, [1997] 1 S.C.R. 213; Royal Bank of Canada v. Sparrow Electric Corp., [1997] 1 S.C.R. 411; Verdun v. Toronto-Dominion Bank, [1996] 3 S.C.R. 550; Friesen v. Canada, [1995] 3 S.C.R. 103.

**22** I also rely upon s. 10 of the Interpretation Act, R.S.O. 1980, c. 219, which provides that every Act "shall be deemed to be remedial" and directs that every Act shall "receive such fair, large and liberal construction and interpretation as will best ensure the attainment of the object of the Act according to its true intent, meaning and spirit".

**23** Although the Court of Appeal looked to the plain meaning of the specific provisions in question in the present case, with respect, I believe that the court did not pay sufficient attention to the scheme of the ESA, its object or the intention of the legislature; nor was the context of the words in issue appropriately recognized. I now turn to a discussion of these issues.

**24** In Machtinger v. HOJ Industries Ltd., [1992] 1 S.C.R. 986, at p. 1002, the majority of this Court recognized the importance that our society accords to employment and the fundamental role that it has assumed in the life of the individual. The manner in which employment can be terminated was said to be equally important (see also Wallace v. United Grain Growers Ltd., [1997] 3 S.C.R. 701). It was in this context that the majority in Machtinger described, at p. 1003, the object of the ESA as being the protection of ". . . the interests of employees by requiring employers to comply with certain minimum standards, including minimum periods of notice of termination". Accordingly, the majority concluded, at p. 1003, that, ". . . an interpretation of the Act which encourages employers to comply with the minimum requirements of the Act, and so extends its protections to as many employees as possible, is to be favoured over one that does not".

**25** The objects of the termination and severance pay provisions themselves are also broadly premised upon the need to protect employees. Section 40 of the ESA requires employers to give their employees reasonable notice of termination based upon length of service. One of the primary purposes of this notice period is to provide employees with an opportunity to take preparatory measures and seek alternative employment. It follows that s. 40(7)(a), which provides for termination pay in lieu of notice when an employer has failed to give the required statutory notice, is in-

tended to "cushion" employees against the adverse effects of economic dislocation likely to follow from the absence of an opportunity to search for alternative employment. (Innis Christie, Geoffrey England and Brent Cotter, Employment Law in Canada (2nd ed. 1993), at pp. 572-81.)

**26** Similarly, s. 40a, which provides for severance pay, acts to compensate long-serving employees for their years of service and investment in the employer's business and for the special losses they suffer when their employment terminates. In R. v. TNT Canada Inc. (1996), 27 O.R. (3d) 546, Robins J.A. quoted with approval at pp. 556-57 from the words of D. D. Carter in the course of an employment standards determination in Re Telegram Publishing Co. v. Zwelling (1972), 1 L.A.C. (2d) 1 (Ont.), at p. 19, wherein he described the role of severance pay as follows:

> Severance pay recognizes that an employee does make an investment in his employer's business -- the extent of this investment being directly related to the length of the employee's service. This investment is the seniority that the employee builds up during his years of service. . . . Upon termination of the employment relationship, this investment of years of service is lost, and the employee must start to rebuild seniority at another place of work. The severance pay, based on length of service, is some compensation for this loss of investment.

**27** In my opinion, the consequences or effects which result from the Court of Appeal's interpretation of ss. 40 and 40a of the ESA are incompatible with both the object of the Act and with the object of the termination and severance pay provisions themselves. It is a well established principle of statutory interpretation that the legislature does not intend to produce absurd consequences. According to Côté, supra, an interpretation can be considered absurd if it leads to ridiculous or frivolous consequences, if it is extremely unreasonable or inequitable, if it is illogical or incoherent, or if it is incompatible with other provisions or with the object of the legislative enactment (at pp. 378-80). Sullivan echoes these comments noting that a label of absurdity can be attached to interpretations which defeat the purpose of a statute or render some aspect of it pointless or futile (Sullivan, Construction of Statutes, supra, at p. 88).

**28** The trial judge properly noted that, if the ESA termination and severance pay provisions do not apply in circumstances of bankruptcy, those employees "fortunate" enough to have been dismissed the day before a bankruptcy would be entitled to such payments, but those terminated on the day the bankruptcy becomes final would not be so entitled. In my view, the absurdity of this consequence is particularly evident in a unionized workplace where seniority is a factor in determining the order of lay-off. The more senior the employee, the larger the investment he or she has made in the employer and the greater the entitlement to termination and severance pay. However, it is the more senior personnel who are likely to be employed up until the time of the bankruptcy and who would thereby lose their entitlements to these payments.

**29** If the Court of Appeal's interpretation of the termination and severance pay provisions is correct, it would be acceptable to distinguish between employees merely on the basis of the timing of their dismissal. It seems to me that such a result would arbitrarily deprive some employees of a means to cope with the economic dislocation caused by unemployment. In this way the protections of the ESA would be limited rather than extended, thereby defeating the intended working of the legislation. In my opinion, this is an unreasonable result.

**30** In addition to the termination and severance pay provisions, both the appellants and the respondent relied upon various other sections of the ESA to advance their arguments regarding the

intention of the legislature. In my view, although the majority of these sections offer little interpretive assistance, one transitional provision is particularly instructive. In 1981, s. 2(1) of the ESAA introduced s. 40a, the severance pay provision, to the ESA. Section 2(2) deemed that provision to come into force on January 1, 1981. Section 2(3), the transitional provision in question provided as follows:

> 2. . . .
>
> (3) Section 40a of the said Act does not apply to an employer who became a bankrupt or an insolvent person within the meaning of the Bankruptcy Act (Canada) and whose assets have been distributed among his creditors or to an employer whose proposal within the meaning of the Bankruptcy Act (Canada) has been accepted by his creditors in the period from and including the 1st day of January, 1981, to and including the day immediately before the day this Act receives Royal Assent.

**31** The Court of Appeal found that it was neither necessary nor appropriate to determine the intention of the legislature in enacting this provisional subsection. Nevertheless, the court took the position that the intention of the legislature as evidenced by the introductory words of ss. 40 and 40a was clear, namely, that termination by reason of a bankruptcy will not trigger the severance and termination pay obligations of the ESA. The court held that this intention remained unchanged by the introduction of the transitional provision. With respect, I do not agree with either of these findings. Firstly, in my opinion, the use of legislative history as a tool for determining the intention of the legislature is an entirely appropriate exercise and one which has often been employed by this Court (see, e.g., R. v. Vasil, [1981] 1 S.C.R. 469, at p. 487; Paul v. The Queen, [1982] 1 S.C.R. 621, at pp. 635, 653 and 660). Secondly, I believe that the transitional provision indicates that the Legislature intended that termination and severance pay obligations should arise upon an employers' bankruptcy.

**32** In my view, by extending an exemption to employers who became bankrupt and lost control of their assets between the coming into force of the amendment and its receipt of royal assent, s. 2(3) necessarily implies that the severance pay obligation does in fact extend to bankrupt employers. It seems to me that, if this were not the case, no readily apparent purpose would be served by this transitional provision.

**33** I find support for my conclusion in the decision of Saunders J. in Royal Dressed Meats Inc., supra. Having reviewed s. 2(3) of the ESAA, he commented as follows (at p. 89):

> . . . any doubt about the intention of the Ontario Legislature has been put to rest, in my opinion, by the transitional provision which introduced severance payments into the E.S.A. . . . it seems to me an inescapable inference that the legislature intended liability for severance payments to arise on a bankruptcy. That intention would, in my opinion, extend to termination payments which are similar in character.

**34** This interpretation is also consistent with statements made by the Minister of Labour at the time he introduced the 1981 amendments to the ESA. With regard to the new severance pay provision he stated:

> The circumstances surrounding a closure will govern the applicability of the severance pay legislation in some defined situations. For example, a bankrupt or insolvent firm will still be required to pay severance pay to employees to the extent that assets are available to satisfy their claims.
>
> . . .
>
> . . . the proposed severance pay measures will, as I indicated earlier, be retroactive to January 1 of this year. That retroactive provision, however, will not apply in those cases of bankruptcy and insolvency where the assets have already been distributed or where an agreement on a proposal to creditors has already been reached.
>
> (Legislature of Ontario Debates, 1st sess., 32nd Parl., June 4, 1981, at pp. 1236-37.)

Moreover, in the legislative debates regarding the proposed amendments the Minister stated:

> For purposes of retroactivity, severance pay will not apply to bankruptcies under the Bankruptcy Act where assets have been distributed. However, once this act receives royal assent, employees in bankruptcy closures will be covered by the severance pay provisions.
>
> (Legislature of Ontario Debates, 1st sess., 32nd Parl., June 16, 1981, at p. 1699.)

**35** Although the frailties of Hansard evidence are many, this Court has recognized that it can play a limited role in the interpretation of legislation. Writing for the Court in R. v. Morgentaler, [1993] 3 S.C.R. 463, at p. 484, Sopinka J. stated:

> . . . until recently the courts have balked at admitting evidence of legislative debates and speeches. . . . The main criticism of such evidence has been that it cannot represent the "intent" of the legislature, an incorporeal body, but that is equally true of other forms of legislative history. Provided that the court remains mindful of the limited reliability and weight of Hansard evidence, it should be admitted as relevant to both the background and the purpose of legislation.

**36** Finally, with regard to the scheme of the legislation, since the ESA is a mechanism for providing minimum benefits and standards to protect the interests of employees, it can be characterized as benefits-conferring legislation. As such, according to several decisions of this Court, it ought to be interpreted in a broad and generous manner. Any doubt arising from difficulties of language should be resolved in favour of the claimant (see, e.g., Abrahams v. Attorney General of Canada, [1983] 1 S.C.R. 2, at p. 10; Hills v. Canada (Attorney General), [1988] 1 S.C.R. 513, at p. 537). It seems to me that, by limiting its analysis to the plain meaning of ss. 40 and 40a of the ESA,

the Court of Appeal adopted an overly restrictive approach that is inconsistent with the scheme of the Act.

**37** The Court of Appeal's reasons relied heavily upon the decision in Malone Lynch, supra. In Malone Lynch, Houlden J. held that s. 13, the group termination provision of the former ESA, R.S.O. 1970, c. 147, and the predecessor to s. 40 at issue in the present case, was not applicable where termination resulted from the bankruptcy of the employer. Section 13(2) of the ESA then in force provided that, if an employer wishes to terminate the employment of 50 or more employees, the employer must give notice of termination for the period prescribed in the regulations, "and until the expiry of such notice the terminations shall not take effect". Houlden J. reasoned that termination of employment through bankruptcy could not trigger the termination payment provision, as employees in this situation had not received the written notice required by the statute, and therefore could not be said to have been terminated in accordance with the Act.

**38** Two years after Malone Lynch was decided, the 1970 ESA termination pay provisions were amended by The Employment Standards Act, 1974, S.O. 1974, c. 112. As amended, s. 40(7) of the 1974 ESA eliminated the requirement that notice be given before termination can take effect. This provision makes it clear that termination pay is owing where an employer fails to give notice of termination and that employment terminates irrespective of whether or not proper notice has been given. Therefore, in my opinion it is clear that the Malone Lynch decision turned on statutory provisions which are materially different from those applicable in the instant case. It seems to me that Houlden J.'s holding goes no further than to say that the provisions of the 1970 ESA have no application to a bankrupt employer. For this reason, I do not accept the Malone Lynch decision as persuasive authority for the Court of Appeal's findings. I note that the courts in Royal Dressed Meats, supra, and British Columbia (Director of Employment Standards) v. Eland Distributors Ltd. (Trustee of) (1996), 40 C.B.R. (3d) 25 (B.C.S.C.), declined to rely upon Malone Lynch based upon similar reasoning.

**39** The Court of Appeal also relied upon Re Kemp Products Ltd., supra, for the proposition that although the employment relationship will terminate upon an employer's bankruptcy, this does not constitute a "dismissal". I note that this case did not arise under the provisions of the ESA. Rather, it turned on the interpretation of the term "dismissal" in what the complainant alleged to be an employment contract. As such, I do not accept it as authoritative jurisprudence in the circumstances of this case. For the reasons discussed above, I also disagree with the Court of Appeal's reliance on Mills-Hughes v. Raynor (1988), 63 O.R. (2d) 343 (C.A.), which cited the decision in Malone Lynch, supra, with approval.

**40** As I see the matter, when the express words of ss. 40 and 40a of the ESA are examined in their entire context, there is ample support for the conclusion that the words "terminated by the employer" must be interpreted to include termination resulting from the bankruptcy of the employer. Using the broad and generous approach to interpretation appropriate for benefits-conferring legislation, I believe that these words can reasonably bear that construction (see R. v. Z. (D.A.), [1992] 2 S.C.R. 1025). I also note that the intention of the Legislature as evidenced in s. 2(3) of the ESAA, clearly favours this interpretation. Further, in my opinion, to deny employees the right to claim ESA termination and severance pay where their termination has resulted from their employer's bankruptcy, would be inconsistent with the purpose of the termination and severance pay provisions and would undermine the object of the ESA, namely, to protect the interests of as many employees as possible.

**41** In my view, the impetus behind the termination of employment has no bearing upon the ability of the dismissed employee to cope with the sudden economic dislocation caused by unemployment. As all dismissed employees are equally in need of the protections provided by the ESA, any distinction between employees whose termination resulted from the bankruptcy of their employer and those who have been terminated for some other reason would be arbitrary and inequitable. Further, I believe that such an interpretation would defeat the true meaning, intent and spirit of the ESA. Therefore, I conclude that termination as a result of an employer's bankruptcy does give rise to an unsecured claim provable in bankruptcy pursuant to s. 121 of the BA for termination and severance pay in accordance with ss. 40 and 40a of the ESA. Because of this conclusion, I do not find it necessary to address the alternative finding of the trial judge as to the applicability of s. 7(5) of the ESA.

**42** I note that subsequent to the Rizzo bankruptcy, the termination and severance pay provisions of the ESA underwent another amendment. Sections 74(1) and 75(1) of the Labour Relations and Employment Statute Law Amendment Act, 1995, S.O. 1995, c. 1, amend those provisions so that they now expressly provide that where employment is terminated by operation of law as a result of the bankruptcy of the employer, the employer will be deemed to have terminated the employment. However, s. 17 of the Interpretation Act directs that, "[t]he repeal or amendment of an Act shall be deemed not to be or to involve any declaration as to the previous state of the law". As a result, I note that the subsequent change in the legislation has played no role in determining the present appeal.

## 6. Disposition and Costs

**43** I would allow the appeal and set aside paragraph 1 of the order of the Court of Appeal. In lieu thereof, I would substitute an order declaring that Rizzo's former employees are entitled to make claims for termination pay (including vacation pay due thereon) and severance pay as unsecured creditors. As to costs, the Ministry of Labour led no evidence regarding what effort it made in notifying or securing the consent of the Rizzo employees before it discontinued its application for leave to appeal to this Court on their behalf. In light of these circumstances, I would order that the costs in this Court be paid to the appellant by the Ministry on a party-and-party basis. I would not disturb the orders of the courts below with respect to costs.

cp/d/hbb/DRS/DRS

# Tab 14

*Indexed as:*

# Non-Marine Underwriters, Lloyd's of London v. Scalera

**Vincent Scalera, appellant;**
**v.**
**M. J. Oppenheim in his quality as Attorney in Canada for the Non-Marine Underwriters, members of Lloyd's of London, respondent.**

[2000] 1 S.C.R. 551

[2000] S.C.J. No. 26

2000 SCC 24

File No.: 26695

Supreme Court of Canada

1999: October 14 / 2000: May 3.

**Present: L'Heureux-Dubé, Gonthier, McLachlin, Iacobucci, Major, Bastarache and Binnie JJ.**

ON APPEAL FROM THE BRITISH COLUMBIA COURT OF APPEAL (139 paras.)

*Insurance -- Homeowner's insurance -- Insurer's duty to defend -- Plaintiff bringing action against insured alleging battery, negligent battery, negligent misrepresentation and breach of fiduciary duty -- Policy containing exclusion for intentional acts of insured -- Whether insurer has a duty to defend.*

*Torts -- Intentional torts -- Battery -- Evidence -- Burden of proof -- Consent -- Whether plaintiff must prove lack of consent.*

In 1996, a plaintiff brought a civil action against five B.C. Transit bus drivers, including the appellant, arising out of various alleged sexual assaults between 1988 and 1992. The allegations included battery, negligent battery, negligent misrepresentation and breach of fiduciary duty. The appellant owned a homeowner's insurance policy issued by the respondent insurer. The policy provided coverage for "compensatory damage because of bodily injury" arising from the insured's personal ac-

tions, excepting "bodily injury or property damage caused by any intentional or criminal act". The British Columbia Supreme Court dismissed the respondent's request for a declaration that it not be required to defend [page552] the appellant against the plaintiff's claims. The Court of Appeal allowed the respondent's appeal.

Held: The appeal should be dismissed.

Per L'Heureux-Dubé, Gonthier, McLachlin and Binnie JJ.: The plaintiff's claims could not trigger coverage under the policy. Accordingly, the respondent has no duty to defend. While there is substantial agreement with Iacobucci J.'s reasoning, his approach to the tort of battery in the sexual context is disagreed with. In the tort of sexual battery, consent operates as a defence and must be proven by the defendant. The plaintiff is not required to prove that the defendant either knew that she was not consenting or that a reasonable person in the defendant's position would have known that she was not consenting.

The traditional rights-based approach to the law of battery that is now the law of Canada should not be set aside lightly. The tort of battery is a form of trespass against the person and is aimed at protecting the personal autonomy of the individual. Its purpose is to recognize the right of each person to control his or her body and who touches it, and to permit damages where this right is violated. The compensation stems not from fault, but from violation of the right to personal autonomy. When a person interferes with the body of another, a prima facie case of violation of the plaintiff's autonomy is made out. The law may then fairly call upon the person thus implicated to explain, or raise some defence, such as the defence of consent. If he can show that he acted with consent, the prima facie violation is negated and the plaintiff's claim will fail. But it is not up to the plaintiff to prove that, in addition to directly interfering with her body, the defendant was also at fault. Unlike negligence, where the requirement of fault can be justified because the tortious sequence may be complicated, trespass to the person is confined to direct interferences. Where the trespass causes actual injury to the plaintiff, there is a direct connection between the defendant's action and the plaintiff's injury. The traditional approach to trespass is also practical, since, if the defendant is in a position to say what happened, it is both sensible and just to give him an incentive to do so by putting the burden of explanation on him. In addition, the close causal relationship between the defendant's conduct and the violation of the plaintiff's bodily integrity, the identification of the loss with the plaintiff's personality and freedom, the infliction of the loss in isolated (as opposed to systemic) circumstances, and [page553] the perception of the defendant's conduct as anti-social all support the legal position that once the direct interference with the plaintiff's person is shown, the defendant may fairly be called upon to explain his behaviour if indeed it was innocent.

Therefore, while a plaintiff generally must prove all elements of the tort she alleges, the fact that contact must be harmful or offensive to constitute battery does not mean that the plaintiff must prove that she did not consent and that the defendant actually or constructively knew she did not consent to sexual contact. When it is accepted that the foundation of the tort of battery is a violation of personal autonomy, all contact outside the exceptional category of contact that is generally accepted or expected in the course of ordinary life is prima facie offensive. Since sexual contact is not generally accepted or expected in the course of ordinary activities, the plaintiff may establish an action for sexual battery without negativing actual or constructive consent. Nothing special about sexual battery justifies requiring the plaintiff to prove that she did not consent or that the defendant either knew or ought to have known that she did not consent.

The exclusion clause in the policy must be interpreted as requiring an intent to injure. Where there is an allegation of sexual battery, courts will conclude as a matter of legal inference that the defendant intended harm for the purpose of construing exemptions of insurance coverage for intentional injury.

It is unnecessary to comment on the relationship between battery and negligence.

Per Iacobucci, Major and Bastarache JJ.: The respondent has no duty to defend the appellant because the plaintiff's statement of claim makes no allegation that could potentially give rise to indemnity under the insurance contract.

An insurer only has a duty to defend when a lawsuit against the insured raises a claim that could potentially [page554] fall within coverage. The insurer's duty to defend is related to its duty to indemnify. Therefore if an insurance policy, like the one in this case, excludes liability arising from intentionally caused injuries, there will be no duty to defend actions based on such injuries.

A three-step process must be applied to determine whether a claim could trigger indemnity. First, a court should determine which of the plaintiff's legal allegations are properly pleaded. In doing so, courts are not bound by the legal labels chosen by the plaintiff. A plaintiff cannot change an intentional tort into a negligent one simply by choice of words, or vice versa. Therefore, when ascertaining the scope of the duty to defend, a court must look beyond the choice of labels, and examine the substance of the allegations contained in the pleadings. This does not involve deciding whether the claims have any merit; all a court must do is decide, based on the pleadings, the true nature of the claims.

At the second stage, the court should determine if any claims are entirely derivative in nature. The duty to defend will not be triggered simply because a claim can be cast in terms of both negligence and intentional tort. A claim for negligence will not be derivative if the underlying elements of the negligence and of the intentional tort are sufficiently disparate to render the two claims unrelated. However, if both the negligence and intentional tort claims arise from the same actions and cause the same harm, the negligence claim is derivative, and it will be subsumed into the intentional tort for the purposes of the exclusion clause analysis. If neither claim is derivative, the claim of negligence will survive and the duty to defend will apply. Finally, at the third stage, the court must decide whether any of the properly pleaded, non-derivative claims could potentially trigger the insurer's duty to defend. This appeal's holding with respect to the proper characterization of a plaintiff's tort allegations should not be taken to affect any areas of law outside the insurance context presented by this appeal.

In this case, the exclusion clause must be read to require that the injuries be intentionally caused, in that they must be the product of an intentional tort and not of negligence. The plaintiff has stated three possible claims arising out of the alleged sexual assaults: sexual battery, negligent battery, and breach of fiduciary duty. Sexual [page555] battery requires the plaintiff to prove that a reasonable person should have known that the plaintiff did not validly consent to the sexual activity in question. Since non-consensual sexual activity is inherently harmful, any injuries resulting therefrom are intentionally caused, and the exclusion clause would apply. If a reasonable person would not have known that the plaintiff did not validly consent, the plaintiff's claim will fail, and there will be no duty to indemnify or duty to defend. The plaintiff's claims of negligence and breach of fiduciary duty are either not properly pleaded or are subsumed into the sexual battery because these claims are based on the same facts and resulted in the same harm. Therefore the exclusion clause applies

equally to them. There being no potentially indemnifiable claim, the respondent has no duty to defend.

**Cases Cited**

By McLachlin J.

Referred to: Collins v. Wilcock, [1984] 3 All E.R. 374; Cook v. Lewis, [1951] S.C.R. 830; Larin v. Goshen (1974), 56 D.L.R. (3d) 719; Walmsley v. Humenick, [1954] 2 D.L.R. 232; Tillander v. Gosselin (1966), 60 D.L.R. (2d) 18, aff'd (1967), 61 D.L.R. (2d) 192; Dahlberg v. Naydiuk (1969), 10 D.L.R. (3d) 319; Ellison v. Rogers (1967), 67 D.L.R. (2d) 21; Reibl v. Hughes, [1980] 2 S.C.R. 880; Norberg v. Wynrib, [1992] 2 S.C.R. 226; Scott v. Shepherd (1773), 2 Black. W. 892, 96 E.R. 525; Leame v. Bray (1803), 3 East 593, 102 E.R. 724; Fowler v. Lanning, [1959] 1 Q.B. 426; Letang v. Cooper, [1965] 1 Q.B. 232; Bell Canada v. COPE (Sarnia) Ltd. (1980), 11 C.C.L.T. 170, aff'd (1980), 31 O.R. (2d) 571; Cole v. Turner (1704), 6 Mod. 149, 87 E.R. 907; Stewart v. Stonehouse, [1926] 2 D.L.R. 683; In re F., [1990] 2 A.C. 1; M. (K.) v. M. (H.), [1992] 3 S.C.R. 6; Freeman v. Home Office, [1983] 3 All E.R. 589, aff'd [1984] 1 All E.R. 1036; H. v. R., [1996] 1 N.Z.L.R. 299; Pursell v. Horn (1838), 8 AD. & E. 602, 112 E.R. 966; Green v. Goddard (1704), 2 Salkeld 641, 91 E.R. 540; Humphries v. Connor (1864), 17 Ir. Com. L. Rep. 1; Forde v. Skinner (1830), 4 Car. & P. 239, 172 E.R. 687; Schweizer v. Central Hospital (1974), 53 D.L.R. (3d) 494; Allan v. New Mount Sinai Hospital (1980), 109 D.L.R. (3d) 634, rev'd on other grounds (1981), 33 O.R. (2d) 603; Brushett v. Cowan (1990), 3 C.C.L.T. (2d) 195; [page556] O'Bonsawin v. Paradis (1993), 15 C.C.L.T. (2d) 188; State Farm Fire and Casualty Co. v. Williams, 355 N.W.2d 421 (1984).

By Iacobucci J.

Referred to: Sansalone v. Wawanesa Mutual Insurance Co., [2000] 1 S.C.R. 627, 2000 SCC 25; Brissette Estate v. Westbury Life Insurance Co., [1992] 3 S.C.R. 87; Wigle v. Allstate Insurance Co. of Canada (1984), 49 O.R. (2d) 101; Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co., [1993] 1 S.C.R. 252; Indemnity Insurance Co. of North America v. Excel Cleaning Service, [1954] S.C.R. 169; Parsons v. Standard Fire Insurance Co. (1880), 5 S.C.R. 233; Scott v. Wawanesa Mutual Insurance Co., [1989] 1 S.C.R. 1445; Consolidated-Bathurst Export Ltd. v. Mutual Boiler and Machinery Insurance Co., [1980] 1 S.C.R. 888; Guarantee Co. of North America v. Gordon Capital Corp., [1999] 3 S.C.R. 423; Nichols v. American Home Assurance Co., [1990] 1 S.C.R. 801; Conner v. Transamerica Insurance Co., 496 P.2d 770 (1972); Modern Livestock Ltd. v. Kansa General Insurance Co. (1993), 11 Alta. L.R. (3d) 355; B.P. Canada Inc. v. Comco Service Station Construction & Maintenance Ltd. (1990), 73 O.R. (2d) 317; Kates v. Hall, [1990] 5 W.W.R. 569; Colorado Farm Bureau Mutual Insurance Co. v. Snowbarger, 934 P.2d 909 (1997); Aerojet-General Corp. v. Transport Indemnity Co., 948 P.2d 909 (1997); Lawyers Title Insurance Corp. v. Knopf, 674 A.2d 65 (1996); Allstate Insurance Co. v. Patterson, 904 F. Supp. 1270 (1995); Allstate Insurance Co. v. Brown, 834 F. Supp. 854 (1993); Gray v. Zurich Insurance Co., 419 P.2d 168 (1966); Bacon v. McBride (1984), 6 D.L.R. (4th) 96; Peerless Insurance Co. v. Viegas, 667 A.2d 785 (1995); Houg v. State Farm Fire and Casualty Co., 481 N.W.2d 393 (1992); Linebaugh v. Berdish, 376 N.W.2d 400 (1985); Horace Mann Insurance Co. v. Leeber, 376 S.E.2d 581 (1988); Allstate Insurance Co. v. Troelstrup, 789 P.2d 415 (1990); Nationwide Mutual Fire Insurance Co. v. Lajoie, 661 A.2d 85 (1995); M. (K.) v. M. (H.), [1992] 3 S.C.R. 6; Canadian Indemnity Co. v. Walkem Machinery & Equipment Ltd., [1976] 1 S.C.R. 309; Wilson v. Pringle, [1986] 2 All E.R.

440; Spivey v. Battaglia, 258 So.2d 815 (1972); Bettel v. Yim (1978), 20 O.R. (2d) 617; Long v. Gardner (1983), 144 D.L.R. (3d) 73; Veinot v. Veinot (1977), 81 D.L.R. (3d) 549; Rumsey v. The Queen (1984), 12 D.L.R. (4th) 44; Holt v. Verbruggen (1981), 20 C.C.L.T. 29; Garratt v. Dailey, 279 P.2d 1091 (1955); Vosburg v. Putney, 50 N.W. 403 (1891); Reibl v. Hughes, [1980] 2 S.C.R. 880; Clayton v. New Dreamland Roller Skating Rink, Inc., 82 A.2d 458 (1951); [page557] Kirkpatrick v. Crutchfield, 100 S.E. 602 (1919); Cook v. Lewis, [1951] S.C.R. 830; Norberg v. Wynrib, [1992] 2 S.C.R. 226; Hambley v. Shepley (1967), 63 D.L.R. (2d) 94; Mandel v. The Permanent (1985), 7 O.A.C. 365; Wiffin v. Kincard (1807), 2 Bos. & Pul. (N.R.) 471, 127 E.R. 713; Coward v. Baddeley (1859), 4 H. & N. 478, 157 E.R. 927; Freeman v. Home Office, [1983] 3 All E.R. 589, aff'd [1984] 1 All E.R. 1036; H. v. R., [1996] 1 N.Z.L.R. 299; State Farm Fire and Casualty Co. v. Williams, 355 N.W.2d 421 (1984); R. v. Mills, [1999] 3 S.C.R. 668; R. v. Osolin, [1993] 4 S.C.R. 595; R. v. Seaboyer, [1991] 2 S.C.R. 577; R. v. Ewanchuck, [1999] 1 S.C.R. 330; M. (M.) v. K. (K.) (1989), 61 D.L.R. (4th) 392; Harder v. Brown (1989), 50 C.C.L.T. 85; Lyth v. Dagg (1988), 46 C.C.L.T. 25; R. v. McCraw, [1991] 3 S.C.R. 72; CNA Insurance Co. v. McGinnis, 666 S.W.2d 689 (1984); B.B. v. Continental Insurance Co., 8 F.3d 1288 (1993); J.C. Penney Casualty Insurance Co. v. M.K., 804 P.2d 689 (1991); State Farm Fire & Casualty Co. v. D.T.S., 867 S.W.2d 642 (1993); American States Insurance Co. v. Borbor, 826 F.2d 888 (1987); Troelstrup v. District Court, 712 P.2d 1010 (1986); Rodriguez v. Williams, 729 P.2d 627 (1986); Horace Mann Insurance Co. v. Independent School District No. 656, 355 N.W.2d 413 (1984); Altena v. United Fire and Casualty Co., 422 N.W.2d 485 (1988); Wilkieson-Valiente v. Wilkieson, [1996] I.L.R. para. 1-3551; Ellison v. Rogers (1967), 67 D.L.R. (2d) 21; Hatton v. Webb (1977), 81 D.L.R. (3d) 377; Co-operative Fire & Casualty Co. v. Saindon, [1976] 1 S.C.R. 735; Newcastle (Town) v. Mattatall (1988), 52 D.L.R. (4th) 356; Long Lake School Division No. 30 of Saskatchewan Board of Education v. Schatz (1986), 18 C.C.L.I. 232; Devlin v. Co-operative Fire & Casualty Co. (1978), 90 D.L.R. (3d) 444; Pistolesi v. Nationwide Mutual Fire Insurance Co., 644 N.Y.S.2d 819 (1996); M'Alister v. Stevenson, [1932] A.C. 562; Frame v. Smith, [1987] 2 S.C.R. 99; Rodriguez by Brennan v. Williams, 713 P.2d 135 (1986).

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APPEAL from a judgment of the British Columbia Court of Appeal (1998), 106 B.C.A.C. 268, 172 W.A.C. 268, 48 B.C.L.R. (3d) 143, 158 D.L.R. (4th) 385, 2 C.C.L.I. (3d) 1, [1998] I.L.R. para. 1-3568, [1998] 9 W.W.R. 209, [1998] B.C.J. No. 834 (QL), allowing an appeal from the British Columbia Supreme Court (1997), 47 B.C.L.R. (3d) 187, 49 C.C.L.I. (2d) 305, [1998] I.L.R. para. 1-3519, [1997] B.C.J. No. 2481 (QL). Appeal dismissed.

Bruce P. Cran and Murray G. Madryga, for the appellant. Eric A. Dolden and Karen F. W. Liang, for the respondent.

Solicitors for the appellant: Cran Law Offices, Vancouver.
Solicitors for the respondent: Dolden Walker Folick, Vancouver.

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The judgment of L'Heureux-Dubé, Gonthier, McLachlin and Binnie JJ. was delivered by

1 **McLACHLIN J.**:-- I have read the reasons of Iacobucci J. and agree with the result he reaches and with much of his reasoning. I would respectfully disagree, however, from the view that in the tort of sexual battery, the onus rests on the plaintiff to prove that the defendant either knew that she was not consenting or that a reasonable person in [page560] the defendant's position would have known that she was not consenting.

2 As Goff L.J. (as he then was) stated in Collins v. Wilcock, [1984] 3 All E.R. 374 (Q.B.), at p. 378, "[t]he fundamental principle, plain and incontestable, is that every person's body is inviolate". The law of battery protects this inviolability, and it is for those who violate the physical integrity of others to justify their actions. Accordingly, in my respectful view, the plaintiff who alleges sexual battery makes her case by tendering evidence of force applied directly to her. "Force", in the context of an allegation of sexual battery, simply refers to physical contact of a sexual nature, and is neutral in the sense of not necessarily connoting a lack of consent. If the defendant does not dispute that the contact took place, he bears the burden of proving that the plaintiff consented or that a reasonable person in his position would have thought that she consented. My reasons for so concluding are the following.

I. Analysis

A. The Canadian Law of Battery Places the Onus of Proving Consent on the Defendant

3 As Iacobucci J. states (at para. 103) "for traditional batteries, consent is conceived of as an affirmative defence that must be raised by the defendant".

4 This Court has long affirmed this proposition. In Cook v. Lewis, [1951] S.C.R. 830, at p. 839, Cartwright J. stated that "where a plaintiff is injured by force applied directly to him by the defendant his case is made by proving this fact and [page561] the onus falls upon the defendant to prove 'that such trespass was utterly without his fault'."

5 In Larin v. Goshen (1974), 56 D.L.R. (3d) 719 (N.S.C.A.), at p. 722, Macdonald J.A., citing numerous authorities, stated: "The law in Canada at present is this: In an action for damages in trespass where the plaintiff proves that he has been injured by the direct act of the defendant, the onus falls upon the defendant to prove that his act was both unintentional and without negligence on

his part, in order for him to be entitled to a dismissal of the action." (Emphasis in original.) See also Walmsley v. Humenick, [1954] 2 D.L.R. 232 (B.C.S.C.); Tillander v. Gosselin (1966), 60 D.L.R. (2d) 18 (Ont. H.C.), aff'd (1967), 61 D.L.R. (2d) 192 (Ont. C.A.); Dahlberg v. Naydiuk (1969), 10 D.L.R. (3d) 319 (Man. C.A.), and Ellison v. Rogers (1967), 67 D.L.R. (2d) 21 (Ont. H.C.). A number of academic commentators also agree that the burden of proving consent lies on the defence: see J. G. Fleming, The Law of Torts (9th ed. 1998), at p. 86; A. M. Linden and L. N. Klar, Canadian Tort Law: Cases, Notes and Materials (10th ed. 1994), at p. 102, note 2; and G. H. L. Fridman, The Law of Torts in Canada (1989), vol. 1, at p. 63.

**6** This proposition holds for particular forms of battery like medical battery and sexual battery. In Reibl v. Hughes, [1980] 2 S.C.R. 880, at p. 890, dealing with medical battery, Laskin C.J. stated for the Court that:

> The tort [of battery] is an intentional one, consisting of an unprivileged and unconsented to invasion of one's bodily security. True enough, it has some advantages for a plaintiff over an action of negligence since it does not require proof of causation and it casts upon the defendant the burden of proving consent to what was done.

And in Norberg v. Wynrib, [1992] 2 S.C.R. 226, dealing with sexual battery, La Forest J., for the plurality, stated, at p. 246, that "[a] battery is the intentional infliction of unlawful force on another person. Consent, express or implied, is a defence [page562] to battery." None of the members of the Court participating in the decision dissented from the view that the burden lies on the defendant to prove consent.

**7** The question, then, is whether we should in this case depart from the settled rule that requires the plaintiff in a battery case to show only contact through a direct, intentional act of the defendant and places the onus on the defendant of showing consent or lawful excuse, including actual or constructive consent. For the reasons that follow, I am not convinced that we should alter the established rule.

### B. The Traditional Approach to Trespass is Justified as a Rights-Based Tort

**8** The traditional rule, as noted, is that the plaintiff in an action for trespass to the person (which includes battery) succeeds if she can prove direct interference with her person. Interference is direct if it is the immediate consequence of a force set in motion by an act of the defendant: see Scott v. Shepherd (1773), 2 Black. W. 892, 96 E.R. 525 (K.B.); Leame v. Bray (1803), 3 East 593, 102 E.R. 724 (K.B.). The burden is then on the defendant to allege and prove his defence. Consent is one such defence.

**9** Some critics have suggested that this rule should be altered. They suggest that tort must always be fault-based. This means the plaintiff must prove fault as part of her case, by showing either: (1) that the defendant intended to harm; (2) that the defendant failed to take reasonable care or was "negligent"; or (3) that the tort is one of strict liability, i.e. legally presumed fault. On a practical level, some, like F. L. Sharp, argue that the traditional approach confers an unfair advantage on the plaintiff by easing her burden of proof: "Negligent Trespass in Canada: A Persistent Source of Embarrassment" (1977-78), 1 Advocates' Q. 311, at pp. 312-14 and 326 [page563]. It is suggested that the law has moved in this direction in England: see Fowler v. Lanning, [1959] 1 Q.B. 426, approved in obiter in Letang v. Cooper, [1965] 1 Q.B. 232 (C.A.). In the spirit of these comments, my col-

league Iacobucci J. proposes to alter the traditional rule, at least for sexual battery, to require the plaintiff to prove fault, i.e. that the defendant either knew or ought to have known that she was not consenting.

**10** I do not agree with these criticisms of the traditional rule. In my view the law of battery is based on protecting individuals' right to personal autonomy. To base the law of battery purely on the principle of fault is to subordinate the plaintiff's right to protection from invasions of her physical integrity to the defendant's freedom to act: see R. Sullivan, "Trespass to the Person in Canada: A Defence of the Traditional Approach" (1987), 19 Ottawa L. Rev. 533, at p. 546. Although I do not necessarily accept all of Sullivan's contentions, I agree with her characterization, at p. 551, of trespass to the person as a "violation of the plaintiff's right to exclusive control of his person". This right is not absolute, because a defendant who violates this right can nevertheless exonerate himself by proving a lack of intention or negligence: Cook, supra, at p. 839, per Cartwright J. Although liability in battery is based not on the defendant's fault, but on the violation of the plaintiff's right, the traditional approach will not impose liability without fault because the violation of another person's right can be considered a form of fault. Basing the law of battery on protecting the plaintiff's physical autonomy helps explain why the plaintiff in an action for battery need prove only a direct interference, at which point the onus shifts to the person who is alleged to have violated the right to justify [page564] the intrusion, excuse it or raise some other defence.

**11** I agree with Sullivan's view that the traditional approach to trespass to the person remains appropriate in Canada's modern context for a number of reasons. First, unlike negligence, where the requirement of fault can be justified because the tortious sequence may be complicated, trespass to the person is confined to direct interferences. Where the trespass causes actual injury to the plaintiff, there is a direct connection between the defendant's action and the plaintiff's injury. As Sullivan notes, at p. 562:

> ... where the injury complained of is an immediate consequence of the defendant's act, it is intuitively sound to require compensation from the defendant unless he offers a defence. In cases of direct interference, the relationship between the defendant's will, his decision to act, and the injury to the plaintiff is both simple and clear; there are no competing causal factors to obscure the defendant's role or dilute his factual responsibility. The question of his moral and legal responsibility is thus posed with unusual sharpness: as between the defendant who caused the injury and the plaintiff who received it, other things being equal, who shall pay? ... Once the plaintiff has shown that his right to personal autonomy has been violated by the defendant, prima facie the defendant should pay. [Emphasis added.]

**12** Another factor supporting retaining the traditional approach to trespass and battery is that it makes practical sense. Linden J. in Bell Canada v. COPE (Sarnia) Ltd. (1980), 11 C.C.L.T. 170 (Ont. H.C.), aff'd (1980), 31 O.R. (2d) 571 (C.A.), after noting the attacks on the Canadian law of trespass, writes (at p. 180):

> The trespass action still performs several functions, one of its most important being a mechanism for shifting the onus of proof of whether there has been intentional or negligent wrongdoing to the defendant, rather than [page565]

> requiring the plaintiff to prove fault. The trespass action, though perhaps somewhat anomalous, may thus help to smoke out evidence possessed by defendants, who cause direct injuries to plaintiffs, which should assist Courts to obtain a fuller picture of the facts, a most worthwhile objective. [Emphasis added.]

**13** In cases of direct interference, the defendant is likely to know how and why the interference occurred. I agree with Sullivan's suggestion, at p. 563, that "if the defendant is in a position to say what happened, it is both sensible and just to give him an incentive to do so by putting the burden of explanation on him".

**14** Finally, I share Sullivan's concern with the fact that cases of direct interference with the person tend to produce high "demoralization costs" (p. 563). Victims and those who identify with them tend to feel resentment and insecurity if the wrong is not compensated. The close causal relationship between the defendant's conduct and the violation of the plaintiff's bodily integrity, the identification of the loss with the plaintiff's personality and freedom, the infliction of the loss in isolated (as opposed to systemic) circumstances, and the perception of the defendant's conduct as anti-social, all support the legal position that once the direct interference with the plaintiff's person is shown, the defendant may fairly be called upon to explain his behaviour if indeed it was innocent.

**15** These arguments persuade me that we should not lightly set aside the traditional rights-based approach to the law of battery that is now the law of Canada. The tort of battery is aimed at protecting the personal autonomy of the individual. Its purpose is to recognize the right of each person to control his or her body and who touches it, and to permit damages where this right is violated. The compensation stems from violation of the right to autonomy, not fault. When a person interferes with [page566] the body of another, a prima facie case of violation of the plaintiff's autonomy is made out. The law may then fairly call upon the person thus implicated to explain, if he can. If he can show that he acted with consent, the prima facie violation is negated and the plaintiff's claim will fail. But it is not up to the plaintiff to prove that, in addition to directly interfering with her body, the defendant was also at fault.

**16** Having stated that we should not set aside the traditional approach to battery, I do not wish to foreclose the possibility of future growth in this area of the law. References in definitions of the tort of battery to "injury", or to contact being "unlawful" or "harmful or offensive" are different ways of expressing the idea that not every physical contact constitutes a battery. In other words, the tort requires contact "plus" something else. One view, as I discuss in the next section, is that the "plus" refers merely to non-trivial contact. The caselaw to date tends to support this view, and generally does not require actual physical or psychological injury: Cole v. Turner (1704), 6 Mod. 149, 87 E.R. 907; Stewart v. Stonehouse, [1926] 2 D.L.R. 683 (Sask. C.A.), at p. 684; Fleming, supra, at p. 29; Fridman, supra, at p. 45. In a future case, it may be necessary to consider whether the "plus" required in addition to contact should be extended beyond the minimum of non-trivial acts. However, the issue does not arise in this case, since the plaintiff pleads physical and psychological damage. This is sufficient to bring the case within the traditional view of battery, however the "plus" is defined. Therefore, for the purposes of this case, I proceed upon the traditional view.

[page567]

C. The Argument that the Contact Must Be "Harmful or Offensive" Does Not Support Placing the Onus of Proving Non-Consent on the Plaintiff

**17** The proposition that the law should require a plaintiff in an action for sexual battery to prove that she did not consent, is supported, it is suggested, by a requirement that the contact involved in battery must be harmful or offensive. The argument may be summarized as follows. The plaintiff must prove all the essential elements of the tort of battery. One of these is that the contact complained of was inherently harmful or offensive on an objective standard. Consensual sexual contact is neither harmful nor offensive. Therefore the plaintiff, in order to make out her case, must prove that she did not consent or that a reasonable person in the defendant's position would not have thought she consented.

**18** I do not dispute that a plaintiff generally must prove all elements of the tort she alleges. Nor do I dispute that contact must be "harmful or offensive" to constitute battery. However, I am not persuaded that plaintiffs in cases of sexual battery must prove that contact was "non-consensual" in order to prove that it was "harmful or offensive". If one accepts that the foundation of the tort of battery is a violation of personal autonomy, it follows that all contact outside the exceptional category of contact that is generally accepted or expected in the course of ordinary life, is prima facie offensive. Sexual contact does not fall into the category of contact generally accepted or expected in the course of ordinary activities. Hence the plaintiff may establish an action for sexual battery without negativing actual or constructive consent.

**19** The idea that battery is confined to conduct that is "harmful or offensive" finds root in the old [page568] cases involving trivial contacts. While the law of battery traditionally has held that the defendant, not the plaintiff, bears the onus of proving consent, it has also held that not every trivial contact suffices to establish battery. The classic example is being jostled in a crowd. A person who enters a crowd cannot sue for being jostled; such contact is not "offensive". Two theories have been put forward to explain this wrinkle on the general rule that all a plaintiff in a battery action must prove is direct contact. The first is implied consent: Salmond and Heuston on the Law of Torts (21st ed. 1996), at p. 121. The second sees these cases as "a general exception embracing all physical contact which is generally acceptable in the ordinary conduct of everyday life": In re F., [1990] 2 A.C. 1 (H.L.), at p. 73, per Lord Goff.

**20** Both these theories are consistent with the settled rule in Canadian law that a plaintiff in a battery action need not prove the absence of consent. On the implied consent theory, even if the plaintiff proves contact, the burden never shifts to the defendant to prove consent because consent is implied by law. On the "exception" theory, the plaintiff cannot succeed merely by proving contact if such contact falls within the exceptional category of conduct generally acceptable in ordinary life. It is not necessary in this appeal to choose between these approaches, but in my view both refer to the sort of everyday physical contact which one must be expected to tolerate, even if one does not actually consent to it.

**21** The question then becomes whether sexual battery falls into the extraordinary category of cases where proving contact will not suffice to establish the plaintiff's case. Is sexual activity the sort of activity where consent is implied? Clearly it is not. [page569] Alternatively, is it the sort of activity, like being jostled in a crowd, that is generally accepted and expected as a normal part of life? Again, I think not. The sort of conduct the cases envision is the inevitable contact that goes with ordinary human activity, like brushing someone's hand in the course of exchanging a gift, a gratuitous handshake, or being jostled in a crowd. Sexual contact does not fall into this category. It

is not the casual, accidental or inevitable consequence of general human activity and interaction. It involves singling out another person's body in a deliberate, targeted act.

**22** The assertion in some of the authorities that the contact must be harmful or offensive to constitute battery (see, e.g., La Forest J. in M. (K.) v. M. (H.), [1992] 3 S.C.R. 6, at p. 25), reflects the need to exclude from battery the casual contacts inevitable in ordinary life. It does not, however, require the conclusion that to make out a case of battery, a plaintiff must prove that the contact was physically or psychologically injurious or morally offensive. The law of battery protects the inviolability of the person. It starts from the presumption that apart from the usual and inevitable contacts of ordinary life, each person is entitled not to be touched, and not to have her person violated. The sexual touching itself, absent the defendant showing lawful excuse, constitutes the violation and is "offensive". Sex is not an ordinary casual contact which must be accepted in everyday life, nor is it the sort of contact to which consent can be implied. To require a plaintiff in an action for sexual battery to prove that she did not consent or that a reasonable person in the defendant's position would not have thought she consented, would be to deny the protection the law has traditionally afforded to the [page570] inviolability of the body in the situation where it is perhaps most needed and appropriate.

**23** Only two cases, one in England concerning therapeutic administration of drugs and one in New Zealand concerning sexual assault, are cited in favour of the proposition that the plaintiff must show harm by proving a lack of consent as an element of the tort of battery: see Freeman v. Home Office, [1983] 3 All E.R. 589 (Q.B.), aff'd [1984] 1 All E.R. 1036 (C.A.), H. v. R., [1996] 1 N.Z.L.R. 299 (H.C.). The proposition that the plaintiff must prove a lack of consent, on the basis that she must prove that the impugned contact was harmful, is not supported by the law of battery, which has traditionally been confined to acts which are inherently harmful, like hitting, shooting or stabbing someone. Rather, its focus is on the protection of one's bodily integrity from any unwanted contact. Many of the older cases concern contacts devoid of any real harm apart from the violation of bodily integrity: Pursell v. Horn (1838), 8 AD. & E. 602, 112 E.R. 966 (pouring water on a person); Green v. Goddard (1704), 2 Salkeld 641, 91 E.R. 540 (forcibly taking an object held by another); Humphries v. Connor (1864), 17 Ir. Com. L. Rep. 1 (Q.B.) (taking flower worn by plaintiff), and Forde v. Skinner (1830), 4 Car. & P. 239, 172 E.R. 687 (cutting a person's hair). In more modern times, the same is true of medical battery cases. Like sexual acts, medical interventions may incidentally produce physical and psychological harm which may go to damages, but the basic "offence" or "harm" upon which the tort rests is the violation of the plaintiff's bodily integrity. As I discuss below, Canadian courts do not require plaintiffs alleging medical battery to prove that the defendant medical practitioner knew or ought to have known that the plaintiff did not consent to the medical contact.

[page571]

**24** The practical counterpart of the argument that battery must involve inherently harmful or offensive conduct in some larger sense is the suggestion that absent such a requirement, plaintiffs will be able to unfairly drag defendants into court as a result of consensual sex, putting them to the trouble and risk of proving that the plaintiff consented or that a reasonable person would have concluded she consented. This point was not strongly argued, and with reason. Few plaintiffs to con-

sensual sex or in situations where consent is a reasonable inference from the circumstances, are likely to sue if they are virtually certain to lose when the facts come out. Moreover, the rules of court provide sanctions for vexatious litigants. There is no need to change the law of battery to avoid vexatious claims.

**25** Moreover, the prospect of plaintiffs suing and saying nothing about consent is more theoretical than real. In fact, plaintiffs suing for sexual battery usually testify that they did not consent to the sexual contact. Failure to do so, absent an explanation, makes it more likely the defendant could win when he calls evidence of consent or reasonable appearance of consent. Even if a plaintiff were to bring an action in sexual battery against the estate of a deceased defendant, many provincial and territorial evidence acts would not allow the plaintiff to obtain a judgment against the estate unless her evidence were corroborated by other material evidence: see Evidence Acts of Alberta, R.S.A. 1980, c. A-21, s. 12; Newfoundland, R.S.N. 1990, c. E-16, s. 16; Northwest Territories, R.S.N.W.T. 1988, c. E-8, s. 17; Nova Scotia, R.S.N.S. 1989, c. 154, s. 45; Ontario, R.S.O. 1990, c. E.23, s. 13; Prince Edward Island, R.S.P.E.I. 1988, c. E-11, s. 11; Yukon, R.S.Y. 1986, c. 57, s. 14. At the same time, as discussed more fully below, placing on the plaintiff the legal burden of always [page572] negativing actual and constructive consent on pain of non-suit, may lead to injustice.

**26** I conclude that the fact that the law of battery excludes trivial contact and requires contact that is "harmful or offensive" does not require us to conclude that the plaintiff bears the burden of proving that the defendant actually or constructively knew she did not consent to sexual contact.

### D. There Is Nothing Particular About Sexual Assault that Makes it Necessary to Have a Special Rule of Battery for Sexual Assaults for What the Plaintiff Must Prove

**27** If there were something special about sexual battery that justified requiring the plaintiff to prove that the defendant either knew she was not consenting or ought to have known that she was not consenting, a case might be made for so doing. The result would be a special rule for sexual battery inconsistent with the law of battery generally, and the creation of a new tort of sexual battery. Thus far the courts have declined to do this. As Professor Feldthusen notes, "[t]here has yet to be recognised a new nominate tort of sexual battery" (emphasis in original): "The Canadian Experiment with the Civil Action for Sexual Battery", in N. J. Mullany, ed., Torts in the Nineties (1997), 274, at p. 281. The sexual aspects of the claim go only to damages. However, as I stated above, a new tort of sexual battery with different rules from ordinary battery could be recognized in an appropriate case.

**28** Before examining whether sexual battery is so different that special rules are required as to what the plaintiff must show, it is important to take note of the danger of placing special, unjustified [page573] burdens on victims of sexual encounters. At p. 282, Feldthusen notes that "in the criminal sphere, enquiries into alleged consent have allowed the focus of the criminal trial to shift from the actions of the defendant to the character of the complainant. The same potential exists in tort law" (emphasis added). As he points out, "[t]here exist in our law deeply imbedded tendencies towards victim blaming" (p. 283). This is not to say that alleged victims of sexual assault could never be singled out by placing special rules of proof on them that do not apply to other types of plaintiffs. It is rather to say that we must guard against placing such burdens upon alleged victims of sexual assault unless it can objectively be shown that it is necessary to do so in order to achieve justice.

**29** To require plaintiffs in actions for sexual battery to prove that they did not consent and that a reasonable person in the circumstances of the defendant would not have believed they consented, is to place a burden on plaintiffs in actions for sexual battery that plaintiffs in other types of battery do not bear. It is to do so, moreover, in the absence of any compelling reason. Indeed, there are powerful reasons for applying the usual rules that require a plaintiff to prove only direct contact in cases of sexual battery.

**30** The first concern is that by requiring the plaintiff to prove more than the traditional battery claim requires, we inappropriately shift the focus of the trial from the defendant's behaviour to the plaintiff's character. Requiring the plaintiff to prove that a reasonable person in the position of the defendant would have known that she was not consenting requires her to justify her actions. In practical terms, she must prove that she made it clear through her conduct and words that she did not consent to the sexual contact. Her conduct, not the [page574] defendant's, becomes the primary focus from the outset. If she cannot prove these things, she will be non-suited and the defendant need never give his side of the story.

**31** The proposed shift to the plaintiff of the onus of disproving constructive consent runs the risk of victim blaming, against which Feldthusen and others properly warn. It also runs the risk of making it impossible for deserving victims of sexual battery to even get their foot in the litigation door. Consider the case of the victim of sexual assault who cannot testify to the events because of shock, loss of memory or inebriation. If she can prove that she was sexually assaulted and identify the perpetrator through third-person evidence, should she be non-suited at the outset because she cannot prove that her conduct in the circumstances would have led a reasonable person to conclude she was not consenting? Is it not better in such cases that the defendant be called upon to give evidence so the court can decide the case on a more complete picture of the facts? This is what the law of battery would traditionally require. Why should we exempt the defendant because the battery is a sexual battery?

**32** The proposed shift of onus runs counter to Parliament's expressed view in the criminal context. Although the aims of criminal law and the law of tort are not identical, it remains significant that Parliament in s. 273.2(b) of the Criminal Code, R.S.C., 1985, c. C-46, stipulates that those accused of sexual assault who seek to invoke the defence of honest but mistaken belief in consent must have taken reasonable steps in the circumstances known to them at the time to ascertain the complainant's [page575] consent. Parliament has thus moved to counteract the historic tendency of criminal trials for sexual assault to focus unduly on the behaviour of the complainant, and to redirect some of the focus to the defendant. The traditional tort of battery already provides this focus in the civil domain. That focus should be retained in my view. To quote Sullivan, supra, at p. 563, "if the defendant is in a position to say what happened, it is both sensible and just to give him an incentive to do so by putting the burden of explanation on him".

**33** Requiring the plaintiff to disprove constructive consent seems all the more unfair because the relevant facts lie first and foremost within the defendant's sphere of knowledge. He alone knows whether he actually believed the plaintiff was consenting, and if he believed she was consenting, he is in the best position to give evidence on the factors that led him to believe that. The plaintiff, by contrast, is not in a position to produce evidence of what was in the defendant's mind nor in as good a position to say what factors led him to that state of mind and whether he acted reasonably. While the defendant's particular knowledge about his state of mind regarding consent is not determinative of who bears the burden of proof regarding consent, it is one of the principles of fairness and policy

that are said to influence the allocation of this burden: see J. Sopinka, S. N. Lederman, and A. W. Bryant, The Law of Evidence in Canada (2nd ed. 1999), at para. 3.70; McCormick on Evidence (5th ed. 1999), vol. 2, at para. 337.

**34** I conclude that there is nothing about sexual battery that requires that the traditional rules of onus governing battery actions be changed. On the contrary, placing the onus on the plaintiff of disproving consent and constructive consent seems [page576] unfairly to impose special obligations on plaintiffs who sue for sexual assault.

### E. To Require the Plaintiff to Prove that the Defendant Knew or Ought to Have Known She Was Not Consenting Presents the Dilemma of Either Changing the Law for Other Types of Battery or Introducing an Inconsistency in the Law of Battery

**35** To hold that battery must involve a contact that is inherently harmful or offensive has the potential to change the law relating to other types of battery, like medical battery. Alternatively, if it does not, it will introduce an inconsistency into the law of battery.

**36** As discussed, Canadian courts have repeatedly held that for medical battery, the defendant bears the onus of proving consent as a defence: see, for example, Reibl, supra; Schweizer v. Central Hospital (1974), 53 D.L.R. (3d) 494 (Ont. H.C.); Allan v. New Mount Sinai Hospital (1980), 109 D.L.R. (3d) 634 (Ont. H.C.), rev'd on other grounds (1981), 33 O.R. (2d) 603 (C.A.); Brushett v. Cowan (1990), 3 C.C.L.T. (2d) 195 (Nfld. C.A.), at p. 199, and O'Bonsawin v. Paradis (1993), 15 C.C.L.T. (2d) 188 (Ont. Ct. (Gen. Div.)). Like sexual contact, the act of medical intervention is not inherently harmful or offensive, beyond its potential to violate bodily integrity. If sexual battery requires the plaintiff to prove that the defendant knew or ought to have known that the plaintiff did not consent, it is difficult to see why the same would not hold for medical malpractice. Yet no one has suggested that the law of medical malpractice ought to be changed to place an additional burden on the plaintiff of proving a culpable state of mind in the defendant medical practitioner. The alternative, if the law of battery were changed in this regard for sexual battery, would be inconsistency in the law of battery. Neither alternative is attractive. This suggests a further reason for being wary of the proposition that battery requires proof [page577] by the plaintiff of an inherently harmful or offensive act.

### F. Requiring the Plaintiff to Prove that the Defendant Knew or Ought to Have Known that She Did Not Consent is Neither Necessary nor Sufficient to Permit the Conclusion that the Insurers in this Case Are Not Obligated to Defend the Defendant

**37** The question at issue on this appeal is whether the insurer may avoid the obligation to defend the defendant to the battery action under the policy exclusion for "any intentional ... act". I agree with Iacobucci J. that this clause must be interpreted as requiring an intent to injure. It follows that for the tort of sexual battery to be excluded from policy coverage, it must always involve intent to injure.

**38** As I understand his reasons, Iacobucci J. finds this intent to injure is present on the basis of legal inference, not as a matter of fact. The law presumes that in actions of battery for sexual assault, the defendant intends to injure the plaintiff. Thus Iacobucci J. states "[g]iven ... actual or constructive knowledge of non-consent, the law will not permit the appellant to claim that he did not

intend any harm" (para. 94 (emphasis added)). This legal inference is necessary because in cases of constructive knowledge, the defendant may be held liable despite the fact that he had no actual knowledge of lack of consent and hence no actual intent to harm the plaintiff. Iacobucci J. elaborates at para. 121 in reviewing the American jurisprudence [page578] on this issue, in the context of sexual assaults on children:

> Courts have had little difficulty in concluding that defendants in these cases are presumed to intend harm to their victims -- notwithstanding the fact that "males who are involved in such activities do not expect or intend that the females will sustain any injury"... . [Emphasis added.]

In other words, where there is an allegation of sexual battery, courts will conclude as a matter of legal inference that the defendant intended harm for the purpose of construing exemptions of insurance coverage for intentional injury.

**39** This presumption of intent to harm does not depend on requiring the plaintiff to prove that the defendant knew or ought to have known that the plaintiff was not consenting to the sexual contact. Rather, the presumption flows from the allegation in the pleadings of battery of a sexual nature. American cases, like State Farm Fire and Casualty Co. v. Williams, 355 N.W.2d 421 (Minn. 1984), do not turn on the plaintiff's bearing the burden of showing the defendant either knew or ought to have known she did not consent. The logic is simply that either the act must have been consensual or not consensual. If it was not consensual, the policy does not apply because neither the insured nor the insurer contemplated coverage for non-consensual sexual activities. If it was consensual, then there is no battery and no claim for recovery. In either case, the policy does not apply. As stated in Williams, at p. 424:

> Does the fact that Williams, the victim, was an adult distinguish this case? We think not. Neither the insured nor the insurer in entering into the insurance contract contemplated coverage against sexual claims arising out of non-consensual sexual assaults.

**40** This reasoning applies equally to allegations of negligent sexual battery where the alleged negligence relates to the defendant's belief in the plaintiff's consent to sexual contact. For these reasons [page579] I conclude that it is not necessary to place on the plaintiff the burden of proving the defendant's knowledge or constructive knowledge of the plaintiff's non-consent.

**41** If this reasoning is correct, then placing the non-traditional burden of disproving consent or constructive consent on the plaintiff is neither a necessary nor a sufficient condition of concluding that the policy does not apply in cases like this. Regardless of how one views the matter of onus, the result will be the same.

### G. Negligent Battery

**42** It is unnecessary on this appeal to comment on the relationship between battery (traditionally thought of mainly as an intentional tort) and negligence. In this case, insofar as one could speak of negligent battery, it would be to recognize the defence of reasonable belief in consent to a suit based on an intentional act. As discussed, the law in these circumstances presumes an intention to injure, taking it out of the realm of pure negligence and bringing it within the ambit of the exclusion clause.

II. Conclusion

**43** I conclude that there is no justification in cases of battery of a sexual nature for departing from the traditional rule that the plaintiff in a battery action must prove direct contact, at which point the onus shifts to the defendant to prove consent. To do so would be to place a burden upon plaintiffs in battery actions of a sexual nature which plaintiffs in other battery actions do not bear. I see neither the need nor the justification for doing this on the material before us in this case.

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**44** This said, I agree fully with Iacobucci J. that the law will not permit a defendant in an action for sexual battery to say that though he might be found to have committed the battery, he did not intend any harm. This leaves the defendant with two alternatives discussed in Williams, supra. Either the plaintiff consented, in which case no action lies, or she did not consent and the defendant is deemed to have intended to injure her. In neither case does the policy provide coverage.

**45** Like Iacobucci J., I would dismiss the appeal with costs.

The reasons of Iacobucci, Major and Bastarache JJ. were delivered by

IACOBUCCI J.:--

I. Introduction and Overview

**46** This appeal raises the novel question of whether an insurance company has a duty to defend the holder of a homeowner's insurance policy against a civil sexual assault suit. In answering this question, we must also address the role of consent in an action for sexual assault.

**47** It should be noted that this appeal was heard along with the appeal in Sansalone v. Wawanesa Mutual Insurance Co., [2000] 1 S.C.R. 627, 2000 SCC 25, reasons in which are being released concurrently.

**48** This appeal concerns the insurance implications of a series of allegedly non-consensual sexual touchings. For ease of reference, I will use the term "sexual assault" to refer in general to any allegation of non-consensual sexual touching. My use of the term "sexual assault" should not be taken to imply any specific legal ramifications. But for "sexual battery", by contrast, I will give a more specific definition in the course of these reasons.

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**49** An insurance company's duty to defend is related to its duty to indemnify. A homeowner's insurance policy entitles the holder to have the insurer indemnify any liability falling within the policy's terms. Since the insurance company will be paying these costs, it has also developed the right -- now a duty -- to conduct the defence of such claims. However, the duty to defend is not so great that it is presumed to be independent of the duty to indemnify. Absent express language to the

contrary, the duty to defend extends only to claims that could potentially trigger indemnity under the policy. Therefore if an insurance policy, like the one in this case, excludes liability arising from intentionally caused injuries, there will be no duty to defend intentional torts.

**50** Determining whether or not a given claim could trigger indemnity is a three-step process. First, a court should determine which of the plaintiff's legal allegations are properly pleaded. In doing so, courts are not bound by the legal labels chosen by the plaintiff. A plaintiff cannot change an intentional tort into a negligent one simply by choice of words, or vice versa. Therefore, when ascertaining the scope of the duty to defend, a court must look beyond the choice of labels, and examine the substance of the allegations contained in the pleadings. This does not involve deciding whether the claims have any merit; all a court must do is decide, based on the pleadings, the true nature of the claims.

**51** At the second stage, having determined what claims are properly pleaded, the court should determine if any claims are entirely derivative in nature. The duty to defend will not be triggered simply because a claim can be cast in terms of both negligence and intentional tort. If the alleged negligence is based on the same harm as the intentional [page582] tort, it will not allow the insured to avoid the exclusion clause for intentionally caused injuries.

**52** Finally, at the third stage the court must decide whether any of the properly pleaded, non-derivative claims could potentially trigger the insurer's duty to defend. In this appeal, I conclude that the respondent has no duty to defend. The plaintiff has alleged three basic claims against the appellant: sexual battery, negligence, and breach of fiduciary duty.

**53** To prove a claim for sexual battery, the plaintiff will have to establish that the defendant intentionally inflicted a harmful or offensive touching on her. In the context of sexual battery, "harmful or offensive" is equivalent to non-consensual. This test is objective: to establish sexual battery, the plaintiff must demonstrate that a reasonable person would have known that the plaintiff did not validly consent to sexual relations. To put it another way, the plaintiff will have to prove that the defendant should have known that she did not validly consent. It is important to note that, absent any evidence from the defendant, a simple allegation of non-consensual sex will suffice to meet this initial burden. If the plaintiff succeeds, then the defendant must also be presumed to have intended to injure the plaintiff, given the inherently harmful nature of non-consensual sexual activity. The same facts that prove the sexual battery also necessarily prove an intent to injure, and therefore the exclusion clause should apply. If, on the other hand, the plaintiff cannot establish non-consent, then the plaintiff's action would have no chance of success, there would be no possibility of a claim for indemnity, and the duty to defend would not arise.

**54** The claims for negligence and breach of fiduciary duty fail to trigger the duty to defend not because they could not fall within coverage, but because they are either not properly pleaded, or derivative of the claim for sexual battery. As a [page583] result, they are also covered by the exclusion for injuries intentionally caused.

**55** As there are no properly pleaded claims that, even if successful, could potentially trigger indemnity, the respondent has no duty to defend, and I would therefore dismiss the appeal.

## II. Facts

**56** The underlying action in this appeal is based on a series of alleged sexual assaults committed against a young girl ("the plaintiff"), who was born in 1974 and was an adolescent at the time of

the incidents in question. The plaintiff worked part-time at a grocery store owned and operated by her parents, located near the terminus of two B.C. Transit bus routes. In 1996, the plaintiff brought a civil action against five B.C. Transit bus drivers, including the appellant, alleging various sexual assaults between 1988 and 1992. The liability insurance policy owned by one of the bus drivers, Vincent Scalera, is at issue in this appeal.

**57** The plaintiff's statement of claim alleges that between 1986 and 1992, while on duty with B.C. Transit, the appellant regularly attended the store belonging to the plaintiff's parents, and became acquainted with the plaintiff. She, in turn, regularly rode on buses driven by the appellant. The statement of claim further alleges as follows:

> 103. On one occasion between approximately January and June of 1991 Scalera committed various sexual acts upon [the plaintiff], including:
>
> (a) sexual kissing;
> (b) sexual touching of her neck, back, breasts, and genitals; and
> (c) fellatio
>
> together (the "Scalera sexual acts").

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> 104. Scalera committed the Scalera sexual acts upon [the plaintiff] in various locations, including:
>
> (a) on buses owned by B.C. Transit; and
> (b) in his truck.
>
> 105. The Scalera sexual acts were committed upon [the plaintiff] by Scalera for a sexual purpose and/or without [the plaintiff]'s consent.
> 106. Scalera committed the Scalera sexual acts upon [the plaintiff] by coercion, manipulation, and abuse of power.
> 107. The Scalera sexual acts were sexual assaults and/or sexual exploitation and/or unlawful.
> 108. At all material times, Scalera was an adult and [the plaintiff] was an infant and/or a young person.
> 109. Scalera, by words or conduct, threatened that harm would come to [the plaintiff] if she disclosed the Scalera sexual acts to another person, intending to persuade [the plaintiff] to submit to the Scalera sexual acts.
> 110. Scalera, by words or conduct, knowingly, fraudulently, and deceitfully misrepresented the Scalera sexual acts committed by him upon [the plaintiff] as:
>
> (a) the prerogative of an adult;
> (b) consensual activity; and/or
> (c) a healthy, normal expression of his affection for her

together (the "Scalera Representations").

111. Scalera made the Scalera Representations intending to persuade [the plaintiff] to submit to the Scalera sexual acts.
112. The Scalera Representations were untrue.
113. [The plaintiff] relied on the Scalera Representations concerning the nature of the Scalera sexual acts and thereby submitted to the Scalera sexual acts.
114. [The plaintiff] relied on the Scalera Representations concerning the nature of the Scalera sexual acts and thereby failed to report Scalera's conduct to other adults.
115. Scalera knew or ought to have known that the Scalera sexual acts were unlawful and/or the Scalera Representations were untrue.

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116. Scalera knew or ought to have known that [the plaintiff] was an infant and/or a young person.
117. Scalera knew or ought to have known that [the plaintiff] did not consent to the Scalera sexual acts.
118. Scalera owed a duty of care to [the plaintiff], which duty of care arose from the relationship of authority and trust between himself as an adult and/or bus driver and [the plaintiff] as an infant and/or young person and/or bus passenger, and Scalera breached this duty of care.
119. Scalera owed a fiduciary duty to [the plaintiff], which fiduciary duty arose from the relationship of authority and trust between himself as an adult and/or bus driver and [the plaintiff] as an infant and/or young person and/or bus passenger, and Scalera breached this fiduciary duty.
120. Scalera committed the Scalera sexual acts willfully and without lawful justification.
121. The Scalera sexual acts were committed intentionally and/or with reckless disregard as to their effect on [the plaintiff].
122. By reason of Scalera's actions in committing the Scalera sexual acts [the plaintiff] has suffered nervous shock and sustained severe personal injuries, particulars of which are set out in paragraph 127 below.

...

128. As a result of the aforesaid sexual assaults, sexual exploitation, intentional infliction of nervous shock, misrepresentations, negligence, breaches of duty, and breaches of fiduciary duty committed by ... Scalera, and/or B.C. Transit [the plaintiff] has suffered a loss of income and a loss of ability to earn income in the future.
129. As a result of the aforesaid sexual assaults, sexual exploitation, intentional infliction of nervous shock, misrepresentations, negligence, breaches of duty, and

> breaches of fiduciary duty committed by ... Scalera, and/or B.C. Transit [the plaintiff] has and/or will continue to incur expenses, including obtaining proper psychiatric and psychological counselling and treatment which will be required on both an ongoing and crisis basis.

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**58** In response to a demand for particulars, counsel for the plaintiff stated that the coercion, manipulation, and abuse of power alleged in para. 106 of the statement of claim consisted of:

(a) pressure to engage in the sexual acts as a result of Scalera's position as an adult and [the plaintiff]'s position as an infant and/or young person;
(b) pressure to engage in the sexual acts in order to demonstrate affection to Scalera;
(c) pressure to engage in the sexual acts in order to secure and/or maintain Scalera's alleged affection and/or friendship;
(d) pressure to engage in the sexual acts in order to overcome personal loneliness and/or insecurity;
(e) pressure to engage in the sexual acts in order to demonstrate maturity.

**59** The appellant owned a homeowner's insurance policy issued by the respondent. The relevant provisions of that policy are as follows:

SECTION TWO -- PERSONAL LIABILITY INSURANCE

...

> This insurance applies only to accidents or occurrences which take place during the period of insurance indicated on the Declarations. ...
>
> We will pay all sums which you become legally liable to pay as compensatory damage because of bodily injury or property damage. ...
>
> You are insured for claims made against you arising from:

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> 1. Personal Liability -- legal liability arising out of your personal actions anywhere in the world.
>
> ...

We will defend, by counsel of our choice, any suit against you alleging bodily injury or property damage and seeking compensatory damages, even if it is groundless, false or fraudulent. We reserve the right to investigate, negotiate and settle any claim or suit if we decide this is appropriate.

...

GENERAL EXCLUSIONS APPLICABLE TO THIS SECTION TWO

You are not insured for claims arising from:

...

(5) bodily injury or property damage caused by any intentional or criminal act or failure to act by:

(a) any person insured by this document ...

**60** The respondent sought a declaration that it not be required to defend the appellant against the plaintiff's claims. Humphries J. dismissed the respondent's petition, but the Court of Appeal allowed the appeal.

III. Judicial Decisions

A. British Columbia Supreme Court (1997), 47 B.C.L.R. (3d) 187

**61** Humphries J. interpreted the insurance policy's exclusion such that only intentional acts, but not intentional injuries, trigger exclusion. However, she believed that the relevant act underlying the plaintiff's claim must be sexual assault, not merely sexual contact, for it to fall within the exclusion. Relying on Co-operative Fire & Casualty Co. v. Saindon, [1976] 1 S.C.R. 735, she found at para. 23 that "[i]f the allegations in the Statement of Claim include a possible claim in negligence against [the appellant], and if such a plea is a legitimate one made in good faith, [the respondent] [page588] cannot rely on the exclusion clause because injury or damage caused by a negligent act falls outside it". Since it was possible that the appellant had intended only sexual contact, but was simply negligent regarding sexual assault, there was a duty to defend.

B. British Columbia Court of Appeal (1998), 48 B.C.L.R. (3d) 143

(i) Hollinrake J.A., Proudfoot J.A. concurring

**62** The appeals of the respondent and Wawanesa Mutual Insurance Co., respondent in the companion appeal, Sansalone, were consolidated at the Court of Appeal. Having accepted Saindon as the leading case on point, Hollinrake J.A. turned to the specific issues raised by the Scalera appeal. He concluded that the exclusion clause in question barred claims based on intentional acts. Since most tort claims allege negligence and not intent to injure, excluding intentional acts from coverage was "in keeping with coverage historically provided by policies insuring against liability imposed by law caused by accident" (para. 91). It was also consistent with the reasonable expectations of the parties.

**63** Hollinrake J.A. found that the claim advanced sounded in intentional tort, and saw no reason to require the respondent to prove the intent to injure. The appellant's act was clearly intentional and

was within the exclusion clause, so there was no possibility of coverage. Any claims based on the power-dependency relationship between the plaintiff and the appellant also fell within the exclusion, as it had in Sansalone. Finally, Hollinrake J.A. disagreed with Finch J.A. as to the meaning of the duty to defend clause. He concluded that, in order for there to be a duty to defend, there had to be at least a possibility of coverage. Since he had [page589] already determined that there was no possibility of coverage, he allowed the appeal.

(ii) Finch J.A., dissenting

**64** Finch J.A. concluded that in spite of the exclusion clause's language referring only to intentional acts, it must be read to exclude liability only for injury or damage caused intentionally. To do otherwise would exclude the vast majority of all claims, since most accidents or occurrences can be traced back to an intentional act. Finch J.A. did not read the pleadings as alleging an intention on the part of the appellant to cause the plaintiff injury. He therefore concluded that the duty to defend should apply.

**65** Moreover, Finch J.A. held that under the wording of the appellant's policy, the duty to defend was not linked to the duty to indemnify. As a result, the respondent was obliged to defend any claim for bodily injury causing compensable damages, regardless of whether that claim could also trigger indemnity.

## IV. Issues

**66** This appeal raises four issues.

1. Is the duty to defend in the appellant's insurance policy linked to the duty to indemnify?
2. Do the intentional act exclusion clauses in the appellant's insurance policy operate to relieve the respondent's duty in this case?
3. Was there an "accident" or "occurrence" that is sufficient to trigger coverage?
4. Does s. 28 of the British Columbia Insurance Act, R.S.B.C. 1996, c. 226, absolve the respondent of any duty to defend the appellant?

[page590]

Because of my disposition of the first two issues, I find it unnecessary to address the latter two in this appeal.

## V. Analysis

### A. General Principles of Insurance Contract Interpretation

**67** To begin with, I should like to discuss briefly several principles that are relevant to the interpretation of the insurance policy in question. While these principles are merely interpretive aids that cannot decide any issues by themselves, they are nonetheless helpful when interpreting provisions of an insurance contract.

(i) The General Purpose of Insurance

**68** It is important to keep in mind the underlying economic rationale for insurance. C. Brown and J. Menezes, Insurance Law in Canada (2nd ed. 1991), state this point well at pp. 125-26:

> Insurance is a mechanism for transferring fortuitous contingent risks. Losses that are neither fortuitous nor contingent cannot economically be transferred because the premium would have to be greater than the value of the subject matter in order to provide for marketing and adjusting costs and a profit for the insurer. It follows, therefore, that even where the literal working of a policy might appear to cover certain losses, it does not, in fact, do so if (1) the loss is from the inherent nature of the subject matter being insured, or (2) it results from the intentional actions of the insured.

**69** In other words, insurance usually makes economic sense only where the losses covered are unforeseen or accidental: "The assumptions on which insurance is based are undermined if successful claims arise out of loss which is not fortuitous" (C. Brown, Insurance Law in Canada (3rd ed. 1997), at p. 4). This economic rationale takes on a public policy flavour where, as here, the acts for which the insured is seeking coverage are socially harmful. It may be undesirable to encourage people to injure others intentionally by indemnifying them from the civil consequences. On the other hand, denying coverage has the undesirable [page591] effect of precluding recovery against a judgment-proof defendant, thus perhaps discouraging sexual assault victims from bringing claims. See B. Feldthusen, "The Civil Action for Sexual Battery: Therapeutic Jurisprudence?" (1993), 25 Ottawa L. Rev. 203, at p. 233.

(ii) Contra Proferentem

**70** Since insurance contracts are essentially adhesionary, the standard practice is to construe ambiguities against the insurer: Brissette Estate v. Westbury Life Insurance Co., [1992] 3 S.C.R. 87, at p. 92; Wigle v. Allstate Insurance Co. of Canada (1984), 49 O.R. (2d) 101 (C.A.), per Cory J.A. A corollary of this principle is that "coverage provisions should be construed broadly and exclusion clauses narrowly": Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co., [1993] 1 S.C.R. 252, at p. 269; Indemnity Insurance Co. of North America v. Excel Cleaning Service, [1954] S.C.R. 169, at pp. 179-80, per Estey J. Therefore one must always be alert to the unequal bargaining power at work in insurance contracts, and interpret such policies accordingly.

(iii) Reasonable Expectations

**71** Where a contract is unambiguous, a court should give effect to the clear language, reading the contract as a whole: Brissette Estate, supra, at p. 92; Parsons v. Standard Fire Insurance Co. (1880), 5 S.C.R. 233. Where there is ambiguity, this Court has noted "the desirability ... of giving effect to the reasonable expectations of the parties": Reid Crowther, supra, at p. 269 (citing Brown and Menezes, supra, at pp. 123-31, and Brissette Estate, supra). See also Scott v. Wawanesa Mutual Insurance Co., [1989] 1 S.C.R. 1445, at p. 1467; Wigle, supra. Estey J. stated the point succinctly in Consolidated-Bathurst Export Ltd. v. Mutual [page592] Boiler and Machinery Insurance Co., [1980] 1 S.C.R. 888, at pp. 901-2:

> [L]iteral meaning should not be applied where to do so would bring about an unrealistic result or a result which would not be contemplated in the commercial atmosphere in which the insurance was contracted. Where words may bear two constructions, the more reasonable one, that which produces a fair result, must certainly be taken as the interpretation which would promote the intention of the parties. Similarly, an interpretation which defeats the intentions of the parties and their objective in entering into the commercial transaction in the first place should be discarded in favour of an interpretation of the policy which promotes a sensible commercial result... . Said another way, the courts should be loath to support a construction which would either enable the insurer to pocket the premium without risk or the insured to achieve a recovery which could neither be sensibly sought nor anticipated at the time of the contract.

This court recently re-stated the importance of commercial reality, in another context, in Guarantee Co. of North America v. Gordon Capital Corp., [1999] 3 S.C.R. 423, at para. 62.

**72** With these principles in mind, I now wish to discuss the principal issues in this appeal.

B. The Scope of the Insurer's Duty to Defend

(i) The Linkage Between the Duties to Indemnify and to Defend

**73** The appellant's first argument is that the duty to defend is independent of the duty to indemnify. The relevant clause in the appellant's policy states: "We will defend, by counsel of our choice, any suit against you alleging bodily injury or property damage and seeking compensatory damages, even if it is groundless, false or fraudulent." The appellant argues, and Finch J.A. agreed in dissent at the Court of Appeal, that this requires not a potentially [page593] indemnifiable claim, but only a claim alleging bodily injury and seeking compensatory damages.

**74** With respect, I cannot agree. McLachlin J. addressed this question in Nichols v. American Home Assurance Co., [1990] 1 S.C.R. 801. The policy in that appeal specifically limited the duty to defend to suits "seeking damages which are or may be payable under the terms of this Policy" (p. 805), and so there was obviously no independent duty to defend under that particular policy. However, McLachlin J. went on, at pp. 810-11, to set out general principles governing the duty to defend, regardless of whether there is express language or not:

> Thus far, I have proceeded only by reference to the actual wording of the policy. However, general principles relating to the construction of insurance contracts support the conclusion that the duty to defend arises only where the pleadings raise claims which would be payable under the agreement to indemnify in the insurance contract. Courts have frequently stated that "[t]he pleadings govern the duty to defend": Bacon v. McBride (1984), 6 D.L.R. (4th) 96 (B.C.S.C.), at p. 99. Where it is clear from the pleadings that the suit falls outside of the coverage of the policy by reason of an exclusion clause, the duty to defend has been held not to arise: Opron Maritimes Construction Ltd. v. Canadian Indemnity Co. (1986), 19 C.C.L.I. 168 (N.B.C.A.), leave to appeal refused by this Court, [1987] 1 S.C.R. xi.

> At the same time, it is not necessary to prove that the obligation to indemnify will in fact arise in order to trigger the duty to defend. The mere possibility that a claim within the policy may succeed suffices. In this sense, as noted earlier, the duty to defend is broader than the duty to indemnify.
>
> ...
>
> Other Canadian authority overwhelmingly supports the view that normally the duty to defend arises only with respect to claims which, if proven, would fall [page594] within the scope of coverage provided by the policy... .
>
> The same view generally prevails in the United States... .

**75** McLachlin J. also provided two policy reasons in support of this conclusion, and in so doing refuted the contrary arguments made in the American case Conner v. Transamerica Insurance Co., 496 P.2d 770 (Okla. 1972). First, the insurer would have to pay defence costs for claims outside the policy's scope. This raised "policy questions of whether others in the insurance pool should be taxed with providing defences for matters outside the purview of the policy": Nichols, supra, at pp. 811-12. Second, an independent duty to defend raises conflict of interest problems. If the insurer is defending claims for which it owes no duty to indemnify, there is a strong incentive simply to settle the claim as quickly as possible. At the very least, the insurer has an incentive to try to prove only that the insured is liable for claims falling outside coverage. There would be little incentive to establish that the insured was entirely without blame. McLachlin J. therefore concluded, at p. 812, that

> considerations relat[ing] to insurance law and practice, as well as the authorities, overwhelmingly support the view that the duty to defend should, unless the contract of insurance indicates otherwise, be confined to the defence of claims which may be argued to fall under the policy. That said, the widest latitude should be given to the allegations in the pleadings in determining whether they raise a claim within the policy.

**76** While this is obiter dictum, I find McLachlin J.'s arguments compelling. Absent specific language to the contrary, the duty to defend is broader than the duty to indemnify only in so far as it extends to groundless, false, or fraudulent claims. Given the historical evolution of the duty [page595] to defend as a way for insurers to protect their interests when they will be forced to pay any resulting judgment (see J. M. Fischer, "Broadening the Insurer's Duty to Defend: How Gray v. Zurich Insurance Co. Transformed Liability Insurance Into Litigation Insurance" (1991), 25 U.C. Davis L. Rev. 141, at pp. 146-57; E. S. Pryor, "The Tort Liability Regime and the Duty to Defend" (1999), 58 Md. L. Rev. 1), it makes little sense to presume an independent duty to defend absent express language: see B. Vail, "'My Mistake, Your Problem': The Duty to Defend Liability Claims in Canada" (1996), 6 C.I.L.R. 201, at p. 207, and Fischer, supra. To hold otherwise would convert indemnity insurance into litigation insurance. In my opinion, such an interpretation would violate the reasonable expectations of the parties absent express language to that effect.

**77** Although prior to Nichols, Canadian courts were split on the issue, since Nichols courts have followed the dictum from that case. See Modern Livestock Ltd. v. Kansa General Insurance Co. (1993), 11 Alta. L.R. (3d) 355 (Q.B.); B.P. Canada Inc. v. Comco Service Station Construction

& Maintenance Ltd. (1990), 73 O.R. (2d) 317 (H.C.), and Kates v. Hall, [1990] 5 W.W.R. 569 (B.C.S.C.).

**78** This conclusion is consistent with the majority of American courts, which have concluded that the "duty to defend arises when the underlying complaint alleges any facts that might fall within the coverage of the policy": Colorado Farm Bureau Mutual Insurance Co. v. Snowbarger, 934 P.2d 909 (Colo. Ct. App. 1997), at p. 912. See also, e.g., Aerojet-General Corp. v. Transport Indemnity Co., 948 P.2d 909 (Cal. 1997), at p. 921; Lawyers Title Insurance Corp. v. Knopf, 674 A.2d 65 (Md. Ct. Spec. App. 1996), at p. 70; Allstate Insurance Co. v. Patterson, 904 F. Supp. 1270 (D. Utah 1995); Allstate Insurance Co. v. Brown, 834 F. Supp. 854 [page596] (E.D. Pa. 1993). To the contrary, see Gray v. Zurich Insurance Co., 419 P.2d 168 (Cal. 1966).

(ii) The Relevance of the Pleadings

**79** The appellant notes that the plaintiff's statement of claim alleged the non-intentional torts of negligence and breach of fiduciary duty. He therefore argues that the respondent has a duty to defend because the exclusion clause does not apply to these claims. However, these bare assertions alone cannot be determinative. Otherwise, the parties to an insurance contract would always be at the mercy of the third-party pleader. What really matters is not the labels used by the plaintiff, but the true nature of the claim.

**80** The general rule regarding the role of the pleadings is well stated by Wallace J. in Bacon v. McBride (1984), 6 D.L.R. (4th) 96 (B.C.S.C.), at p. 99:

> The pleadings govern the duty to defend -- not the insurer's view of the validity or nature of the claim or by the possible outcome of the litigation. If the claim alleges a state of facts which, if proven, would fall within the coverage of the policy the insurer is obliged to defend the suit regardless of the truth or falsity of such allegations.

This principle was expanded upon by McLachlin J., for the Court in Nichols, supra, at pp. 810-11, in the following words cited in part above:

> Where it is clear from the pleadings that the suit falls outside of the coverage of the policy by reason of an exclusion clause, the duty to defend has been held not to arise: Opron Maritimes Construction Ltd. v. Canadian Indemnity Co. (1986), 19 C.C.L.I. 168 (N.B.C.A.), leave to appeal refused by this Court, [1987] 1 S.C.R. xi.
>
> At the same time, it is not necessary to prove that the obligation to indemnify will in fact arise in order to trigger the duty to defend. The mere possibility that a claim within the policy may succeed suffices. In this sense, as noted earlier, the duty to defend is broader than the duty [page597] to indemnify. O'Sullivan J.A. wrote in Prudential Life Insurance Co. v. Manitoba Public Insurance Corp. (1976), 67 D.L.R. (3d) 521 (Man. C.A.), at p. 524:

> Furthermore, the duty to indemnify against the costs of an action and to defend does not depend on the judgment obtained in the action. The existence of the duty to defend depends on the nature of the claim made, not on the judgment that results from the claim. The duty to defend is normally much broader than the duty to indemnify against a judgment. (Emphasis added.)

> In that case it was unclear whether the insurer might be liable to indemnify under the policy, so the duty to defend was held to apply. In the court's view it would have been unjust for the insurers to be able to assert that "the claim is probably groundless, or will probably end up falling outside of the indemnity coverage. Since we have no proof that we owe an indemnity in this case, we take the position that we owe no duty to defend".

**81** This does not, however, mean that the parties to an insurance contract are to be bound by the plaintiff's choice of labels, and thus defenceless against inaccurate or manipulative pleadings. Nichols only held that, having determined the nature of the claim, an insured need not further prove that the claim would succeed. This is just common sense, since otherwise an insured would have to prove he is actually liable in order to get an insurer to defend a liability claim.

**82** In my view, the correct approach in the circumstances of this case is to ask if the allegations, properly construed, sound in intentional tort. If they do, the plaintiff's use of the word "negligence" will not be controlling. The Rhode Island Supreme Court, in Peerless Insurance Co. v. Viegas, 667 A.2d 785 (1995), cleverly expressed the point as follows at p. 789:

[page598]

> In civil actions for damages that result from an act of child sexual molestation, an insurer will be relieved from its duty to defend and to indemnify its insured if the perpetrator is insured under a policy in which there is contained an intentional act exclusion provision... . The fact that the allegations in that complaint are described in terms of "negligence" is of no consequence. A plaintiff, by describing his or her cat to be a dog, cannot simply by that descriptive designation cause the cat to bark.

**83** To be somewhat more prosaic, when determining the scope of the duty to defend, courts must take the factual allegations as pleaded, but then ask which of the plaintiff's legal claims could potentially be supported by those factual allegations. This is clear from Bacon, supra, at p. 99, where the court limited the duty to defend to cases where the "claim alleges a state of facts which, if proven, would fall within ... coverage" (emphasis added). Similarly, in Nichols, supra, at p. 810, McLachlin J. cited with approval O'Sullivan J.A.'s direction to look at "the nature of the claim made".

**84** I would note that this approach can assist the insured, and not just the insurer. For example, as the California Supreme Court noted in Gray, supra, at p. 176,

> the complainant in the third party action drafts his complaint in the broadest terms; he may very well stretch the action which lies in only nonintentional conduct to the dramatic complaint that alleges intentional misconduct. In light of the likely overstatement of the complaint and of the plasticity of modern pleading, we should hardly designate the third party as the arbiter of the policy's coverage.

Conversely, a plaintiff may draft a statement of claim in a way that seeks to turn intention into negligence in order to gain access to an insurer's deep pockets. See E. S. Pryor, "The Stories We Tell: Intentional Harm and the Quest for Insurance Funding" (1997), 75 Tex. L. Rev. 1721, at p. 1735. A court must therefore look beyond the labels used by the plaintiff, and determine the true nature of [page599] the claim pleaded. It is important to emphasize that at this stage a court must not attempt to determine the merit of any of the plaintiff's claims. Instead, it should simply determine whether, assuming the verity of all of the plaintiff's factual allegations, the pleadings could possibly support the plaintiff's legal allegations.

**85** Having construed the pleadings, there may be properly pleaded allegations of both intentional and non-intentional tort. When faced with this situation, a court construing an insurer's duty to defend must decide whether the harm allegedly inflicted by the negligent conduct is derivative of that caused by the intentional conduct. In this context, a claim for negligence will not be derivative if the underlying elements of the negligence and of the intentional tort are sufficiently disparate to render the two claims unrelated. If both the negligence and intentional tort claims arise from the same actions and cause the same harm, the negligence claim is derivative, and it will be subsumed into the intentional tort for the purposes of the exclusion clause analysis. If, on the other hand, neither claim is derivative, the claim of negligence will survive and the duty to defend will apply. Parenthetically, I note that the foregoing should not preclude a duty to defend simply because the plaintiff has pleaded in the alternative. As Pryor, "The Stories We Tell: Intentional Harm and the Quest for Insurance Funding", supra, points out at p. 1752, "[p]laintiffs must have the freedom to plead in the alternative, to develop alternative theories, and even to submit alternative theories to the jury". A claim should only be treated as "derivative", for the purposes of this analysis, if it is an ostensibly separate claim which nonetheless is clearly inseparable from a claim of intentional tort.

**86** The reasons for this conclusion are twofold. First, as discussed above, one must always remember that insurance is presumed to cover only negligence, not intentional injuries. Second, this [page600] approach will discourage manipulative pleadings by making it fruitless for plaintiffs to try to convert intentional torts into negligence, or vice versa. While courts should not concern themselves with whether or not pleadings are designed to generate insurance coverage, following the guidelines set out above will provide insurers with sufficient protections against manipulative pleadings.

**87** These concepts may seem rather complicated in the abstract, but they are more straightforward to apply in practice. While this issue is relatively new to Canadian law, it has been extensively canvassed in the United States, where courts have denied insurance coverage for claims of negligent battery, negligent misrepresentation, negligent infliction of emotional distress, negligent interference with familial relations, and any other claim of "negligence" where it is derivative of an intentional sexual assault. For example, in Houg v. State Farm Fire and Casualty Co., 481 N.W.2d 393 (Minn. Ct. App. 1992), a parishioner sued a priest who had been counselling her for sexual assault. In addition to intentional sexual battery, the plaintiff alleged negligent counselling by the defendant.

**88** The court had little difficulty in finding that this allegation of negligence did not raise the duty to defend, because "[a]ny negligent counseling is so intertwined with [the insured]'s sexual exploitation of a psychologically dependent person as to be inseparable" (Houg, supra, at p. 397). To use the approach I have set out above, the negligent counselling claim was merely derivative of the sexual assault. The fact that there may have been negligent aspects of the priest's conduct will not change the essentially intentional nature of his conduct, for the purpose of the exclusion clause. To similar effect are: Linebaugh v. Berdish, 376 N.W.2d 400 (Mich. Ct. App. 1985) (denying a claim for "negligent" child molestation, which was "a transparent [page601] attempt to trigger insurance coverage by characterizing allegations of tortious conduct under the guise of 'negligent' activity" (p. 406)); Horace Mann Insurance Co. v. Leeber, 376 S.E.2d 581 (W. Va. 1988) (alleged negligent seduction of a child by a teacher (p. 587)); Allstate Insurance Co. v. Troelstrup, 789 P.2d 415 (Colo. 1990) (same (p. 418, n. 7)); Nationwide Mutual Fire Insurance Co. v. Lajoie, 661 A.2d 85 (Vt. 1995) (agreeing with the trial judge that "labeling [the insured]'s conduct as negligent 'is simply a disingenuous attempt to create a factual dispute'" (p. 86)); Colorado Farm Bureau Mutual Insurance Co. v. Snowbarger, supra ("[T]he only facts recited in the complaint concern the repeated acts of sexual assault. There are no factual allegations provided in the complaint to substantiate a negligence theory" (p. 912)).

**89** I wish to make it clear that I am not denying that a given state of facts may give rise to several different tort claims. For example, in M. (K.) v. M. (H.), [1992] 3 S.C.R. 6, the Court noted at p. 59 that "[i]ncest is a breach of both common law and equitable duties". The Court therefore held that limitation periods applying to intentional or negligent actions did not apply to claims for breach of fiduciary duty. While I fully agree with this proposition, I would note that the present appeal presents a distinct question. In the context of an insurance contract's intentional injury exclusion clause, the goal is to determine the gravamen of the complaint, and whether one can infer an intent to injure from that complaint. Limitations issues, as shown by M. (K.), are different, and not applicable in the present appeal. Indeed, this appeal's holding with respect to the proper characterization of a plaintiff's tort allegations should not be taken [page602] to affect any areas of law outside the insurance context presented by this appeal.

(iii) Conclusion on the Scope of the Insurer's Duty to Defend

**90** I therefore conclude that the respondent will only have to defend the appellant if the plaintiff's statement of claim alleges a state of facts that, properly construed, would support an action that could potentially fall within coverage.

C. Is There a Claim that Could Fall Within Coverage?

**91** There is no dispute in this case that the plaintiff's allegations fall within the general coverage provisions of the policy. All that is at stake is whether the exclusion clause applies. That clause states that the appellant is "not insured for claims arising from: ... bodily injury or property damage caused by any intentional or criminal act or failure to act" by the insured.

**92** At the outset, the wording of this clause presents a threshold issue. The respondent argues that the clause requires only an intentional act, not an intent to injure. The majority below agreed with this interpretation. However, I agree with Finch J.A.'s dissent on this point. If the respondent were correct, almost any act of negligence could be excluded under this clause. After all, most every act of negligence can be traced back to an "intentional ... act or failure to act". As this Court made

clear in Canadian Indemnity Co. v. Walkem Machinery & Equipment Ltd., [1976] 1 S.C.R. 309, "negligence is by far the most frequent source of exceptional liability which [an insured] has to contend with. Therefore, a policy which would not cover liability due to negligence could not properly be called 'comprehensive'" (pp. 316-17). Consistent with this decision, the purpose of insurance, and the doctrines of reasonable expectations and contra proferentem referred to above, I believe the exclusion clause must be read to require that the injuries be intentionally caused, in that they are the [page603] product of an intentional tort and not of negligence.

**93** Our task, therefore, is to decide which of the plaintiff's legal allegations are properly pleaded, whether any of them are derivative, and whether any of the surviving claims evince an intention to injure, thus triggering the exclusion clause. To do this, it is necessary to understand precisely what the elements of the various torts alleged against the appellant are. If the elements of a tort claim require proof of conduct that also proves an intent to injure, there will be no duty to defend because any potentially successful claim would fall under the exclusion clause.

**94** As will be seen from the following discussion, I conclude that each of the plaintiff's properly pleaded claims necessarily involves an intent to injure, because each requires proof that the appellant either knew, or should have known, that the plaintiff did not validly consent to sexual activity. Given this actual or constructive knowledge of non-consent, the law will not permit the appellant to claim that he did not intend any harm. The exclusion therefore applies because there is no claim against the appellant that, if successful, could potentially fall within coverage. There being no potentially indemnifiable claim, the respondent has no duty to defend.

(i) Sexual Battery

(a) Elements of the Tort of Sexual Battery

**95** The tort of sexual battery is a relatively new one. As Professor Feldthusen points out in "The Canadian Experiment with the Civil Action for [page604] Sexual Battery", in N. J. Mullany, ed., Torts in the Nineties (1997), 274, at p. 274, this action is one that has appeared more frequently in the last 15 years. The sexual battery action signals the possibility of "dramatic changes to the law of consent, to the action for breach of fiduciary duty, to the rules governing punitive damages, to the rules of discovery and to the law of evidence" (p. 275). However, this appeal requires no such changes. Contrary to McLachlin J.'s assertions, my approach entails nothing more than understanding how traditional tort law applies in the context of sexual battery.

**96** Sexual battery is a form of battery, the traditional test for which is relatively straightforward. In M. (K.), supra, at p. 25, La Forest J. defined assault and battery as "causing another person to apprehend the infliction of immediate harmful or offensive force on her person coupled with the actual infliction of that harmful or offensive force". What is notably absent from this definition is any intent to injure. Professor Klar, in his second edition of Tort Law (1996), makes this point at p. 42:

> For the tort of intentional battery, the defendant must have intended an offensive, physical contact with the plaintiff. The defendant need not have intended to harm or injure the plaintiff, although in most battery cases there is an intention to injure.

**97** A. M. Linden, in Canadian Tort Law (6th ed. 1997), emphasizes this point at p. 43: "A battery can be committed even though no harm or insult is intended by the contact. If the contact is offensive to the recipient, even if a compliment was intended, it is tortious." See also Wilson v. Prin-

gle, [1986] 2 All E.R. 440 (C.A.), at p. 445; Spivey v. Battaglia, 258 So.2d 815 (Fla. 1972); O. M. Reynolds, "Tortious Battery: Is 'I Didn't [page605] Mean Any Harm' Relevant?" (1984), 37 Okla. L. Rev. 717.

**98** Intentional battery generally requires only the intent to cause the physical consequences, namely, an offensive touching. Klar, supra, makes this point at p. 30:

> Technically, however, the concept of "intention" in the intentional torts does not require defendants to know that their acts will result in harm to the plaintiffs. Defendants must know only that their acts will result in certain consequences. It is not necessary for defendants to realize that these intended consequences are in fact an infringement of the legal rights of others. Intention, in other words, focusses on physical consequences.

To similar effect is Linden, supra, at p. 33: "Conduct is intentional if the actor desires to produce the consequences that follow from an act."

**99** Moreover, if a tort is intended, it will not matter that the result was more harmful than the actor should, or even could have foreseen. Linden, supra, at p. 45, quotes Borins Co. Ct. J. (as he then was) in Bettel v. Yim (1978), 20 O.R. (2d) 617, at p. 628:

> If physical contact was intended, the fact that its magnitude exceeded all reasonable or intended expectations should make no difference. To hold otherwise ... would unduly narrow recovery where one deliberately invades the bodily interests of another with the result that the totally innocent plaintiff would be deprived of full recovery for the totality of the injuries suffered as a result of the deliberate invasion of his bodily interests. [Emphasis added.]

**100** The appellant's argument, in light of the foregoing, is quite simple. Battery requires only intentional contact, not an intent to harm. Therefore, he could have had non-consensual sex with the plaintiff, thus committing battery, while thinking consent was present and thus not intending any harm. Any injuries could therefore have been unintentional, [page606] and the exclusion clause should not apply because a claim within coverage could succeed.

**101** The problem with the appellant's argument is that it fails to recognize the subtleties of intentional tort, particularly as they apply to sexual battery. The law of intentional tort has traditionally focussed on a different set of problems from those presented in cases of sexual battery. In traditional battery, which is what the above-cited authorities were considering, what is usually at stake is whether the defendant can be liable for unintended physical consequences of his or her intentional actions, as in Bettel, supra. In these cases, the plaintiff's consent is not in question because of the nature of the conduct. Punching, shooting, stabbing, or otherwise attempting to injure another person is clearly offensive, and we would not expect someone to consent to it. See, e.g., Long v. Gardner (1983), 144 D.L.R. (3d) 73 (Ont. H.C.); Veinot v. Veinot (1977), 81 D.L.R. (3d) 549 (N.S.C.A.); Rumsey v. The Queen (1984), 12 D.L.R. (4th) 44 (F.C.T.D.); Holt v. Verbruggen (1981), 20 C.C.L.T. 29 (B.C.S.C.). As Borins Co. Ct. J. said in Bettel, supra, at p. 627, defendants in these cases have acted "with intent to violate the interests of others" (quoting J. J. Atrens, "International Interference with the Person", in Studies in Canadian Tort Law (1968), 378). Consent simply is not an issue, and intent to injure is obvious.

**102** Moreover, even in those cases where intent to harm is less obvious, lack of consent usually is obvious. For example, Reynolds, supra, discusses various instances where courts have debated the need to show intent to harm. These cases typically involve childish pranks, see Garratt v. Dailey, 279 P.2d 1091 (Wash. 1955), Vosburg v. Putney, 50 N.W. 403 (Wis. 1891); unconsented medical treatment, [page607] see Reibl v. Hughes, [1980] 2 S.C.R. 880, Clayton v. New Dreamland Roller Skating Rink, Inc., 82 A.2d 458 (N.J. Super. Ct. App. Div. 1951); or unintended consequences, see Bettel, supra, Kirkpatrick v. Crutchfield, 100 S.E. 602 (N.C. 1919). In all of these situations, there is never any suggestion that the plaintiff consented to the battery; the focus instead is on whether the appellant intended any harm, and these cases have generally decided that no such intent is needed.

**103** What is necessary, therefore, is to decide what role consent plays in an action for sexual battery. It is clear that for traditional batteries, consent is conceived of as an affirmative defence that must be raised by the defendant. As Cartwright J. said in Cook v. Lewis, [1951] S.C.R. 830, at p. 839, "where a plaintiff is injured by force applied directly to him by the defendant his case is made by proving this fact and the onus falls upon the defendant to prove 'that such trespass was utterly without his fault'". Obviously, one way to make this showing, is by establishing that the plaintiff consented to the touching. Therefore in Norberg v. Wynrib, [1992] 2 S.C.R. 226, La Forest J. stated in obiter dictum that "[c]onsent, express or implied, is a defence to battery" (p. 246). See also Reibl, supra, at p. 890 (battery "casts upon the defendant the burden of proving consent to what was done"); Hambley v. Shepley (1967), 63 D.L.R. (2d) 94 (Ont. C.A.), at p. 95; Linden, supra, at p. 67; G. H. L. Fridman, The Law of Torts in Canada (1989), vol. 1, at p. 63. If consent is merely a defence to battery, then presumably the plaintiff could establish battery without showing lack of consent. To paraphrase Cartwright J. in Cook, the plaintiff's case would be made by showing the mere application of force by the defendant. As I understand it, this is the position taken by McLachlin J. However, I have trouble concluding on these terms that the appellant necessarily intended injury. Without a fault requirement of any kind, I cannot agree that the exclusion clause [page608] would necessarily apply, and the respondent would therefore have a duty to defend.

**104** This doctrine is of course consistent with our basic notions of intentional tort. A person's body is inviolable, and those who interfere with one's "intangible right to autonomy over one's own body" will be held liable: Klar, supra, at p. 41. However, not all intentional touchings are presumptively instances of battery. There are any number of contacts that are usually consensual. For example, in Mandel v. The Permanent (1985), 7 O.A.C. 365 (Div. Ct.), at p. 370, Henry J. noted that a man's placing his hand on the plaintiff's arm to guide her to the door was "merely a polite gesture and an accepted usage in daily life in a civilized society, whether or not she was in fact consenting to it". A more obvious example is certain sports, where physical contact is expected and even encouraged. What these examples show is that, in all cases, one must look to the context to understand the role of consent.

**105** While, for reasons already given, consent is not a well-developed concept in battery cases, it is closely related to the more familiar requirement in tort law that a given contact be "harmful or offensive" if it is to generate liability: see M. (K.), supra, at p. 25. Unlike more traditional batteries, sexual activity by itself is not inherently harmful. Without denying the seriousness and frequency of sexual assault, the simple fact is that sexual activity -- unlike being punched, stabbed, or shot -- is usually consensual. It generally becomes harmful only if it is non-consensual, in the wider meaning of that word. Without trying to catalogue the various [page609] ways that consent may be vitiated, I note that Norberg, supra, established that simply because someone ostensibly consents to sexual ac-

tivity does not mean that their consent is valid. See, generally, Feldthusen, "The Canadian Experiment with the Civil Action for Sexual Battery", supra, at pp. 282-86.

**106** That the "harmful or offensive" standard is a familiar one in tort law is shown by Wiffin v. Kincard (1807), 2 Bos. & Pul. (N.R.) 471, 127 E.R. 713 (C.P.), and Coward v. Baddeley (1859), 4 H. & N. 478, 157 E.R. 927 (Ex.). In those cases, the courts determined that touching someone on the shoulder to get their attention is not a battery, even if the recipient objected to the contact. As Linden, supra, at p. 44, points out:

> A line must be drawn between those contacts which are regarded as normal everyday events, which people must put up with in a crowded world, and those which are considered to be offensive and, therefore, unacceptable.

Klar, supra, at pp. 43-44, elaborates on this point:

> The distinction between "hostile" and "friendly" contact seems to depend upon the standard of generally acceptable conduct in society. The test is objective: what would the reasonable person consider to be acceptable? Two recent English cases demonstrate this proposition. In the first, Collins v. Wilcock, [1984] 1 W.L.R. 1172 (Q.B.), the act of a police officer in taking hold of someone's arm to restrain her from walking off was deemed to constitute a battery. The test suggested by Goff L.J. was this: "whether the physical conduct so persisted in has in the circumstances gone beyond generally acceptable standards of conduct." Ibid., at 1178... . In the second case, Wilson v. Pringle, [1986] 2 All E.R. 440 (C.A.), a schoolboy playfully pulled the schoolbag off the plaintiff's shoulder, causing him injury. In deciding whether this was a hostile touching and consequently a battery, Croom-Johnson L.J....agreed that certain conduct must be judged as [page610] "acceptable in the ordinary conduct of everyday life." [Emphasis added.]

**107** In England, courts have concluded that "[t]he absence of consent is so inherent in the notion of a tortious invasion of interests in the person that the absence of consent must be established by the plaintiff": Street on Torts (10th ed. 1999), at p. 32. This issue was decided by Freeman v. Home Office, [1983] 3 All E.R. 589 (Q.B.), aff'd [1984] 1 All E.R. 1036 (C.A.), where the court held that a prisoner suing for battery because of therapeutic drug injections had the burden of proving non-consent. While it is not necessary in this appeal to decide whether the burden of proving non-consent will always rest on the plaintiff, I believe that it should for sexual battery. To repeat, sexual contact is only "harmful or offensive" when it is non-consensual. To succeed in an action for intentional battery, one must prove both that (a) the defendant intended to do the action; and (b) the reasonable person would have perceived that action as being harmful or offensive. For sexual activity, an action is harmful or offensive if it is non-consensual. Therefore in sexual battery, the trier of fact must be satisfied that the defendant intended to engage in sexual activity which a reasonable person would have perceived to be non-consensual.

**108** The New Zealand High Court came to the same conclusion in H. v. R., [1996] 1 N.Z.L.R. 299, at p. 305:

> In sexual abuse cases, a conceptual difficulty with the tort has been as to whether an absence of consent is an element of the tort, or a defence. It seems to me that to the extent that it has always been necessary for the plaintiff to prove a hostile intent to ground this tort, the burden of demonstrating a lack of consent must be surmounted by the plaintiff, of course on the civil standard. I[f] that is so, lack of consent has always been, strictu sensu, an element of the offence.

[page611]

In short, the appellant's attempt to convert an intentional tort into negligence because of the possibility that he lacked a subjective intent to injure must fail. Consent, in so far as it is concerned with whether something is harmful or offensive, is an objective standard. If the plaintiff can prove that the appellant failed to meet this standard, the latter is liable for intentional sexual battery, not negligence.

**109** In summary, I would advance the following basic propositions. For there to be a duty to defend, there must be the possibility of a duty to indemnify. In the context of the pleadings in this case raising in substance a sexual assault through a sexual battery, the issue of consent produces two possible results for the purposes of the duty to defend, both of which are unfavourable to the appellant. If the consent of the plaintiff was present, then no claim of sexual battery is made out since the conduct of the appellant would not be regarded objectively as being harmful or offensive, and therefore the duty to indemnify would not arise because the plaintiff's claim has no possibility of success. See State Farm Fire and Casualty Co. v. Williams, 355 N.W.2d 421 (Minn. 1984), at p. 424. On the other hand, if consent of the plaintiff is absent, the conduct of the appellant would be actionable as an intentional tort of sexual battery. As I will discuss, infra, in such a case an intent to harm is inferred, the exclusion clause would apply, and there would be no duty to indemnify. There being no state of affairs in which there could be a duty to indemnify, the duty to defend does not apply.

**110** I wish to emphasize that the foregoing should not be taken to endorse in any way the inappropriate stereotype that women are to be presumed willing partners to sexual activity. See R. v. Mills, [1999] 3 S.C.R. 668, at para. 90; R. v. Osolin, [1993] 4 S.C.R. 595, at p. 670; R. v. Seaboyer, [1991] 2 S.C.R. 577, at p. 604; [page612] Federal/Provincial/Territorial Working Group of Attorneys General Officials on Gender Equality in the Canadian Justice System, Gender Equality in the Canadian Justice System: Summary Document and Proposals for Action (1992). Nothing in these reasons should be read to the contrary. Putting the onus of proving lack of consent on the plaintiff simply recognizes that in the sexual assault context, "non-consensual" is equivalent to "harmful or offensive"; and the latter has always been an element of the plaintiff's case.

**111** I would also emphasize that the plaintiff's burden in a civil action to prove non-consent is much less onerous than the one faced by the prosecution in a criminal case. As Major J. noted in R. v. Ewanchuk, [1999] 1 S.C.R. 330, at para. 42, the mens rea of criminal sexual assault requires the Crown to prove beyond a reasonable doubt that the accused was "knowing of, or being reckless of or wilfully blind to, a lack of consent on the part of the person touched". To prove the civil tort of sexual battery, by contrast, one need only prove by a balance of probabilities that the defendant knew or ought to have known that the plaintiff did not consent.

**112** The onus of proving consent will be largely of theoretical importance. To meet her initial burden, the plaintiff need simply allege that the sexual activity was non-consensual. The issue will then be the same regardless of where the onus lies: on the balance of probabilities, should the defendant have known that the plaintiff did not validly consent? The only time the plaintiff's burden of pleading non-consent would be relevant is in those rare cases where, for whatever reason, the defence chooses to present no evidence. In such a case, having the onus on the plaintiff ensures that the defendant will only be liable if the plaintiff alleges, at a minimum, that the sexual activity was non-consensual. While the practical difference is thus minimal, I believe the theoretical one is important. Placing the onus of proving lack of consent on the [page613] plaintiff better reflects our traditional notions of tort law, as adapted to the relatively new tort of sexual battery.

**113** Having concluded that in the context of sexual battery the "harmful or offensive" element is satisfied by showing lack of consent, I will now discuss whether the elements of a sexual battery claim necessarily prove an intent to injure on the part of the defendant. If a sexual battery claim requires proof of elements that also establish an intent to injure, then any successful claim would necessarily be excluded under the policy and there can be no duty to defend such a claim.

(b) Are There Properly Pleaded Allegations of Sexual Battery that Could Trigger the Duty to Indemnify?

**114** As set out above, the first step is to determine whether there are properly pleaded allegations of sexual battery. In my opinion, this requirement is clearly satisfied. The plaintiff has alleged intentional sexual activity by the appellant, to which the plaintiff did not consent. Moreover, para. 117 of the statement of claim specifically alleges that "Scalera knew or ought to have known that [the plaintiff] did not consent to the Scalera sexual acts". The next question is whether sexual battery necessarily implies an intent to injure sufficient to trigger the exclusion clause.

**115** This Court was presented with this issue, in a different context, in Norberg, supra. In that case the Court split three ways on the appropriate characterization of the actions of a doctor who convinced a drug-addicted patient to engage in sexual acts with him in return for pills to which she was addicted. This issue is not before the Court in this [page614] appeal. However, I will assume all three approaches set out in that case -- sexual battery, breach of duty, and breach of fiduciary duty -- are possible.

**116** Writing for himself, Gonthier and Cory JJ., La Forest J. concluded that Wynrib's conduct amounted to sexual assault. Drawing an analogy to contract law, La Forest J. concluded that consent may be vitiated where "there is an overwhelming imbalance in the power relationship between the parties" (p. 248). If there was no valid consent, Wynrib was liable for battery.

**117** What La Forest J.'s reasons left undecided is whether or not Wynrib had any intent to harm, or indeed whether such intent is necessary for sexual battery. La Forest J. did not inquire into subjective intent to harm, but instead focused on the presence or absence of valid consent. This approach is consistent with the few reported lower court decisions addressing sexual assault. For example, in M. (M.) v. K. (K.) (1989), 61 D.L.R. (4th) 392 (B.C.C.A.), the court concluded that notwithstanding the fact that the victim initiated the sexual contact, there could be no valid consent between a 41-year-old man and his 15-year-old foster daughter. Harder v. Brown (1989), 50 C.C.L.T. 85 (B.C.S.C.), and Lyth v. Dagg (1988), 46 C.C.L.T. 25 (B.C.S.C.), similarly declined to consider intention to harm, instead finding that consent was vitiated by the extreme power imbalances in the relationships.

**118** One conclusion that could be drawn from these cases is that sexual battery requires no intent to harm, only the absence of consent. If this is correct, the exclusion clause would not necessarily apply to a sexual battery claim, and the respondent would have a duty to defend. However, in my view [page615] this interpretation is not correct. Consent, linked as it is to the "harmful or offensive" standard, as already discussed, is an objective standard. Sexual battery requires an objective set of circumstances such that the defendant either knew or should have known that there was no valid consent.

**119** Leaving aside the physical injuries that can be inflicted by sexual assault, there can be no question that it occasions untold injury to the victim's dignity, physical integrity, and psychological well-being. The same facts that prove lack of consent will prove intent to injure; this follows because if a reasonable person should have known there was no consent, the law will not excuse that person's failure to perceive the lack of consent. On the other hand, a defendant will not be liable for sexual assault if there was no way for him or her to know that the victim did not, or could not, consent to sexual activity.

**120** This Court has recognized the grave harm occasioned by sexual assault. For example, in R. v. McCraw, [1991] 3 S.C.R. 72, the Court held that threats of rape amounted to threats of serious bodily harm, within the meaning of s. 264.1(1)(a) of the Criminal Code. Cory J. aptly summarized the harm inherent in non-consensual sexual activity, at pp. 83-84:

> It seems to me that to argue that a woman who has been forced to have sexual intercourse has not necessarily suffered grave and serious violence is to ignore the perspective of women. For women rape under any circumstance must constitute a profound interference with their physical integrity. As well, by force or threat of force, it denies women the right to exercise freedom of choice as to their partner for sexual relations and the timing of those relations. These are choices of great importance that may have a substantial effect upon the life and health of every woman. Parliament's intention in replacing the rape laws with the sexual assault offences was to convey the message that rape is not just a sexual act but is basically an act of violence. See K. [page616] Mahoney, "R. v. McCraw: Rape Fantasies v. Fear of Sexual Assault" (1989), 21 Ottawa L. Rev. 207, at pp. 215-16.

See also Osolin, supra, at p. 669; Ewanchuk, supra, at para. 69 (per L'Heureux-Dubé J.). While McCraw was concerned with forcible rape, I do not think the harm is any less real just because the victim has been coerced into sex by mental as opposed to physical means. It can hardly be disputed, I think, that any type of non-consensual sex clearly evinces an intent to harm the victim thereof.

**121** In the considerable jurisprudence on the point, most U.S. courts have reached the same conclusion. The majority of these cases have involved sexual assaults of children. Courts have had little difficulty in concluding that defendants in these cases are presumed to intend harm to their victims -- notwithstanding the fact that "males who are involved in such activities do not expect or intend that the females will sustain any injury": CNA Insurance Co. v. McGinnis, 666 S.W.2d 689 (Ark. 1984), at p. 690. See also B.B. v. Continental Insurance Co., 8 F.3d 1288 (8th Cir. 1993); J.C. Penney Casualty Insurance Co. v. M.K., 804 P.2d 689 (Cal. 1991); Horace Mann Insurance Co. v. Leeber, supra; State Farm Fire & Casualty Co. v. D.T.S., 867 S.W.2d 642 (Mo. Ct. App. 1993); Amercian States Insurance Co. v. Borbor, 826 F.2d 888 (9th Cir. 1987); Troelstrup v. District

Court, 712 P.2d 1010 (Colo. 1986) (en banc); Rodriguez v. Williams, 729 P.2d 627 (Wash. 1986) (en banc); Linebaugh v. Berdish, supra; Horace Mann Insurance Co. v. Independent School District No. 656, 355 N.W.2d 413 (Minn. 1984). These cases are obviously much easier than the present appeal. It is difficult to imagine someone successfully arguing that they intended no harm from sex with someone too young to consent to sexual activity.

[page617]

**122** While there is more of a divergence of opinion when it comes to assaults on adults, some U.S. courts have also inferred an intent to harm in these cases. For example, in State Farm Fire and Casualty Co. v. Williams, supra, the court denied insurance coverage to someone who had sexually assaulted a man with cerebral palsy who was confined to a wheelchair. The court first examined cases involving assaults on minors, and concluded as follows, at p. 424:

> Does the fact that Williams, the victim, was an adult distinguish this case? We think not. Neither the insured nor the insurer in entering into the insurance contract contemplated coverage against claims arising out of non-consensual sexual assaults. On the other hand, if the sexual contacts were consensual, as asserted by respondent Keller, there would be no assault and hence no claim for recovery.

See also Houg, supra; Altena v. United Fire and Casualty Co., 422 N.W.2d 485 (Iowa 1988); and D. S. Florig, "Insurance Coverage for Sexual Abuse or Molestation" (1995), 30 Tort & Ins. L.J. 699.

**123** Finally, I would note that the Canadian case most directly on point has reached a similar conclusion. Wilkieson-Valiente v. Wilkieson, [1996] I.L.R. para. I-3351 (Ont. Ct. (Gen. Div.)), involved an action by a young girl against her stepfather. The court disagreed with the defendant's assertion that "it is possible to commit a sexual assault without necessarily 'intending' injury" (p. 4132). Instead, the court concluded as follows at p. 4133:

> It may be conceivable, in rare circumstances, to commit a sexual assault without an intent to cause any psychological harm, (such as in the case of a transitory touching of a sleeping or unconscious victim). However, bearing in mind that "intentionally" does not refer to "desired result" but "awareness of possible result" such cases will be rare indeed. Particularly, as here, where the pleadings claim repeated sexual assaults over a period of many years on a victim who is a child, it is inconceivable that any right-thinking person would not be fully [page618] aware of the possible, indeed probable consequences of such conduct; that is, psychological harm to the victim.

**124** Unlike the Court in Wilkieson-Valiente, supra, I cannot accept that one can commit sexual assault without an intent to harm: see Linden, supra, at p. 45; Restatement (Second) of Torts, s. 18 cmt. d (1965). Even if the victim is unconscious, the perpetrator has still violated another person's physical integrity. However, I agree that to prove sexual assault, a plaintiff must prove sufficient culpability on the part of the defendant that an intent to harm follows. Accordingly, the exclusion clause must apply, and the respondent has no duty to defend the plaintiff's claim of sexual battery.

(ii) Negligent Battery

(a) Elements of Negligent Battery

**125** Klar, supra, defines negligent battery at p. 47:

> A negligent battery exists when the defendant causes a direct, offensive, physical contact with the plaintiff as a result of negligent conduct. The defendant's negligence consists of unreasonably disregarding a foreseeable risk of contact, even though the contact was neither desired nor substantially certain to occur.

The plaintiff has also alleged breach of duty, which is essentially negligence. In Norberg, supra, Sopinka J. relied on this theory to find Dr. Wynrib liable to Ms. Norberg. However, his reasoning was based on the professional duty owed by a physician to a patient. No such duty was alleged in the present appeal. Instead, and absent any particularized pleading by the plaintiff, I must presume that [page619] she is relying on a traditional negligent battery theory.

**126** As Klar's definition makes clear, the "negligence" in negligent battery refers only to the "risk of contact". One might commit negligent battery by carelessly stretching one's arms, thereby striking someone. More commonly, negligent battery cases have involved projectiles. See Cook, supra; Ellison v. Rogers (1967), 67 D.L.R. (2d) 21 (Ont. H.C.); Hatton v. Webb (1977), 81 D.L.R. (3d) 377 (Alta. Dist. Ct.). The important point is that negligent battery is concerned with the physical consequences of one's actions. However, the appellant has not disputed the physical consequence of his actions for the purposes of this appeal. He has, appropriately, assumed the truth of the allegations contained in the plaintiff's Statement of Claim, which asserts that he intended to have sexual relations with the plaintiff. The only question is whether it was consensual, which is determined on an objective standard, as I have explained above.

**127** I therefore do not find Co-operative Fire & Casualty Co. v. Saindon, supra; Newcastle (Town) v. Mattatall (1988), 52 D.L.R. (4th) 356 (N.B.C.A.); Long Lake School Division No. 30 of Saskatchewan Board of Education v. Schatz (1986), 18 C.C.L.I. 232 (Sask. C.A.), and Devlin v. Co-operative Fire & Casualty Co. (1978), 90 D.L.R. (3d) 444 (Alta. C.A.), to be relevant. These cases are not helpful in the present appeal, as they all involved unforeseen physical consequences of the actions of the insured, and asked whether the result was "substantially certain" given the defendant's actions. The "substantial certainty" test, focusing as it does on physical consequences, has no bearing on the issue of consent. The case at bar involves deciding solely whether the plaintiff validly consented to the appellant's actions. A negligent battery is properly pleaded only if the plaintiff alleges that the appellant was negligent as to the physical consequences of his actions; in other words, that he did not intend for sexual contact to [page620] occur. As explained above, lack of intention to have non-consensual sex is more properly construed as going to the "harmful or offensive" element of intentional battery, and will not found a claim for negligent battery. Therefore negligent battery will only be relevant if the pleadings allege that the appellant negligently harmed the plaintiff by disregarding a foreseeable risk of physical contact. No such allegation has been made. As the court said in Pistolesi v. Nationwide Mutual Fire Insurance Co., 644 N.Y.S.2d 819 (App. Div. 1996), at p. 820:

> ... the mere allegation that the injuries were the unintended result of an intentional act does not convert the cause of action from one sounding in intentional tort to one sounding in negligence... .

(b) Are There Properly Pleaded Allegations of Negligent Battery That Could Trigger the Duty to Indemnify?

**128** Once again, the first step is to determine whether negligent battery was properly pleaded. I have concluded that it was not. As discussed above, negligent battery occurs when the defendant causes harm by negligently disregarding a foreseeable risk of physical contact. The plaintiff has not alleged such conduct; both parties have assumed, for the purposes of this appeal, that the appellant intended to have sexual contact with the plaintiff. Since there is no properly pleaded allegation of negligent battery, it is unnecessary to determine whether the exclusion clause would apply to such a claim.

(iii) Negligent Misrepresentations

**129** Aside from the vague assertions of "breach of duty", the appellant notes that the plaintiff has [page621] alleged negligent acts independent of the sexual assault. For example, the statement of claim alleges negligent misrepresentations. It is unnecessary to spend much time on this issue. It is well established that one can be liable for damages to personal security caused by negligent statements, as well as acts:

> A statement of fact, on which the plaintiff relied, would give rise to liability if (i) it were inaccurate as a result of negligence (and a fortiori deceit); and (ii) it caused physical injury to the plaintiff or damage to his property.
>
> (Fridman, supra, at p. 263.)

See also Klar, supra, at p. 177; M'Alister v. Stevenson, [1932] A.C. 562 (H.L.), at pp. 580-81 (per Atkin L.J.).

**130** Assuming without deciding that negligent misrepresentation has been properly pleaded here, I find that these claims are entirely derivative of the intentional sexual battery, and are thus subsumed into the latter for the purposes of the exclusion clause. The statement of claim alleges that the misrepresentations were designed to seduce the plaintiff, and convince her to engage in sexual activity with the appellant. As such, they were entirely subservient to the sexual battery. They arise from the same actions and cause the same harm. Indeed, para. 111 of the plaintiff's statement of claim alleges that the appellant "made the Scalera Representations intending to persuade [the plaintiff] to submit to the Scalera sexual acts". The West Virginia Supreme Court of Appeals reached the same conclusion in Horace Mann Insurance Co. v. Leeber, supra, at p. 587, where an exclusion clause applied in spite of allegations of negligent seduction of a student by a teacher. The court concluded that the allegations of "negligence" in the complaint were

> a transparent attempt to trigger insurance coverage by characterizing allegations of [intentional] tortious conduct [page622] under the guise of 'negligent' activity. [Insertion in Leeber; quoting Linebaugh, supra, at p. 406.]

I reach the same conclusion in this appeal. While courts must be careful not to restrict pleading in the alternative unduly and should only subsume allegations of negligence that are clearly derivative of the intentional tort, I conclude that this is one of those cases. The plaintiff has clearly alleged intentional conduct by the appellant. Without ruling out the possibility that the plaintiff's pleadings could support claims of both intention and negligence as a matter of tort law, I conclude as a matter of insurance law that the negligent claims are subsumed for the purposes of the exclusion clause. The allegations of negligent misrepresentation are derivative of the intentional sexual assault claims, and cannot trigger the duty to defend.

(iv) Breach of Fiduciary Duty

**131** The final approach to allegations of sexual misconduct in Norberg, supra, was the fiduciary duty route taken by McLachlin J., L'Heureux-Dubé J. concurring. They concluded that the duty owed from a doctor to the patient met the test for fiduciary relationships set out by Wilson J. in Frame v. Smith, [1987] 2 S.C.R. 99, at p. 136. No doubt relying on these reasons, the plaintiff has also alleged breach of fiduciary duties against the appellant.

**132** Without commenting on whether the relationship between the appellant and the plaintiff could potentially be characterized as a fiduciary one, the plaintiff's claims for breach of fiduciary duty are excluded much for the same reasons as the negligence claims. Looking beyond the label to what is actually alleged in the pleadings, and without expressing any opinion on the validity of a fiduciary duty claim on the facts of this appeal, there are no facts pleaded to suggest that the breach of fiduciary [page623] duty was anything but intentional in nature. The appellant was alleged to have intentionally seduced the plaintiff, and whether or not this can be characterized as a fiduciary duty claim, any injuries resulting therefrom were caused intentionally. The harm caused by any breach of fiduciary duty is identical to that caused by the sexual battery, and the claim is therefore subsumed, for the purpose of the exclusion clause, into the intentional battery.

(v) Conclusion

**133** In summary, all of the plaintiff's claims against the appellant are covered by the exclusion clause for injuries caused intentionally. To prove her case, the plaintiff will have to establish that the appellant knew or should have known that the plaintiff did not validly consent to sexual relations with him. In such a situation, the appellant will not be heard to complain that he did not intend any harm. One who engages in objectively non-consensual sexual activity will be presumed to have intended harm; whether or not he subjectively intended harm will not change the injurious nature of his actions, and will not deny an insurer its bargained-for exclusion of intentionally injurious activities. This conclusion is consistent with the basic principles of insurance law discussed above.

**134** In particular, it is consistent with the reasonable expectations of the parties. In this respect, I agree with the Iowa Supreme Court in Altena, supra, at p. 490, where the court quoted the following passage from Rodriguez by Brennan v. Williams, 713 P.2d 135 (Wash. Ct. App. 1986), at pp. 137-38:

> ... [t]he average person purchasing homeowner's insurance would cringe at the very suggestion that [the person] was paying for such coverage. And certainly [the person] would not want to share that type of risk with [page624] other homeowner's policy holders. [Insertions added in Altena.]

Similarly, in Horace Mann Insurance Co. v. Leeber, supra, at pp. 586-87, the court said the following:

> The majority rule rejecting an alleged duty to defend or to pay in sexual misconduct liability insurance cases is consistent with the "doctrine of reasonable expectations." ... [W]e simply believe that the insured under a homeowner's insurance policy does not reasonably expect the insurer to defend an action against the insured for, and to pay for, damages alleged to have been caused by the sexual misconduct of the insured.

See also R. Bell, "Sexual Abuse and Institutions: Insurance Issues" (1996), 6 C.I.L.R. 53, at pp. 54-55.

**135** This conclusion is also consistent with basic insurance theory. Insurance is meant to cover risk of loss. See C. Brown, Insurance Law in Canada (loose-leaf), vol. 1, at p. 1-1. Where the loss is caused intentionally, it is hardly the result of a risk. Regardless of whether an insurance company could find a way profitably to insure someone against intentionally caused injuries, the respondent clearly did not believe it was doing so when it wrote the policy at issue in this appeal. Sexually assaulting someone is not like getting in a car accident, or having someone injure themselves by slipping on an unshovelled sidewalk. If the plaintiff is to succeed, she must prove that the appellant's conduct went beyond mere negligence, and rose to the level of sexual assault. Absent express language to the contrary, I am unable to conclude that the parties to this insurance contract agreed to cover such a claim.

**136** Nor do I believe that contra proferentem, or any other insurance principle, is sufficient to overcome these conclusions. While ambiguous language will often be construed against the insurer, this consideration alone cannot be determinative. Moreover, I find that the most accurate reading of the language [page625] and intentions of the contract is that the exclusion clause applies to the allegations of sexual misconduct made by the plaintiff.

### D. Other Arguments Raised by the Respondent

**137** The respondent has also argued that the actions alleged by the plaintiff are not "accidents" or "occurrences", as required by the policy, and that s. 28 of the British Columbia Insurance Act, excludes the claim because it alleges a criminal act. Given my interpretation of the exclusion clause, I find it unnecessary to consider these other questions and therefore express no opinion on them.

## VI. Summary and Disposition

**138** I believe my conclusions in this appeal can be summarized fairly briefly:

1. An insurance company only has a duty to defend when a lawsuit against the insured raises a claim that could potentially fall within coverage.
2. In determining if a claim falls within coverage, courts are not bound by the labels chosen by the plaintiff, but must determine the true nature of the claim stated in the pleadings.

3. In this appeal, the plaintiff has stated three possible claims arising out of an alleged sexual assault: sexual battery, negligent battery, and breach of fiduciary duty.

   None of these claims could potentially fall within coverage because, even if ultimately successful, the respondent will have no duty to indemnify owing to the insurance policy's exclusion for injuries caused intentionally by the insured.

   a. Sexual battery requires proof that a reasonable person should have known that the plaintiff did not validly consent to the sexual activity in question. Since non-consensual [page626] sexual activity is inherently harmful, any injuries resulting therefrom are intentionally caused, and the exclusion clause would apply. If, to the contrary, a reasonable person would not have known that the plaintiff did not validly consent, the plaintiff's claim will fail, there will be no duty to indemnify, and therefore equally no duty to defend.
   b. Claims of negligence and breach of fiduciary duty are either not properly pleaded, or are subsumed into the sexual battery in this case because these claims are based on the same facts and resulted in the same harm. Therefore the exclusion clause applies equally to them.

4. Since there is no possible set of circumstances in which one of the plaintiff's claims could trigger indemnity, there is no duty to defend.

**139** For the foregoing reasons, I would dismiss the appeal with costs.

cp/d/qlhbb

# Tab 15

1983 CarswellNat 123, [1983] C.T.C. 20, [1983] 1 S.C.R. 29, [1983] 2 C.N.L.R. 89, 46 N.R. 41, 144 D.L.R. (3d) 193, 83 D.T.C. 5041, J.E. 83-140

1983 CarswellNat 123, [1983] C.T.C. 20, [1983] 1 S.C.R. 29, [1983] 2 C.N.L.R. 89, 46 N.R. 41, 144 D.L.R. (3d) 193, 83 D.T.C. 5041, J.E. 83-140

Nowegijick v. R.

Gene A Nowegijick, Appellant, and Her Majesty The Queen, Respondent, and The Grand Council of the Crees (of Quebec) et al, and Chief Henry Mianscum, et al and Grand Chief Billy Diamond, et al and The National Indian Brotherhood, Intervenants

Supreme Court of Canada

Ritchie, Dickson, Beetz, Estey, McIntyre, Chouinard and Lamer, JJ

Judgment: January 25, 1983


Proceedings: on appeal from a judgment of the Federal Court of Appeal, reported [1979] C.T.C. 441

Counsel: *Micha Menczes* for the appellant.

*Wilfred Lefebvre* and *Fred Caron* for the respondent.

*James O'Reilly* (for the Crees) and *William Badcock* (National Indian Brotherhood) for the intervants.

Subject: Income Tax (Federal)

Income tax --- Exemptions — Indians — General

Income tax --- Persons liable

Income tax --- Income from office or employment

Income tax — Federal — Income Tax Act, RSC 1952, c 148 (am SC 1970-71-72, c 63) — 2(1), (2), 5(1) — Indian Act, RSC 1970, c 1-6 — 87 — Whether wages of an Indian, resident on a reserve, received from a corporation, resident on the reserve, exempt from income tax.

The appellant, an Indian who resided on an Indian reserve, was employed as a logger by a corporation which had its head office and administrative offices on the reserve. The logging operations were conducted 10 miles from the reserve. The appellant was paid by cheque at the corporation's office on the reserve. The appellant appealed from an assessment of income tax on the grounds that the tax was a tax in respect of personal property of an Indian situated on a reserve and therefore exempt under the *Indian Act*.

1983 CarswellNat 123, [1983] C.T.C. 20, [1983] 1 S.C.R. 29, [1983] 2 C.N.L.R. 89, 46 N.R. 41, 144 D.L.R. (3d) 193, 83 D.T.C. 5041, J.E. 83-140

**HELD:**

The fact that the services were performed off the reserve was not relevant. The *situs* of the appellant's wages was on the reserve because that was the residence of the employer corporation and it was where the wages were payable. Income was personal property and a tax on income was a tax in respect of personal property within the meaning of section 87 of the *Indian Act* which created an exemption for both persons and property. Appeal allowed.

**Annotation**

This case holds that the wages of an Indian, residing on an Indian reserve, received from an employer, also residing on the reserve, were personal property situated on a reserve within the meaning of section 87 of the *Indian Act* and, therefore, exempt from income tax. Although the decision is relatively narrow in its application, it raises several points of interest.

It was held that the *situs* of the wages was where the debtor (ie, the employer) was resident and where the wages were payable. It was considered to be irrelevant that in fact the services were rendered outside the reserve. This matter of the *situs* of wages is not likely material except for Indians. For example the definition of source of income in paragraph 4(1)(b) of the *Income Tax Act* refers to the place where the duties of an office or employment are performed. Similarly in the case of non-residents the reference in subparagraph 115(1)(a)(i) is to duties "performed by him in Canada". In Article 15 of the Canada-UK Tax Convention the place where the employment "is exercised" is the test. This language is also used in tax conventions with other countries.

The Court also held that wages were personal property and that income tax was in reality a tax on property. The Court distinguished earlier decisions which held that income taxes were taxes on a person and not on property on the grounds that those decisions were not applicable in interpreting the broad language of section 87 of the *Indian Act* so as to contradict the earlier decisions referred to in the judgment. Although wages are "property" it should be noted that sections 5 to 8 specifically set forth how salary and wages are to be dealt with under the Act whereas in section 9 and in subsections 12(1) and 18(1), for example, the reference is to income *from* property and not to property itself.

Another interesting feature is that the Court quoted a departmental Interpretation Bulletin stating that, although administrative policy and interpretation are not determinative, they are entitled to weight and can be an important factor in case of doubt about the meaning of legislation.

**Cases referred to:**

*The Queen* v *National Indian Brotherhood*, [1979] 1 F.C. 103, [1978] C.T.C. 680, 78 D.T.C. 6488;

*Jones v. Meehan*, 175 US 1;

*Greyeyes* v *The Queen*, [1978] C.T.C. 91, 78 D.T.C. 6043;

*Harel* v *Dep Min of Revenue for Quebec*, [1978] 1 S.C.R. 851, [1977] C.T.C. 441;

*Bachrach v. Nelson*, [1932] 182 NE 909;

*MNR* v *Iroquois of Caughnawaga*, [1977] 2 F.C. 269, [1977] C.T.C. 49, 77 D.T.C. 5127;

*McLeod* v *Min of C and E*, [1926] S.C.R. 457; [1917-27] CTC 290;

*Kerr* v *Sup of Income Tax*, [1942] S.C.R. 435, [1943] C.T.C. 97;

*Sura* v *MNR*, [1962] S.C.R. 65, [1962] C.T.C. 1, 62 D.T.C. 1005;

*Alworth v. Min of Finance* (1977) 76 D.L.R. (3d) 99;

*A-G British Columbia* v *Ellett Estate*, [1980] 2 S.C.R. 466, [1980] C.T.C. 338.

***Dickson, J:***

1 The question is whether the appellant, Gene A Nowegijick, a registered Indian can claim by virtue of the *Indian Act*, RSC 1970 c I-6, an exemption from income tax for the 1975 taxation year.

**I**

2

**The Facts:**

3 The facts are few and not in dispute. Mr Nowegijick is an Indian within the meaning of the *Indian Act* and a member of the Gull Bay (Ontario) Indian Band. During the 1975 taxation year Mr Nowegijick was an employee of the Gull Bay Development Corporation, a company without share capital, having its head office and administrative offices on the Gull Bay Reserve. All the directors, members and employees of the Corporation live on the Reserve and are registered Indians.

4 During 1975 the Corporation in the course of its business conducted a logging operation 10 miles from the Gull Bay Reserve. Mr Nowegijick was employed as a logger and remunerated on a piece-work basis. He was paid bi-weekly by cheque at the head office of the Corporation on the Reserve.

5 During 1975, Mr Nowegijick maintained his permanent dwelling on the Gull Bay Reserve. Each morning he would leave the Reserve to work on the logging operations, and return to the Reserve at the end of the working day.

6 Mr Nowegijick earned $11,057.08 in such employment. His assessed taxable income for the 1975 taxation year was $8,698 on which he was assessed tax of $1,965.80. By notice of objection he objected to the assessment on the basis that the income in respect of which the assessment was made is the "personal property of an Indian ... situated on a reserve" and thus not subject to taxation by virtue of section 87 of the *Indian Act*.

7 Mr Nowegijick also brought an action in the Federal Court, Trial Division to set aside the notice of assessment. Mr Justice Mahoney of that Court ordered that Mr Nowegijick's 1975 income tax return be referred back to the Minister of National Revenue for reassessment on the basis that the wages paid him by the Gull Bay Development Corporation were wrongly included in the calculation of his taxable income.

8 The Crown appealed the decision of Mr Justice Mahoney. The Federal Court of Appeal allowed the appeal and restored the original assessment.

9 The proceedings have reached this Court by leave. The Grand Council of Crees of Quebec, three Cree organizations, eight Cree bands and their respective Chiefs have intervened to make common cause with Mr Nowegijick.

**II**

10

**The Legislation**

11 Mr Nowegijick, in his claim for exemption from income tax relies upon section 87 of the *Indian Act*:

> Notwithstanding any other Act of the Parliament of Canada or any Act of the legislature of a province, but subject to subsection (2) and to section 83, the following property is exempt from taxation, namely:
>
> (a) the interest of an Indian or a band in a reserve or surrendered lands; and
>
> (b) the personal property of an Indian or band situated on a reserve;
>
> and no Indian or band is subject to taxation in respect of the ownership, occupation, possession or use of any property mentioned in paragraph (a) or (b) or is otherwise subject to taxation in respect of any such property; and no succession duty, inheritance tax or estate duty is payable on the death of any Indian in respect of any such property or the succession thereto if the property passes to an Indian, nor shall any such property be taken into account in determining the duty payable under the *Dominion Succession Duty Act*, being chapter 89 of the Revised Statutes of Canada, 1952, or the tax payable under the *Estate Tax Act*, on or in respect of other property passing to an Indian.

Section 83 of the *Indian Act*, referred to in section 87 has no application. Subsection 87(2), also mentioned, was repealed in 1960 by SC 1960, c 8, although the reference to it in what was formerly subsection (1) remains.

12 Stripped to relevant essentials section 87 reads:

> Notwithstanding any other Act of the Parliament of Canada the following property is exempt from taxation, namely
>
> (a) the interest of an Indian or a band in reserve or surrendered lands, and
>
> (b) the personal property of an Indian or band situated on a reserve;
>
> and no Indian or band is subject to taxation in respect of the ownership, occupation, possession or use of any property mentioned in paragraph (a) or (b) or is otherwise subject to taxation in respect of any such property ...

13 Further distilled, the section provides that (i) the personal property of an Indian situated on a reserve is exempt from taxation; (ii) no Indian is subject to taxation "in respect of any" such property.

14 It is arguable that the first part of the quoted passage which exempts from taxation (a) the "interest of an Indian or a band in a reserve or surrendered lands" and (b) the "personal property of an Indian or band situated on a reserve", is concerned with exemption from *direct* taxation of land or personal property by a provincial or municipal authority. The legislative history of the section lends support to such an argument. But the section does not end there. It is to the latter part of the section that our attention should primarily be directed.

15 The short but difficult question to be determined is whether the tax sought to be imposed under the *Income Tax Act* 1970-71-72, c 63 upon the income of Mr Nowegijick can be said to be "in respect of any" personal property situated upon a reserve.

16 We need not speculate upon parliamentary intention, an idle pursuit at best, since the antecedent of section 87 of the *Indian Act* was enacted long before income tax was introduced as a temporary war-time measure in 1917.

17 One point might have given rise to argument. Was the fact that the services were performed off the reserve relevant to *situs*? The Crown conceded in argument, correctly in my view, that the *situs* of the salary which Mr Nowegijick received was sited on the reserve because it was there that the residence or place of the debtor, the Gull Bay Development Corporation, was to be found and it was there the wages were payable. See Cheshire *Private International Law* (10th ed) pp 536 *et seq* and also the judgment of Thurlow, ACJ in *R* v *National Indian Brotherhood*, [1979] 1 F.C. 103 particularly at pp 109 *et seq*.

18 The other piece of legislation which bears directly on the question before us is the *Income Tax Act*. I would like to refer to several sections. The first is found in Part I, Division A, of the Act, entitled "Liability for Tax". Subsections 2(1), (2) provide:

> (1) An income tax shall be paid as hereinafter required upon the taxable income for each taxation year of every person resident in Canada at any time in the year.
>
> (2) The taxable income of a taxpayer for a taxation year is his income for the year minus the deductions permitted by Division C.

Thus, income tax is paid upon the taxable income (income minus deductions) of every person resident in Canada.

19 Subsection 5(1) of the Act is worth noting. It defines the taxpayer's income from employment as the salary, wages and other remuneration received. The liability is at the point of receipt. The section reads:

> Subject to this Part, a taxpayer's income for a taxation year from an office or employment is the salary, wages and other remuneration, including gratuities, received by him in the year.

The only other section is subsection 153(1) which provides that every person paying salary or wages to an employee in a taxation year shall deduct the prescribed amount, and remit that amount to the Receiver General of Canada on account of the payee's tax for the year.

**III**

20

**The Federal Court Judgments**

21 I turn now to the conflicting views in the Federal Court. The opinion of Mr Justice Mahoney at trial was expressed in these words:

> The question is whether taxation of the Plaintiff in an amount determined by reference to his taxable income is taxation "in respect of" those wages when they are included in the computation of his taxable income. I think that it is.
>
> The tax payable by an individual under the *Income Tax Act* is determined by application of prescribed rates to his taxable income calculated in the prescribed manner. If his taxable income is increased by the inclusion of his wages in it, he will pay more tax. The amount of the increase will be determined by direct reference to the amount

> of those wages. I do not see that such a process and result admits of any other conclusion than that the individual is thereby taxed in respect of his wages.

22 The Federal Court of Appeal concluded that the tax imposed on Mr Nowegijick under the *Income Tax Act* was not taxation in respect of personal property within the meaning of section 87 of the *Indian Act*. The Court, speaking through Mr Justice Heald, said:

> We are all of the view that there are no significant distinctions between this case and the *Snow* case (*Russell Snow v The Queen*, [1979] C.T.C. 227) where this Court held: "Sec 86 of the *Indian Act* contemplates taxation in respect of specific personal property *qua* property and not taxation in respect of taxable income as defined by the *Income Tax Act*, which, while it may reflect items that are personal property, is not itself personal property but an amount to be determined as a matter of calculation by application of the provisions of the Act".

**IV**

23

**Construction of section 87 of the Indian Act**

24 Indians are citizens and, in affairs of life not governed by treaties or the *Indian Act*, they are subject to all of the responsibilities, including payment of taxes, of other Canadian citizens.

25 It is legal lore that, to be valid, exemptions to tax laws should be clearly expressed. It seems to me, however, that treaties and statutes relating to Indians should be liberally construed and doubtful expressions resolved in favour of the Indian. If the statute contains language which can reasonably be construed to confer tax exemption that construction, in my view, is to be favoured over a more technical construction which might be available to deny exemption. In *Jones v. Meehan*, 175 US 1, it was held that "Indian treaties must be construed, not according to the technical meaning of their words, but in the sense in which they would naturally be understood by the Indians".

26 There is little in the cases to assist in the construction of section 87 of the *Indian Act*. In *R* v *The National Indian Brotherhood*, [1978] C.T.C. 680, 78 D.T.C. 6488, the question was as to *situs*, an issue which does not arise in the present case. The appeal related to the failure of the National Indian Brotherhood to deduct and pay over to the Receiver General for Canada the amount which the defendant was required by the *Income Tax Act* and regulations to deduct from the salaries of its Indian employees. The salaries in question were paid to the employees in Ottawa by cheque drawn on an Ottawa bank. Thurlow, ACJ said:

> I have already indicated that it is my view that the exemption provided for by subsection 87 does not extend beyond the ordinary meaning of the words and expressions used in it. There is no legal basis, notwithstanding the history of the exemption, and the special position of Indians in Canadian society, for extending it by reference to any notional extension of reserves or of what may be considered as being done on reserves. The issue, as I see it, assuming that the taxation imposed by the *Income Tax Act* is taxation of individuals in respect of property and that a salary or a right to salary is property, is whether the salary which the individual Indian received or to which he was entitled was "personal property" of the Indian "situated on a reserve". (at p 6491)

27 The other case is *Greyeyes* v *The Queen*, [1978] C.T.C. 91, 78 D.T.C. 6043. The question was whether an education scholarship paid by the federal government to a status Indian was taxable in the Indian's hands. Mahoney, J held that it was not taxable, by reason of section 87 of the *Indian Act*.

28 Administrative policy and interpretation are not determinative but are entitled to weight and can be an "important factor" in case of doubt about the meaning of legislation: *per* de Grandpré, J *Harel* v *The Deputy Minister of*

*Revenue of the Province of Quebec*, [1978] 1 S.C.R. 851 at 859. During argument in the present appeal the attention of the Court was directed to Revenue Canada Interpretation Bulletin IT-62 dated August 18, 1972, entitled: "Indians". Paragraph 1 of the Bulletin reads:

> This bulletin does not represent a change in either law or assessing policy as it applies to the taxation of Indians but is intended as a statement of the Department's interpretation and policies that have been established for several years.

Paragraph 5 reads:

> While the exemption in the *Indian Act* refers to "property" and the tax imposed under the *Income Tax Act* is a tax calculated on the income of a person rather than a tax in respect of his property, it is considered that the intention of the *Indian Act* is not to tax Indians on income earned on a reserve. Income earned by an Indian off a reserve, however, does not come within this exemption, and is therefore subject to tax under the *Income Tax Act*.

Counsel for the Crown said the Bulletin was simply "wrong".

29 The prime task of the Court in this case is to construe the words "no Indian ... is subject to taxation in respect of any such [personal] property". Is taxable income personal property? The Supreme Court of Illinois in the case of *Bachrach v. Nelson* (1932), 182 NE 909 considered whether "income" is "property" and responded:

> The overwhelming weight of judicial authority holds that it is. The cases of *Eliasberg Bros Mercantile Co v. Grimes*, 204 Ala 492, 86 So 56, 11 ALR 300, *Tax Commissioner v. Putnam*, 227 Mass 522, 116 NE 904, LRA 1917F, 806, *Stratton's Independence v. Howbert*, 231 US 399, 34 S Ct 136, 58 L Ed 285, *Doyle v. Mitchell Bros Co*, 247 US 179, 38 S Ct 467, 62 L Ed 1054, *Board of Revenue v. Montgomery Gaslight Co*, 64 Ala 269, *Greene v. Knox*, 175 NY 432, 67, NE 910, *Hibbard v. State*, 65 Ohio St 574, 64 NE 109, 58 LRA 654, *Ludlow-Saylor Wire Co v. Wollbrinck*, 275 Mo 339, 205 SW 196, and *State v. Pinder*, 7 Boyce (30 Del) 416, 108 A 43, define what is personal property and in substance hold that money or any other thing of value acquired as gain or profit from capital or labor is property, and that, in the aggregate, these acquisitions constitute income, and, in accordance with the axiom that the whole includes all of its parts, income includes property and nothing but property, and therefore is itself property (at p 914).

I would adopt this language. A tax on income is in reality a tax on property itself. If income can be said to be property I cannot think that taxable income is any less so. Taxable income is by definition, subsection 2(2) of the *Income Tax Act*, "his income for the year minus the deductions permitted by Division C". Although the Crown in paragraph 14 of its factum recognizes that "salaries" and "wages" can be classified as "personal property" it submits that the basis of taxation is a person's "taxable" income and that such taxable income is not "personal property" but rather a "concept", that results from a number of operations. This is too fine a distinction for my liking. If wages are personal property it seems to me difficult to say that a person taxed "in respect of" wages is not being taxed in respect of personal property. It is true that certain calculations are needed in order to determine the quantum of tax but I do not think this in any way invalidates the basic proposition.

30 The words "in respect of" are, in my opinion, words of the widest possible scope. They import such means as "in relation to", "with reference to" or "in connection with". The phrase "in respect of" is probably the widest of any expression intended to convey some connection between two related subject matters.

31 Crown counsel submits that the effect of section 87 of the *Indian Act* is to exempt what can properly be classified as "direct taxation on property" and the judgment of Jackett, CJ in *MNR* v *Iroquois of Caughnawaga (Caughnawaga Indian Band)*, [1977] 2 F.C. 269, [1977] C.T.C. 49, 77 D.T.C. 5127, is cited. The question in that case was whether the employer's share of unemployment insurance premiums was payable in respect of persons employed

by an Indian band at a hospital operated by the band on a reserve. It was argued that the premiums were "taxation" on "property" within section 87 of the *Indian Act*. Chief Justice Jackett held that even if the imposition by statute on an employer of liability to contribute to the cost of a scheme of unemployment insurance were "taxation" it would not, in the view of the Chief Justice, be taxation on "property" within the ambit of section 87. The Chief Justice continued:

> From one point of view, all taxation is directly or indirectly taxation on property; from another point of view, all taxation is directly or indirectly taxation on persons. It is my view, however, that when section 87 exempts "personal property of an Indian or band situated on a reserve" from "taxation", its effect is to exempt what can properly be classified as direct taxation on property. The courts have had to develop jurisprudence as to when taxation is taxation on property and when it is taxation on persons for the purposes of section 92(2) of *The British North America Act, 1867*, and there would seem to be no reason why such jurisprudence should not be applied to the interpretation of section 87 of the *Indian Act*. See, for example, with reference to section 92(2), *Provincial Treasurer of Alberta v. Kerr*, [1933] A.C. 710 (at p 271).

32 There is a line of cases which hold that taxes imposed pursuant to various income tax Acts are taxes "on a person" and not taxes on property: *McLeod* v *Minister of Customs and Excise*, [1926] S.C.R. 457; *Kerr* v *Superintendent of Income Tax and Attorney General of Alberta*, [1942] S.C.R. 435; *F Sura* v *Minister of National Revenue*, [1962] S.C.R. 65, [1962] C.T.C. 1, 62 D.T.C. 1005. More recently, in *Alworth* v *Minister of Finance*, [1977] 76 D.L.R. (3d) 99 and in *Attorney General of British Columbia and The Canada Trust Company and Olga Ellett*, [1980] 2 S.C.R. 466, [1980] C.T.C. 338, this Court again had occasion to consider the distinction in the case law between a tax on persons and a tax on property or upon income.

33 In the *McLeod* case the question was whether a fund accumulating in the hands of a trustee under the deceased's will was income accumulating in trust for the benefit of unascertained persons, or persons with contingent interests, within the meaning of subsection 3(6) of the *Income War Tax Act, 1917*. In the *Kerr, Alworth* and *Ellett* cases the issue was one of constitutional law. The *Sura* decision turned on the position under the *Income Tax Act* of persons domiciled in Quebec who did not enter into a pre-nuptial contract stipulating separation as to property and were therefore, under the provisions of the *Civil Code*, married under the regime of the community of property.

34 With all respect for those of a contrary view, I cannot see any compelling reason why the jurisprudence developed for the purpose of resolving constitutional disputes or for determining the tax implications of Quebec's communal property laws, or for interpreting the phrase "unascertained persons or persons with contingent interests" in the *Income War Tax Act* should be applied to limit the otherwise broad sweep of the language of section 87 of the *Indian Act*.

35 With respect, I do not agree with Chief Justice Jackett that the effect of section 87 of the *Indian Act* is only to exempt what can properly be classified as direct taxation on property. Section 87 provides that "the personal property of an Indian ... on a reserve" is exempt from taxation; but it also provides that "no Indian ... is ... subject to taxation in respect of any such property". The earlier words certainly exempt certain property from taxation; but the latter words also exempt certain persons from taxation in respect of such property. As I read it, section 87 creates an exemption for both persons and property. It does not matter then that the taxation of employment income may be characterized as a tax on persons, as opposed to a tax on property.

36 We must, I think, in these cases, have regard to substance and the plain and ordinary meaning of the language used, rather than to forensic dialectics. I do not think we should give any refined construction to the section. A person exempt from taxation in respect of any of his personal property would have difficulty in understanding why he should pay tax in respect of his wages. And I do not think it is a sufficient answer to say that the conceptualization of the *Income Tax Act* renders it so.

37 I conclude by saying that nothing in these reasons should be taken as implying that no Indian shall ever pay tax

of any kind. Counsel for the appellant and counsel for the intervenants do not take that position. Nor do I. We are concerned here with personal property situated on a reserve and only with property situated on a reserve.

38 I would allow the appeal, set aside the judgment of the Federal Court of Appeal and reinstate the judgment in the Trial Division of that Court. Pursuant to the arrangement of the parties the appellant is entitled to his costs in all courts to be taxed as between solicitor and client. There should be no costs payable by or to the intervenors.

END OF DOCUMENT

# Tab 16

*Indexed as:*

# Markevich v. Canada

**Her Majesty The Queen, appellant;**
**v.**
**Joe Markevich, respondent, and**
**Teck Cominco Metals Ltd., intervener.**

[2003] 1 S.C.R. 94

[2003] S.C.J. No. 8

2003 SCC 9

File No.: 28717.

Supreme Court of Canada

Heard: December 4, 2002;
Judgment: March 6, 2003.

**Present: McLachlin C.J. and Gonthier, Iacobucci, Major, Bastarache, Binnie, Arbour, LeBel and Deschamps JJ.**

(56 paras.)

**Appeal From:**

ON APPEAL FROM THE FEDERAL COURT OF APPEAL

**Catchwords:**

*Income tax -- Collection -- Limitation of actions -- Taxpayer failing to pay federal and provincial taxes for 1980 to 1985 taxation years as assessed by Revenue Canada in 1986 -- Revenue Canada taking no collection action until 1998 -- Whether federal and provincial limitation periods bar Revenue Canada from collecting taxpayer's federal and provincial tax debts -- Crown Liability and Proceedings Act, R.S.C. 1985, c. C-50, s. 32 -- Limitation Act, R.S.B.C. 1996, c. 266, ss. 1, 3(5).*

*Crown -- Liability -- Prescription and limitation -- Collection of federal tax debt -- Whether term "proceedings" in federal limitation provision encompasses collection procedures available under Income Tax Act -- Whether cause of action arose "otherwise than in a province" -- Whether Income*

*Tax Act complete code excluding application of federal limitation period to collection procedures -- Crown Liability and Proceedings Act, R.S.C. 1985, c. C-50, s. 32.*

*Limitation of actions -- Collection of provincial tax debt -- Definition of action -- Whether phrase "self help [page95] remedy" in definition of "action" in provincial limitation legislation encompasses collection procedures available under provincial Income Tax Act -- Limitation Act, R.S.B.C. 1996, c. 266, ss. 1, 3(5).*

**Summary:**

In 1986, t he respondent, a resident of British Columbia, received a Notice of Assessment from the Minister of National Revenue that indicated a federal and provincial tax liability of $234,136 arising from a series of assessments and unpaid taxes in respect of his 1980 to 1985 taxation years. The respondent did not challenge this assessment, and paid nothing on the outstanding amount. From 1987 to 1998, Revenue Canada made no effort to collect the debt, and statements issued to the respondent during that period did not reflect the 1986 balance. In 1998, Revenue Canada sent a statement of account to the respondent that indicated a balance of $770,583, which included the amount owing as of 1986 and accrued interest. The respondent applied to the Federal Court, Trial Division, for judicial review of the 1998 claim, and sought a declaration that the Crown was prohibited from taking any steps to collect his tax debts for 1990 and prior years. The motions judge dismissed the application. The Federal Court of Appeal set aside that decision and held that the Crown was, pursuant to s. 32 of the *Crown Liability and Proceedings Act* ("*CLPA*") and s. 3(5) of the B.C. *Limitation Act*, statute-barred from collecting the respondent's federal and provincial tax debt.

*Held*: The appeal should be dismissed.

*Per* McLachlin C.J. and Iacobucci, Major, Bastarache, Binnie, Arbour and LeBel JJ.: The six-year limitation period prescribed by s. 32 of the *CLPA* bars the Crown from collecting the respondent's federal tax debt. First, as a law of general application, s. 32 presumptively applies on a residual basis to all Crown proceedings. The breadth of the provision's application can be narrowed only by an Act of Parliament that has "otherwise provided", either expressly or impliedly, for limitation periods. The *Income Tax Act* ("*ITA*") does not provide for limitation periods within its collection provisions, and the legislative silence with regard to prescription in these provisions, interpreted in conjunction with the express language used in the *ITA*'s assessment provisions, supports the finding that Parliament intended that limitation provisions of general application apply to the Minister's collection of tax debts. A purposive interpretation of the *ITA* confirms this conclusion. Furthermore, the [page96] certainty, evidentiary and diligence rationales for limitation periods do not offend the principles of horizontal and vertical equity that should in part govern the *ITA* and are directly applicable to the collection of tax debts. Second, the ordinary meaning of the phrase "proceedings...in respect of a cause of action" in s. 32 encompasses the statutory collection procedures of the Minister. It would be incongruous to find that s. 32 was intended to apply to the court action but not to the statutory collection procedures that serve the identical purpose. The rationales that support the application of limitation provisions to Crown proceedings apply equally to both the court and non-court proceedings at issue here. To exclude s. 32's application to proceedings that are equivalent in purpose and effect to a court action would frustrate the object and aim of the provision. The legislative history of s. 32 also supports the inference that Parliament intended its application to extend beyond proceedings in court. Third, on both a plain and purposive reading of s. 32, the cause of action in this case arose "otherwise than in a province". Tax debts created under the *ITA* arise pur-

suant to federal legislation and create rights and duties between the federal Crown and residents of Canada or those who have earned income within Canada. The debt may arise from income earned in a combination of provinces or in a foreign jurisdiction. The debt is owed to the federal Crown, which is not located in any particular province and does not assume a provincial locale in its assessment of taxes.

The Minister, in its role as agent of the province of British Columbia, is also barred by s. 3(5) of the B.C. *Limitation Act* from collecting the respondent's provincial tax debt arising under the British Columbia *Income Tax Act* ("B.C. *ITA*"). Section 3(5) applies a limitation period of six years to actions for which prescription is not "specifically provided for" in another Act. Under s. 1 of the B.C. *Limitation Act*, an action is defined as including "any proceeding in a court and any exercise of a self help remedy". The term "self help remedy" encompasses the statutory collection procedures available under the B.C. *ITA*. A statutory collection procedure is a self help mechanism by which the Minister is able to effect a result that could otherwise be achieved only through an action in court. As well, the B.C. *ITA* does not specifically provide for limitation periods in its collection provisions. Since [page97] the province's collection rights are subject to expiry six years after the underlying cause of action arose, so too are the collection rights of the federal Crown as its agent.

*Per* Gonthier and Deschamps JJ.: The conclusion that the cause of action arises "otherwise than in a province" is inappropriate in two ways. First, it emphasizes the residence of the creditor instead of relying on the connecting factors of the cause of action. Second, it means that the federal government is not located anywhere in Canada. Common sense dictates that the federal Crown is located in every province. Since the federal government is, by virtue of its agreement with all of the provinces (except Quebec), responsible for collecting all provincial income taxes, it is sensible to bind its federal tax claim to the limits available on the provincial one. Efficiency is thus preserved by invoking one limitation for both the federal and provincial income tax debts arising in each province other than Quebec. Here, all of the connecting factors point to British Columbia. Consequently, the British Columbia six-year limitation period should apply.

**Cases Cited**

By Major J.

Referred to: Will-Kare Paving & Contracting Ltd. v. Canada, [2000] 1 S.C.R. 915, 2000 SCC 36; 65302 British Columbia Ltd. v. Canada, [1999] 3 S.C.R. 804; Stubart Investments Ltd. v. The Queen, [1984] 1 S.C.R. 536; Friesen v. Canada, [1995] 3 S.C.R. 103; M. (K.) v. M. (H.), [1992] 3 S.C.R. 6; Symes v. Canada, [1993] 4 S.C.R. 695; Ross v. Canada, [2002] 2 C.T.C. 222, 2002 FCT 401; MacKinnon v. Canada, [2002] 4 C.T.C. 48, 2002 FCT 824; Royce v. MacDonald (Municipality) (1909), 12 W.L.R. 347; Nowegijick v. The Queen, [1983] 1 S.C.R. 29; Letang v. Cooper, [1964] 2 All E.R. 929; Domco Industries Ltd. v. Mannington Mills, Inc. (1990), 29 C.P.R. (3d) 481; Berardinelli v. Ontario Housing Corp., [1979] 1 S.C.R. 275; E. H. Price Ltd. v. The Queen, [1983] 2 F.C. 841.

By Deschamps J.

Referred to: Williams v. Canada, [1992] 1 S.C.R. 877.

[page98]

**Statutes and Regulations Cited**

Crown Liability and Proceedings Act, R.S.C. 1985, c. C-50, s. 32 [rep. & sub. 1990, c. 8, s. 31].

Federal Court Act, R.S.C. 1970, c. 10 (2nd Supp.), s. 38(2).

Federal Court Act, R.S.C. 1985, c. F-7, s. 39(3) [rep. 1990, c. 8, s. 10].

Income Tax Act, R.S.B.C. 1996, c. 215, ss. 1(7), 49, 69.

Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.), ss. 152(4), 152(4.2), 159(3), 160(2), 160.1(3), 160.2(3), 160.3(2), 160.4(3), 222, 223(2), (3), (5) to (8), 224(1), 225(1), 225.1(1) to 225.1(4), 227(10.1).

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**History and Disposition:**

APPEAL from a judgment of the Federal Court of Appeal, [2001] 3 F.C. 449, 199 D.L.R. (4th) 255, 270 N.R. 275, 2001 D.T.C. 5305, [2001] 3 C.T.C. 39, [2001] F.C.J. No. 696 (QL), 2001 FCA 144, [page99] reversing a judgment of the Trial Division, [1999] 3 F.C. 28, 163 F.T.R. 209, 172 D.L.R. (4th) 164, 99 D.T.C. 5136, [1999] 2 C.T.C. 104, [1999] F.C.J. No. 250 (QL). Appeal dismissed.

**Counsel:**

Graham R. Garton, Q.C., and Carl Januszczak, for the appellant.

Ian Worland, for the respondent.

Edwin G. Kroft, and Geoffrey T. Loomer, for the intervener.

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The judgment of McLachlin C.J. and Iacobucci, Major, Bastarache, Binnie, Arbour and LeBel JJ. was delivered by

1 **MAJOR J.**:-- The issue in this appeal is narrow and easily stated: that is, whether federal and provincial limitation periods when exceeded apply to the Crown's ability to exercise its statutory powers to collect tax debts. I have concluded that the limitation period prescribed by s. 32 of the *Crown Liability and Proceedings Act*, R.S.C. 1985, c. C-50 ("*CLPA*"), bars the Crown from collecting the respondent's federal tax debt, and that s. 3(5) of the British Columbia *Limitation Act*, R.S.B.C. 1996, c. 266 ("B.C. *Limitation Act*") bars the Crown from collecting the respondent's provincial tax debt.

## I. Factual Background

2 The respondent was a resident of British Columbia at all times relevant to this appeal. He received a Notice of Assessment from the Minister of National Revenue (the "Minister") dated June 17, 1986, that indicated a federal and provincial tax liability of $234,136.04 arising from a series of assessments and unpaid taxes in respect of his 1980 to 1985 taxation years. The respondent did not challenge this assessment, and paid nothing on the outstanding amount after 1986. In 1987, while of no consequence to this appeal, the indebtedness was internally written off by Revenue Canada, but was not extinguished or forgiven. From 1987 to 1998, Revenue Canada made no effort to collect the debt, and statements issued to the respondent during that [page100] period did not reflect the 1986 balance. However, on January 15, 1998, approximately 12 years after the Notice of Assessment, Revenue Canada, for the first time during this period, sent a statement of account to the respondent that indicated a balance of $770,583.42, which included the amount owing as of June 17, 1986, and accrued interest.

3 The respondent applied to the Trial Division of the Federal Court for judicial review of the January 15, 1998 claim, and sought a declaration that the Crown was prohibited from taking any steps to collect his tax debts for 1990 and prior years. The motions judge dismissed the application. The Federal Court of Appeal allowed the appeal from that decision, and held that the Crown was statute-barred from collecting the respondent's tax debt reflected in the 1986 Notice of Assessment. The Crown appeals from that decision.

## II. Relevant Statutory Provisions

4 The following statutory provisions are relevant:

*Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.)

**222.** All taxes, interest, penalties, costs and other amounts payable under this Act are debts due to Her Majesty and recoverable as such in the Federal Court or any other court of competent jurisdiction or in any other manner provided by this Act.

**223...** .

(2) An amount payable by a person (in this section referred to as a "debtor") that has not been paid or any part of an amount payable by the debtor that has not been paid may be certified by the Minister as an amount payable by the debtor.

(3) On production to the Federal Court, a certificate made under subsection (2) in respect of a debtor shall be registered in the Court and when so registered has the same effect, and all proceedings may be taken thereon, as if the certificate were a judgment obtained in the Court against the debtor for a debt in the amount certified plus [page101] interest thereon to the day of payment as provided by the statute or statutes referred to in subsection (1) under which the amount is payable and, for the purpose of any such proceedings, the certificate shall be deemed to be a judgment of the Court against the debtor for a debt due to Her Majesty, enforceable in the amount certified plus interest thereon to the day of payment as provided by that statute or statutes.

**224.** (1) Where the Minister has knowledge or suspects that a person is, or will be within one year, liable to make a payment to another person who is liable to make a payment under this Act (in this subsection and subsections (1.1) and (3) referred to as the "tax debtor"), the Minister may in writing require the person to pay forthwith, where the moneys are immediately payable, and in any other case as and when the moneys become payable, the moneys otherwise payable to the tax debtor in whole or in part to the Receiver General on account of the tax debtor's liability under this Act.

**225.** (1) Where a person has failed to pay an amount as required by this Act, the Minister may give 30 days notice to the person by registered mail addressed to the person's latest known address of the Minister's intention to direct that the person's goods and chattels be seized and sold, and, if the person fails to make the payment before the expiration of the 30 days, the Minister may issue a certificate of the failure and direct that the person's goods and chattels be seized.

**225.1** (1) Where a taxpayer is liable for the payment of an amount assessed under this Act, other than an amount assessed under subsection 152(4.2), 169(3) or 220(3.1), the Minister shall not, for the purpose of collecting the amount, [take any collection action] until after the day that is 90 days after the day of the mailing of the notice of assessment.

*Crown Liability and Proceedings Act*, R.S.C. 1985, c. C-50

**32.** Except as otherwise provided in this Act or in any other Act of Parliament, the laws relating to prescription and the limitation of actions in force in a province between subject and subject apply to any proceedings by or against the Crown in respect of any cause of action arising in that province, and proceedings by or against the Crown in respect of a cause of action arising otherwise than in a province shall be taken within six years after the cause of action arose.

[page102]

British Columbia *Limitation Act*, R.S.B.C. 1996, c. 266

**1** ...

**"action"** includes any proceeding in a court and any exercise of a self help remedy;

**3** ...

(5) Any other action not specifically provided for in this Act or any other Act may not be brought after the expiration of 6 years after the date on which the right to do so arose.

**9** (1) On the expiration of a limitation period set by this Act for a cause of action to recover any debt, damages or other money, or for an accounting in respect of any matter, the right and title of the person formerly having the cause of action and of a person claiming through the person in respect of that matter is, as against the person against whom the cause of action formerly lay and as against the person's successors, extinguished.

...

(3) A cause of action, whenever arising, to recover costs on a judgment or to recover arrears of interest on principal money is extinguished by the expiration of the limitation period set by this Act for an action between the same parties on the judgment or to recover the principal money.

III. Judicial History

**5** At the Federal Court, Trial Division ( [1999] 3 F.C. 28), the motions judge held that s. 32 of the *CLPA* does not apply to the statutory collection procedures authorized by the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) ("*ITA*"). He found both that the collection procedures do not qualify under s. 32 as proceedings in respect of a cause of action, and that the *ITA* is a complete code in itself that excludes the application of s. 32 . The motions judge also held that the B.C. *Limitation Act* does not apply to the Crown's collection of the provincial tax debt under the British Columbia *Income Tax Act*, R.S.B.C. 1996, c. 215 ("B.C. *ITA*"). As a result, his conclusion was that neither the Crown's collection of the [page103] federal nor the provincial tax debt was subject to the limitation periods.

**6** The Federal Court of Appeal disagreed and allowed the appeal ([2001] 3 F.C. 449, 2001 FCA 144). Rothstein J.A. decided that the *ITA* is not a complete code that excludes the application of s. 32 of the *CLPA*, and that the statutory collection procedures qualify as proceedings in respect of a cause of action under s. 32 . Consequently, the limitation period prescribed by s. 32 applies to the statutory collection procedures in the *ITA*. He held that the relevant limitation provision was s. 3(5) of the B.C. *Limitation Act*. Section 3(5) includes both court proceedings and self help remedies, and so applies to both court and statutory collection procedures under the *ITA*. Owing to this provision, the Minister was barred from collecting the federal tax debt six years after the right to do so arose. Rothstein J.A. also concluded that s. 3(5) bars the Crown, in its role as collection agent for British Columbia under the B.C. *ITA*, from pursuing the taxpayer's provincial debt.

IV. Issues

**7** The appeal raises the following issues:

1. (a) Are statutory collection proceedings under the *ITA* subject to a limitation period pursuant to s. 32 of the *CLPA*? This requires the determination of:

   (i) Does the *ITA* provide for limitation periods for the collection of tax debts, or otherwise exclude the operation of s. 32 of the *CLPA*?

   (ii) Is the exercise of a statutory collection power a "proceeding ... in respect of any cause of action" under s. 32?

[page104]

   (b) If s. 32 is found to apply to the statutory collection proceedings, does the cause of action arise in a province or otherwise than in a province?

2. Does the B.C. *Limitation Act* apply to statutory collection proceedings undertaken by the Crown acting as collection agent for the Province of British Columbia pursuant to the B.C. *ITA*?

V. Analysis

A. *The Federal Tax Debt*

(1) Is the Federal Tax Debt Subject to Section 32 of the *CLPA*?

**8** Prior to an analysis of the problem, it is useful to describe the broad collection powers available under the *ITA*. The Minister is authorized to collect tax debts by means of either a court action or statutory collection procedures. Section 222 of the *ITA* provides:

> All taxes, interest, penalties, costs and other amounts payable under this Act are debts due to Her Majesty and recoverable as such in the Federal Court or any other court of competent jurisdiction or in any other manner provided by this Act.

The various collection mechanisms enumerated in the *ITA* provide the Minister with an extensive range of remedies to recover debts. The Minister may certify an unpaid tax amount (s. 223(2)) and register the certificate in the Federal Court (s. 223(3)), at which point the certificate is deemed to be a judgment of that court. The Federal Court can then issue a certificate, notification, or writ evidencing the s. 223(2) certificate, which can be used by the Minister to create a charge, lien, priority, or other interest on property in any province (ss. 223(5) to 223(8)). Under the garnishment provision of s. 224(1), the Minister may require a third party who is indebted to the taxpayer to make payments directly to the Minister. The Minister may also order the seizure and sale of the taxpayer's goods and chattels under s. 225(1). These collection powers cannot be exercised until 90 days after the later of the mailing of a notice of assessment or the mailing of a confirmation [page105] or variation of the assessment, or until the taxpayer's appeal has been finally determined by the Tax Court of Canada (ss. 225.1(1) to 225.1(4)).

**9** The outcome of this appeal narrows to whether the exercise of these collection powers is subject to prescription under s. 32 of the *CLPA*. Section 32 applies limitation periods to proceedings brought by or against the Crown in all cases unless Parliament has otherwise provided. The section states:

> Except as otherwise provided in this Act or in any other Act of Parliament, the laws relating to prescription and the limitation of actions in force in a province between subject and subject apply to any proceedings by or against the Crown in respect of any cause of action arising in that province, and proceedings by or against the Crown in respect of a cause of action arising otherwise than in a province shall be taken within six years after the cause of action arose. [Emphasis added.]

The section applies to the statutory collection procedures if two criteria are met. First, the *ITA* must not otherwise provide for limitation periods with respect to the collection of tax debts. Second, the statutory collection procedures must qualify under s. 32 as "proceedings ... in respect of a cause of action".

**10** I agree with the reasons of the Federal Court of Appeal that each of the two criteria is met in this case, and that s. 32 must apply to the Crown's exercise of statutory collection powers.

(a) *Does the ITA Otherwise Provide for Prescription?*

**11** As a law of general application, s. 32 of the *CLPA* presumptively applies on a residual basis to all Crown proceedings. The breadth of the provision's application can be narrowed only by an Act of Parliament that has "otherwise provided", either expressly or impliedly, for limitation periods. It is evident that the *ITA* does not provide for limitation periods within its collection provisions.

[page106]

**12** The noted author E. A. Driedger in *Construction of Statutes* (2nd ed. 1983), at p. 87, stated that the modern approach to statutory interpretation requires the words of an Act "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". These principles have frequently been adopted by this Court both generally and in the construction of taxation legislation: see *Will-Kare Paving & Contracting Ltd. v. Canada*, [2000] 1 S.C.R. 915, 2000 SCC 36, at para. 32; *65302 British Columbia Ltd. v. Canada*, [1999] 3 S.C.R. 804, both in the majority and minority concurring reasons , and *Stubart Investments Ltd. v. The Queen*, [1984] 1 S.C.R. 536, at p. 578.

**13** The assessment provisions of the *ITA* are clearly stated on prescription. By contrast, the collection provisions of the *ITA* are silent with respect to prescription. There is no reference in s. 222 or its accompanying provisions to either the absence or presence of a limitation period. Nonetheless, the appellant submits that the *ITA* has "otherwise provided" for prescription. In the appellant's submission, the *ITA* constitutes a complete statutory scheme for the collection of taxes, and so silence in the legislation indicates Parliament's intent to avoid fettering the Crown's collection powers with limitation periods.

**14** There is no authority to support the proposition that the *ITA* is a complete code that cannot be informed by laws of general application. The *ITA* does not operate in a legislative vacuum: see *Will-Kare, supra*, at para. 31. See also P. W. Hogg, J. E. Magee and T. Cook, *Principles of Canadian Income Tax Law* (3rd ed. 1999), at p. 2, where the authors note that the "Income Tax Act relies implicitly on the general law". Accordingly , whether a statute or legal principle affects the operation of the *ITA* must be decided by an analysis of the specific provisions involved.

**15** Absent legislation or judicial support, the appellant nonetheless requests the Court to interpret s. 222 of the *ITA* as if it permits the collection of tax debts "at any time". It is "a basic principle of [page107] statutory interpretation that the court should not accept an interpretation which requires the insertion of extra wording where there is another acceptable interpretation which does not require any additional wording": see *Friesen v. Canada*, [1995] 3 S.C.R. 103, at para. 27. This principle weighs against accepting the appellant's interpretation. The provision does not include the words "at any time", and is capable of a reasonable construction without that insertion. The legislative silence with regard to prescription gives rise to the logical inference that Parliament intended for limitation provisions of general application to apply to the Minister's collection powers.

**16** This conclusion is supported by the explicit manner in which the *ITA* addresses limitation periods in its assessment provisions. The Court held in *Friesen, supra*, at para. 27, that "[r]eading extra words into a statutory definition is even less acceptable when the phrases which must be read in appear in several other definitions in the same statute". Numerous provisions in the *ITA* expressly stipulate that the Minister may make an assessment "at any time": see ss. 152(4), 152(4.2), 159(3),

160(2), 160.1(3), 160.2(3), 160.3(2), 160.4(3), and 227(10.1). Parliament has demonstrated a clear willingness to address the issue of limitation periods in the *ITA* where it sees fit to do so. As Rothstein J.A. noted at para. 22, "Parliament has put its mind to the limitation question in the *Income Tax Act* and when it intends there to be no limitation period, it has so stated." Accordingly, the unescapable conclusion is that the plain language used in the collection provisions does not support the inference that Parliament intended to exclude the application of limitation provisions to the Minister's collection powers.

**17** In finding that the collection provisions implicitly exclude s. 32, the learned motions judge appeared to rely predominantly on s. 225.1 of the *ITA*, which prevents the Minister from initiating collection procedures pending objection or appeal of an assessment by the taxpayer. With respect, I do not agree that s. 225.1 lends any weight to the appellant's [page108] argument. The statutory stay prescribed by s. 225.1 is directed towards protecting the taxpayer from collection action pending a final determination of the validity of his or her assessment. Limitation periods, on the other hand, are meant to promote certainty, avoid stale evidence, encourage diligence, and bring repose: see *M. (K.) v. M. (H.)*, [1992] 3 S.C.R. 6, at p. 29, *per* La Forest J. The rationales outlined above for stays and limitation provisions are entirely distinct. I agree with Rothstein J.A.'s conclusion at para. 21:

> The enactment of a statutory stay which specifies when collection action may commence, cannot logically support the inference that Parliament considered that no limitation period should apply to that collection action.

**18** A purposive analysis of the *ITA* confirms that the collection provisions do not by implication exclude the operation of s. 32. The application of limitation periods to the collection of tax debts does not offend the principles of horizontal and vertical equity that, as Iacobucci J. noted in *Symes v. Canada*, [1993] 4 S.C.R. 695, at p. 738, should in part govern the *ITA*. The appellant submits that applying laws of prescription to tax collection would unfairly alleviate the tax burden of individuals who experience fluctuations in income at the expense of those who enjoy a steady stream of income. This apparent problem can be averted, however, by the Minister's reasonably diligent exercise of debt collection. If a taxpayer does not have the ability to satisfy a tax debt prior to the expiration of the limitation period, the Minister can choose from a variety of means to extend the limitation period. In *Ross v. Canada*, [2002] 2 C.T.C. 222, 2002 FCT 401, the Federal Court, Trial Division, held that the registration of a certificate with the Federal Court in accordance with s. 223(3) of the *ITA* gives rise to a renewal of the limitation period. See also *MacKinnon v. Canada*, [2002] 4 C.T.C. 48, 2002 FCT 824, where the court found that the taxpayer's acknowledgement of indebtedness by way of a hypothecation agreement with the Minister, and his partial payment of the tax debt, each served to renew the limitation period. There is no need to exhaustively set out the ways in which [page109] the Minister can extend the limitation period, other than to note that there are numerous avenues open to the Minister by which renewals may be effected. There is no credible basis to support the submission that the laws of prescription will undermine the equitable collection of taxes when minimum diligence would have the opposite effect.

**19** The appellant's submission that the rationales for limitation periods militate against their application to tax collection cannot be correct. As noted above, limitation provisions are based upon what have been described as the certainty, evidentiary, and diligence rationales: see *M. (K.), supra*, at p. 29 . The certainty rationale recognizes that, with the passage of time, an individual "should be secure in his reasonable expectation that he will not be held to account for ancient obligations": *M. (K.), supra*, at p. 29. The evidentiary rationale recognizes the desire to preclude claims where the

evidence used to support that claim has grown stale. The diligence rationale encourages claimants "to act diligently and not 'sleep on their rights'": *M. (K.), supra*, at p. 30.

**20** Each of the rationales submitted as applicable to there being no limitation periods affecting collection are in fact just the opposite and are directly applicable to the Minister's collection of tax debts. If the Minister makes no effort to collect a tax debt for an extended period, at a certain point a taxpayer may reasonably come to expect that he or she will not be called to account for the liability, and may conduct his or her affairs in reliance on that expectation. As well, a limitation period encourages the Minister to act diligently in pursuing the collection of tax debts. In light of the significant effect that collection of tax debts has upon the financial security of Canadian citizens, it is contrary to the public interest for the department to sleep on its rights in enforcing collection. It is evident that the rationales which [page110] justify the existence of limitation periods apply to the collection of tax debts.

**21** The legislative silence with regard to prescription in these provisions, interpreted in conjunction with the express language used in the *ITA*'s assessment provisions, supports the finding that Parliament intended that limitation provisions of general application apply to the Minister's collection of tax debts. A purposive interpretation of the statute confirms this conclusion. There was no evidence before the Court to lend any support to the submission that laws of prescription would frustrate the equitable collection of taxes. Finally, the rationales for limitation periods for the reasons given apply directly to the collection of tax debts.

**22** As a result, whether s. 32 of the *CLPA* applies to the Minister's statutory collection procedures depends entirely upon whether such procedures qualify under s. 32 as "proceedings ... in respect of a cause of action".

(b) *Do the Statutory Collection Procedures Qualify as "Proceedings ... in Respect of a Cause of Action"?*

**23** The application of s. 32 is limited to "proceedings by or against the Crown in respect of a cause of action".

**24** Interpreted in their grammatical and ordinary sense, these words clearly encompass the statutory collection procedures in the *ITA*. Although the word "proceeding" is often used in the context of an action in court, its definition is more expansive. The Manitoba Court of Appeal stated in *Royce v. MacDonald (Municipality)* (1909), 12 W.L.R. 347, at p. 350, that the "word 'proceeding' has a very wide meaning, and includes steps or measures which are not in any way connected with actions or suits". In *Black's Law Dictionary* (6th ed. 1990), at [page111] p. 1204, the definition of "proceeding" includes, *inter alia*, "an act necessary to be done in order to obtain a given end; a prescribed mode of action for carrying into effect a legal right".

**25** The statutory collection procedures closely resemble various proceedings in court. The registration of a certificate in Federal Court is deemed by s. 223(3) to be a judgment of that court. As Rothstein J.A. notes at para. 35:

> A requirement to pay under section 224 (as am. by S.C. 1994, c. 21, s. 101) is analogous to a garnishing order issued by a court... . Seizure and sale of chattels under subsection 225(1) is a provision closely parallel to a writ of execution issued by a court.

By granting the power to effect the collection of tax debts in this manner, Parliament has provided the Minister with an efficient and expeditious alternative to bringing a court action. However, the court and non-court collection procedures are identical in purpose. Both are mechanisms by which the Minister is able to enforce the collection of tax debts and thereby carry into effect the legal rights of the Crown. It is evident that both kinds of procedures are appropriately characterized as legal proceedings.

**26** The appellant's submission turns on whether these proceedings are undertaken "in respect of a cause of action". The words "in respect of" have been held by this Court to be words of the broadest scope that convey some link between two subject matters. See *Nowegijick v. The Queen*, [1983] 1 S.C.R. 29, at p. 39, *per* Dickson J. (as he then was):

> The words "in respect of" are, in my opinion, words of the widest possible scope. They import such meanings as "in relation to", "with reference to" or "in connection with". The phrase "in respect of" is probably the widest of any expression intended to convey some connection between two related subject matters.

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In the context of s. 32, the words "in respect of" require only that the relevant proceedings have some connection to a cause of action.

**27** A "cause of action" is only a set of facts that provides the basis for an action in court: see *Letang v. Cooper*, [1964] 2 All E.R. 929 (C.A.), at p. 934; *Domco Industries Ltd. v. Mannington Mills, Inc.* (1990), 29 C.P.R. (3d) 481 (F.C.A.), *per* Iacobucci C.J. (as he then was), at p. 496; and *Black's Law Dictionary, supra*, at p. 221. In this case, s. 222 of the *ITA* provides that unpaid taxes constitute a debt recoverable by means of a court action, subject to the stay of collection action prescribed by s. 225.1. As a result, as Rothstein J.A. notes at para. 37, the cause of action here involves "the existence of a tax debt and the expiry of the delay period entitling the Minister to take collection action".

**28** In light of the above analysis, the ordinary meaning of the phrase "proceedings ... in respect of a cause of action" encompasses the statutory collection procedures of the Minister. The exercise of the statutory proceedings is entirely dependent upon a set of facts that would support action by the Minister, i.e., the existence of a tax debt and the expiry of the delay period prescribed by s. 225.1.

**29** I now turn to the French version of s. 32, which states:

> Sauf disposition contraire de la présente loi ou de toute autre loi fédérale, les règles de droit en matière de prescription qui, dans une province, régissent les rapports entre particuliers s'appliquent lors des poursuites auxquelles l'État est partie pour tout fait générateur survenu dans la province. Lorsque ce dernier survient ailleurs que dans une province, la procédure se prescrit par six ans.

**30** The words "*poursuite*", "*procédure*" and "*instance*" are all used to render the term "proceedings" in different contexts. "*Procédure*" is even used to describe a cause of action, as demonstrated by the wording of s. 32 of the *CLPA*. This can also be verified in some French publications on the translation of English law (see for instance Bouscaren, Greenstein & Cordahi, *Les bases du droit anglais* [page113] (1981)). It is therefore difficult to consider the definition of a single expression to determine the common meaning of the English and French versions of s. 32. Indeed, the legislative history of s. 32, beginning with s. 38(2) (R.S.C. 1970, c. 10 (2nd Supp.)) and later s. 39(3) (R.S.C. 1985, c. F-7) of the *Federal Court Act* ("*FCA*"), which as discussed below were its precursors, also denotes both that context matters and that changes in terminology are not necessarily meant to bring about a change in the substantive law.

**31** If we were to confine our analysis to the word "*poursuite*", we would find that generally, in Canada, that word excludes non-court proceedings: the term is defined in H. Reid, *Dictionnaire de droit québécois et canadien* (2nd ed. 2001), in the following way, at p. 425:

> [TRANSLATION]
>
> 1. Court action brought by a person in order to assert his right or obtain a sanction against the perpetrator of an offence. E.g.: A creditor's proceedings [*poursuite*] against his debtor.

But French dictionaries, which are also used in Canada, ascribe a broader definition to "*poursuite*". G. Cornu, in *Vocabulaire juridique* (8th ed. 2000), at p. 654, writes:

> [TRANSLATION] Exercise of a remedy [*voie de droit*] to compel someone to perform his obligations or submit to the orders of the law or of the public authority.

Cornu further defines "*voie de droit*" as follows (at p. 909):

> [TRANSLATION] Means given by the law to citizens to have their rights recognized and respected or to defend their interests; generic term encompassing court action, means (jurisdictional) of redress, executions, administrative recourses; by ext., any jurisdictional proceeding even initiated by the prosecution.

General dictionaries such as *Le Petit Larousse* (2003) define "*poursuite*" as a court proceeding, but also as [TRANSLATION] "[a]n action by the tax authorities to collect treasury debts".

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**32** It would therefore be difficult to conclude definitively that "*poursuite*" is more restrictive than "proceedings" and that this is determinative in the context of s. 32. It is then necessary, in this case, to conclude that the common meaning of the English and French versions of the provision is unclear and that resort to the other rules of statutory interpretation is necessary in order to discern Parliament's intent. Applying those rules, construing s. 32 in context, harmoniously with the pur-

pose of the *CLPA*, I have concluded that it was meant to include administrative mechanisms that enable the Crown to achieve exactly the same result as it would through a formal action in court.

**33** At common law, the Crown was not bound by limitation periods unless a federal statute expressly provided otherwise. On the other hand, the Crown was entitled to the benefit of a limitations defence in proceedings brought against it: see D. Sgayias et al., *The Annotated Crown Liability and Proceedings Act 1995* (1994), at pp. 135-36, and P. W. Hogg and P. J. Monahan, *Liability of the Crown* (3rd ed. 2000), at p. 71. The purpose of s. 32 is obviously, in the search for equity, to extend the same benefit of laws of prescription to subjects defending themselves against proceedings brought by the Crown.

**34** A court action brought by the Minister to recover tax debt in this appeal would be subject to the limitation provisions in s. 32. It would be incongruous to find that s. 32 of the *CLPA* was intended to apply to the court action but not to the statutory collection procedures that serve the identical purpose. The certainty, evidentiary and diligence rationales that support the application of limitation provisions to Crown proceedings apply equally to both the court and non-court proceedings at issue here. See *Berardinelli v. Ontario Housing Corp.*, [1979] 1 S.C.R. 275, *per* Estey J., at p. 284:

> When one interpretation can be placed upon a statutory provision which would bring about a more workable and practical result, such an interpretation should be preferred if the words invoked by the Legislature can reasonably bear it ... .

[page115]

There is no reason to infer that Parliament intended for s. 32's application to turn solely upon the technicality of whether the relevant proceeding took place in court. To exclude s. 32's application to proceedings that are equivalent in purpose and effect to a court action would frustrate the object and aim of the provision.

**35** The legislative history of s. 32 of the *CLPA* supports the inference that Parliament intended for its application to extend beyond proceedings in court. Section 38 of the *FCA* was enacted in 1971 (R.S.C. 1970, c. 10 (2nd Supp.)), and later renumbered as s. 39 of R.S.C. 1985, c. F-7. Section 38(2), which was succeeded by s. 39(3), applied limitation provisions to proceedings brought by or against the Crown. Section 39 of the *FCA* stated:

> **39.** (1) Except as expressly provided by any other Act, the laws relating to prescription and the limitation of actions in force in any province between subject and subject apply to any proceedings in the Court in respect of any cause of action arising in that province.
>
> (2) A proceeding in the Court in respect of a cause of action arising otherwise than in a province shall be taken within six years after the cause of action arose.

(3) Except as expressly provided by any other Act, the laws relating to prescription and the limitation of actions referred to in subsections (1) and (2) apply to any proceedings brought by or against the Crown.

Prior to 1992, s. 32 of the *CLPA* (then entitled the *Crown Liability Act*), applied only to tort actions against the Crown. By S.C. 1990, c. 8, ss. 10, and 31, s. 39(3) of the *FCA* was repealed and s. 32 of the *CLPA* was amended to apply to all proceedings in respect of a cause of action brought both by and against the Crown.

**36** It is readily apparent, as the Federal Court of Appeal notes at para. 49, that s. 38(2) and later s. 39(3) were the predecessors to the current s. 32 of the *CLPA*. In determining the legislative intent behind the current wording in s. 32, it is useful to examine the judicial interpretation given to the provisions that came before it. In *E. H. Price Ltd. v. [page116] The Queen*, [1983] 2 F.C. 841, the Federal Court of Appeal considered whether s. 38(2) of the *FCA* applied to the Minister's registration of a certificate under the *Excise Tax Act*. In *obiter*, Clement D.J. held at pp. 847-48 that in the absence of the limiting words "in the Court" that were contained in s. 38(1), "proceedings" under s. 38(2) were not limited to court proceedings and included the Minister's registration of a certificate. In its subsequent amendment of s. 32 of the *CLPA*, Parliament did not include the words "in the court" or words of a similar limiting effect. As Rothstein J.A. found at para. 50, "it is a fair inference that Parliament, not having done so, meant to adopt the interpretation in *E. H. Price* so that 'proceedings' in section 32 include all legal processes in respect of a cause of action, whether court or otherwise". Although the words "in respect of a cause of action" were not included in s. 39(3), for the reasons I have outlined, the inclusion of these words in s. 32 does not have the effect of limiting the provision's application to proceedings in court.

**37** I conclude that the English version best reflects the intent of the legislator. As a result, it should be determined which particular limitation period provided by s. 32 applies to these proceedings. This depends upon whether the cause of action on the federal tax debt arose in a province or otherwise than in a province.

(2) Does the Cause of Action Arise in a Province, or Otherwise than in a Province?

**38** Section 32 applies provincial limitation laws to proceedings in respect of a cause of action arising in a province, and a six-year limitation period to those which arise otherwise than in a province. The motions judge, at para. 59, would have found that the cause of action arose otherwise than in a province. The Court of Appeal applied the provincial limitation provision and so, implicitly at least, [page117] found that the cause of action arose in a province. In this appeal, the matter is of no particular consequence, because in either case the limitation period runs for six years from the date upon which the cause of action arose . Nonetheless, I conclude that the appellant's cause of action arose otherwise than in a province, and hence that the six-year limitation period provided by s. 32 applies.

**39** Tax debts created under the *ITA* arise pursuant to federal legislation and create rights and duties between the federal Crown and residents of Canada or those who have earned income within Canada. The debt may arise from income earned in a combination of provinces or in a foreign jurisdiction. The debt is owed to the federal Crown, which is not located in any particular province and does not assume a provincial locale in its assessment of taxes. Consequently, on a plain reading of s. 32, the cause of action in this case arose "otherwise than in a province".

**40** A purposive reading of s. 32 supports this finding. If the cause of action were found to arise in a province, the limitation period applicable to the federal Crown's collection of tax debts could vary considerably depending upon the province in which the income was earned and its limitation periods. In addition to the administrative difficulties that potentially arise from having to determine the specific portions of tax debts that arise in different provinces, the differential application of limitation periods to Canadian taxpayers could impair the equitable collection of taxes. Disparities amongst provincial limitation periods could foreseeably lead to more stringent tax collection in some provinces and more lenient collection in others. The Court can only presume that in providing for a limitation period of six years to apply to proceedings in respect of a cause of action arising otherwise than in a province, Parliament intended for limitation provisions to apply uniformly throughout the country with [page118] regard to proceedings of the kind at issue in this appeal.

**41** I conclude that the collection proceedings under the *ITA* are subject to prescription six years after the cause of action arose. As noted above, the cause of action in this case comprised the respondent's tax debt and the expiry of the 90-day delay period after the mailing of the Notice of Assessment dated June 17, 1986. As a result, the cause of action arose on September 16, 1986. The Minister undertook no action in the six years after that date to effect a renewal of the limitation period. Consequently, as of September 16, 1992, s. 32 of the *CLPA* barred the Minister from collecting the respondent's 1986 federal tax debt. Limitation periods have traditionally been understood to bar a creditor's remedy but not his or her right to the underlying debt. In my view, this is a distinction without a difference. For all intents and purposes, the respondent's federal tax debt is extinguished.

B. *The Provincial Tax Debt*

**42** The final issue is whether the Minister, in his or her role as agent of the province of British Columbia, is barred by the B.C. *Limitation Act* from collecting tax debts arising under the B.C. *ITA*.

**43** Section 49 of the B.C. *ITA* provides that s. 222 of the *ITA* applies for the purposes of the B.C. *ITA*, subject, as *per* s. 1(7), to such modifications as the circumstances require to make it applicable to British Columbia. Accordingly, tax debts arising under the B.C. *ITA* are debts owed to the province.

**44** Section 69 of the B.C. *ITA* authorizes British Columbia's Minister of Finance and Corporate Relations to enter into a collection agreement whereby the federal government agrees to collect taxes payable under the B.C. *ITA* and remit those taxes to the provincial government. A collection agreement of this kind between British Columbia and the Government of Canada has been in place since 1962: Memorandum of Agreement, [page119] January 28, 1962. Subsection 1(1) of this agreement states as follows:

> Canada, as agent of the Province, will collect for and on behalf of the Province the income taxes imposed under the [B.C. *ITA*] ... . [Emphasis added.]

**45** As a result, the provincial government, as principal, has delegated its right to collect tax debts to the federal government, its agent. It has long been accepted that the authority, express or implied, of every agent is confined within the limits of the powers of his or her principal: see F. M. B. Reynolds, *Bowstead and Reynolds on Agency* (16th ed. 1996), at p. 110. Accordingly, in order to determine the collection rights that are delegated to the federal government, it is necessary to determine the collection rights of the province.

**46** The B.C. *Limitation Act* governs the law on limitations of actions within British Columbia. Section 14(1) of the British Columbia *Interpretation Act*, R.S.B.C. 1996, c. 238, states that unless an enactment specifically provides otherwise it is binding on the Government of British Columbia. The B.C. *Limitation Act* does not provide otherwise, and so its provisions apply to proceedings brought by and against the provincial government.

**47** Section 3(5) of the B.C. *Limitation Act* applies a limitation period of six years to actions for which prescription is not "specifically provided for" in another Act. Under s. 1 of the B.C. *Limitation Act*, an action is defined as including "any proceeding in a court and any exercise of a self help remedy". I agree with both the motions judge and the Court of Appeal that the term "self help remedy" encompasses the statutory collection procedures available under the B.C. *ITA*. A statutory collection procedure is a self help mechanism by which the Minister is able to effect a result that could otherwise be achieved only through an action in court. As well, the B.C. *ITA* does not specifically provide for limitation periods in its collection provisions.

**48** Consequently, the province's right to pursue collection proceedings under the B.C. *ITA* is subject to [page120] the limitation period set out in s. 3(5) of the B.C. *Limitation Act*. Moreover, pursuant to s. 9(1) of the B.C. *Limitation Act*, on the expiration of the limitation period, the province's right and title to the tax debt is extinguished, and pursuant to s. 9(3), the province's right and title to interest on the tax debt is extinguished.

**49** As noted above, the federal Crown's right to collect provincial taxes in this case is no greater than the right delegated to it by the province. Since the province's collection rights are subject to expiry six years after the underlying cause of action arose, so too are the collection rights of the federal Crown as its agent.

**50** The cause of action here consisted of the tax debt and the expiry of the delay period allowing collection action to be taken on September 16, 1986. The Minister undertook no action in the six years after that date to effect a renewal of the limitation period. Consequently, as of September 16, 1992, the federal Crown became statute-barred from collecting the provincial tax debt. As well, the right and title of any claimant to the respondent's provincial tax debt, and its accrued interest, were extinguished on that date.

## VI. Conclusion

**51** For the foregoing reasons, I would dismiss the appeal with costs.

The reasons of Gonthier and Deschamps JJ. were delivered by

**52** DESCHAMPS J.:-- I agree with the reasons of my colleague, Justice Major, except on one point.

**53** In determining where the cause of action arises under s. 32 of the *Crown Liability and Proceedings Act*, R.S.C. 1985, c. C-50, Major J. focusses on the location of the federal government. The conclusion that the cause of action arises "otherwise than in a province" is, in my view, inappropriate in two ways. First, it emphasizes the residence of the creditor instead of relying on the connecting factors of the cause of action and second, it means that the federal [page121] government is not located anywhere in Canada or, as the French version of s. 32 reads, the federal gov-

ernment would be located "*ailleurs que dans une province*". Common sense, rather, would dictate that the federal Crown is located in every province and not "otherwise than in a province" .

**54** The cause of action concept is more readily understood in negligence cases. Here, however, the claim has a statutory foundation. It may be characterized as a right *in personam*, i.e. the right of the Crown against the taxpayer. This Court, in *Williams v. Canada*, [1992] 1 S.C.R. 877, dealt with a similar problem in a case concerned with a tax exemption. Although the residence criterion was modified in favour of a test encompassing all connecting factors, the *situs* analysis was upheld to determine the location of the debt. This concept is also used in private international law in order to determine where enforcement of a claim can be pursued: J.-G. Castel and J. Walker, *Canadian Conflict of Laws* (5th ed. (loose-leaf)), at para. 22.2.

**55** Applying the connecting factors test used in *Williams*, the factors would be the respondent's residence, his place of employment and the place where his income was received. All of these factors point to British Columbia. The British Columbia six-year limitation period should apply.

**56** Since the federal government is, by virtue of its agreement with all of the provinces (except Quebec), responsible for collecting all provincial income taxes, it is sensible to bind its federal tax claim to the limits available on the provincial one. Efficiency is thus preserved by invoking one limitation for both the federal and provincial income tax debts arising in each province, other than Quebec.

**Solicitors:**

Solicitor for the appellant: Department of Justice, Vancouver.

[page122]

Solicitors for the respondent: Legacy Tax & Trust Lawyers, Vancouver.

Solicitors for the intervener: McCarthy Tétrault, Vancouver.

cp/e/qw/qllls

# Tab 17

*Indexed as:*

# CanadianOxy Chemicals Ltd. v. Canada (Attorney General)

**The Attorney General of Canada, appellant;**
**v.**
**CanadianOxy Chemicals Ltd., CanadianOxy Industrial Chemicals Limited Partnership and Canadian Occidental Petroleum Ltd., respondents, and**
**The Attorney General for Ontario, intervener.**

[1999] 1 S.C.R. 743

[1998] S.C.J. No. 87

File No.: 25944.

Supreme Court of Canada

Hearing and judgment: December 10, 1998.
Reasons delivered: April 23, 1999.

**Present: Lamer C.J. and L'Heureux-Dubé, Gonthier, Cory, Iacobucci, Major and Binnie JJ.**

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

*Criminal law -- Search and seizure -- Search warrants -- Criminal Code authorizing issuance of warrants to search for "evidence with respect to the commission of an offence" -- Whether provision authorizes granting of warrants to search for and seize evidence of negligence going to defence of due diligence -- Criminal Code, R.S.C., 1985, c. C-46, s. 487(1)(b).*

A plant operated by the respondents discharged a quantity of chlorine into the adjacent waters, killing a number of fish. This incident occurred during a power outage at the plant, which resulted from a power line being struck by a tree. The respondents reported the discharge to the authorities and an investigation followed. Five months after the discharge, a fishery officer swore an information and obtained a warrant to search the plant for a range of documents. He later obtained an order for a new warrant to reseize several items which had been returned and which were relevant to the investigation. The respondents were charged with offences under the Fisheries Act and the Waste Management Act. They subsequently brought a motion to quash the warrants, alleging that s. 487(1) of

the Criminal Code, which provides for the issuance of search warrants pertaining to "evidence with respect to the commission of an offence", had been exceeded. The chambers judge ruled that the documents seized pertaining to the issue of due diligence were not documents with respect to the commission of this particular offence and quashed both warrants. The Court of Appeal, in a majority decision, upheld the ruling.

Held: The appeal should be allowed.

Statutory provisions should be read to give the words their most obvious ordinary meaning which accords with the context and purpose of the enactment in which they occur. On a plain reading, the phrase "evidence with respect to the commission of an offence" is a broad statement, encompassing all materials which might shed light on the circumstances of an event which appears to constitute an offence. Anything relevant or rationally connected to the incident under investigation, the parties involved, and their potential culpability falls within the scope of the warrant. It can be assumed that Parliament chose not to limit s. 487(1) to evidence establishing an element of the Crown's prima facie case. To conclude otherwise would effectively delete the phrase "with respect to" from the section. While s. 487(1) is broad enough to authorize the search in question even absent this phrase, the inclusion of these words plainly supports the validity of these warrants. Although s. 487(1) is part of the Criminal Code, and may occasion significant invasions of privacy, the public interest requires prompt and thorough investigation of potential offences. It is with respect to that interest that all relevant information and evidence should be located and preserved as soon as possible. This interpretation accords with the purposes underlying the Criminal Code and the demands of a fair and expeditious administration of justice. Furthermore, denying the Crown the ability to gather evidence in anticipation of a defence would have serious consequences on the functioning of our justice system. While the broad powers contained in s. 487(1) do not authorize investigative fishing expeditions, nor do they diminish the proper privacy interests of individuals or corporations, in this case the specific terms of the warrant were not at issue, as the respondents challenged only the underlying authority to grant warrants for the purpose of investigating the presence of negligence. Both a plain reading of the relevant section and consideration of the role and obligations of state investigators support the conclusion that s. 487(1) authorized the granting of the warrants in question.

**Cases Cited**

Referred to: Re Domtar Inc. (1995), 18 C.E.L.R. (N.S.) 106; Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27; Nowegijick v. The Queen, [1983] 1 S.C.R. 29; R. v. McIntosh, [1995] 1 S.C.R. 686; Re Church of Scientology and the Queen (No. 6) (1987), 31 C.C.C. (3d) 449; R. v. Storrey, [1990] 1 S.C.R. 241; Nelles v. Ontario, [1989] 2 S.C.R. 170; R. v. Levogiannis, [1993] 4 S.C.R. 475; Hunter v. Southam Inc., [1984] 2 S.C.R. 145; Descôteaux v. Mierzwinski, [1982] 1 S.C.R. 860; Thomson Newspapers Ltd. v. Canada (Director of Research and Investigation, Restrictive Trade Practices Commission), [1990] 1 S.C.R. 425; Baron v. Canada, [1993] 1 S.C.R. 416.

**Statutes and Regulations Cited**

Criminal Code, R.S.C., 1985, c. C-46, s. 487(1)(b) [am. c. 27 (1st Supp.), s. 68; am. 1994, c. 44, s. 36].
Fisheries Act, R.S.C., 1985, c. F-14, ss. 36(3), 40(2).

Interpretation Act, R.S.C., 1985, c. I-21, s. 12.
Waste Management Act, S.B.C. 1982, c. 41, ss. 3(1.1) [ad. 1985, c. 52, s. 96], 34(3).

**Authors Cited**

Ontario. Commission on Proceedings Involving Guy Paul Morin. Report, vol. 1. Toronto: Ontario Ministry of the Attorney General, 1998.

APPEAL from a judgment of the British Columbia Court of Appeal (1997), 145 D.L.R. (4th) 427, 90 B.C.A.C. 126, 147 W.A.C. 126, 114 C.C.C. (3d) 537, [1997] B.C.J. No. 724 (QL), affirming a decision of the British Columbia Supreme Court (1996), 138 D.L.R. (4th) 104, 108 C.C.C. (3d) 497, [1996] B.C.J. No. 1482 (QL), quashing certain search warrants. Appeal allowed.

S. David Frankel, Q.C., and Kenneth Yule, for the appellant.
Gary A. Letcher, Jonathan S. McLean and Eric B. Miller, for the respondents.
Michal Fairburn, for the intervener.

Solicitor for the appellant: The Attorney General of Canada, Vancouver.
Solicitors for the respondents: Edwards, Kenny & Bray, Vancouver.
Solicitor for the intervener: The Attorney General for Ontario, Toronto.

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The judgment of the Court was delivered by

1 **MAJOR J.**:-- This appeal raises the question of whether search warrants issued under s. 487(1)(b) of the Criminal Code, R.S.C., 1985, c. C-46, authorize investigators to search for and seize evidence of negligence in the investigation of strict liability offences. At the conclusion of argument the question was answered in the affirmative and the appeal was allowed with reasons to follow.

I. Facts

2 On October 13, 1994 a chlor-alkali plant operated by the respondents (collectively referred to as "CanadianOxy") in North Vancouver, British Columbia discharged a quantity of chlorine into the waters of Burrard Inlet, killing a number of fish. This incident occurred during a three and a half hour power outage at the plant, as a result of one of two B.C. Hydro 60 kv power lines servicing the plant being struck by a tree.

3 The company reported the discharge to the authorities and an investigation by the Department of Fisheries and Oceans followed. Fishery Officer Robert Tompkins went to the plant that night, spoke with the Plant Chemist, and seized a number of documents. He also seized samples of dead fish recovered in the vicinity of the plant by the Harbour Master's patrol vessel. He advised the Plant Manager that he had reasonable grounds to believe that an offence had been committed under the Fisheries Act, R.S.C., 1985, c. F-14.

**4** Over a short time Tompkins made three further visits to the plant, formally interviewed the Plant Chemist, was shown the valve which the company had identified as the cause of the discharge and was provided with certain documents. His request to interview additional employees was refused.

**5** Tompkins subsequently made a written request to CanadianOxy's counsel for additional technical information believed relevant for Environment Canada's Pollution Abatement Division to assess whether the discharge had been preventable. Only a few of these questions were answered.

**6** On March 16, 1995, five months after the discharge, Tompkins swore an information and obtained a warrant to search the respondents' plant for a range of documents relating to process records, plant maintenance, employee training, discipline, and general plant operations. In the information, Tompkins described the reasons for seeking this information:

> The business records ... are required to establish and prove that CanadianOxy Chemicals Ltd... . operate a chlor-alkali plant that discharges effluent to the waters of Burrard Inlet near North Vancouver, B.C., that the release of effluent with a chlorine concentration exceeding 10 ppm, which I know would be acutely lethal to fish, occurred on October 13, 1994, and that the company could have taken additional reasonable measures to prevent the release of a deleterious substance into water frequented by fish....
>
> ... I have reasonable grounds to believe that correspondence had been generated by company personnel in January 1994, and that maintenance was performed in March 1994, and again in October 1994, and that the company conducted their own investigation, prepared reports, and provided information regarding the incident until February 1995... .
>
> It is necessary to examine effluent discharge records, effluent water quality sampling and analysis records, mechanical and instrument maintenance records, environmental control records, instrument calibration records and flow rate calculation records covering an extended period of time before and after October 13, 1994. This will ... permit analysis of the maintenance programs undertaken by CanadianOxy Chemicals Ltd.
>
> It is necessary to examine company personnel records covering the period between January 1, 1994 and February 28, 1995 ... to determine if any company employees have been disciplined in any manner as a result of this incident... .

**7** The warrant was executed on March 17, 1995. In total 139 items were seized pursuant to the warrant, and 73 additional items were seized under the investigators' understanding of the "plain view" doctrine. Following the search, Tompkins learned by coincidence of an adverse ruling by a British Columbia Provincial Court judge on the validity of a similar seizure in an unrelated case. As a result, he sought legal advice with respect to a number of the items taken.

**8** On April 26, 1995, Tompkins made two applications to a Justice of the Peace, one for an order to return the documents which had been improperly seized under the first warrant, and the se-

cond for a new warrant to re-seize 13 of the items returned which were relevant to the investigation. These orders were granted and executed the same day.

**9** On June 15, 1995 the respondents were charged with:

> (a) depositing, or permitting the deposit, of a deleterious substance in waters frequented by fish, contrary to ss. 36(3) and 40(2) of the Fisheries Act; and
> (b) introducing, or causing or allowing the introduction of waste into the environment, contrary to ss. 3(1.1) and 34(3) of the Waste Management Act, S.B.C. 1982, c. 41 (now R.S.B.C. 1996, c. 482).

**10** The respondents subsequently brought a motion to quash the warrants alleging that s. 487(1) of the Criminal Code had been exceeded. The warrants were broad enough to authorize a search for evidence of negligence which if found would negate a defence of due diligence.

## II. Judicial History

### A. British Columbia Supreme Court (1996), 138 D.L.R. (4th) 104

**11** Sigurdson J. felt bound by Re Domtar Inc. (1995), 18 C.E.L.R. (N.S.) 106 (B.C.S.C.), which held that a s. 487 warrant could not be used to search for and seize evidence of negligence going to the defence of due diligence. As a result, he ruled that the documents seized pertaining to the issue of due diligence were not documents with respect to the commission of this particular offence and quashed both warrants.

### B. British Columbia Court of Appeal (1997), 145 D.L.R. (4th) 427

**12** In dismissing the appeal, Goldie J.A. (Carrothers J.A. concurring) held that the appellant had failed to demonstrate on any reasonable construction that s. 487(1)(b) authorizes the issuance of a warrant that includes a search for evidence with respect to due diligence in a regulatory offence. In dissent, Southin J.A. concluded that a warrant can issue upon proper evidence to search for and seize things relating to the question of due diligence.

## III. Analysis

**13** At issue is whether search warrants issued pursuant to s. 487(1) of the Criminal Code are limited only to evidence relevant to an element of the offence which is part of the Crown's prima facie case, or whether such warrants encompass evidence that may relate to potential defences, such as due diligence, which may or may not be raised at the trial. The relevant section of the Code provides:

> 487. (1) A justice who is satisfied by information on oath in Form 1 that there are reasonable grounds to believe that there is in a building, receptacle or place
>
> ...
>
> (b) anything that there are reasonable grounds to believe will afford evidence with respect to the commission of an offence, or will reveal the wherea-

> bouts of a person who is believed to have committed an offence, against this Act or any other Act of Parliament,
>
> ...
>
> may at any time issue a warrant under his hand authorizing a person named therein or a peace officer
>
> (d) to search the building, receptacle or place for any such thing and to seize it ... [Emphasis added.]

**14** Statutory provisions should be read to give the words their most obvious ordinary meaning which accords with the context and purpose of the enactment in which they occur; Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27, at paras. 21-22. It is only when genuine ambiguity arises between two or more plausible readings, each equally in accordance with the intentions of the statute, that the courts need to resort to external interpretive aids. In our opinion there is no such ambiguity in s. 487(1).

A. The Ordinary Meaning of the Words

**15** On a plain reading, the phrase "evidence with respect to the commission of an offence" is a broad statement, encompassing all materials which might shed light on the circumstances of an event which appears to constitute an offence. The natural and ordinary meaning of this phrase is that anything relevant or rationally connected to the incident under investigation, the parties involved, and their potential culpability falls within the scope of the warrant.

**16** This reading is supported by Dickson J.'s interpretation of almost identical language in Nowegijick v. The Queen, [1983] 1 S.C.R. 29, at p. 39:

> The words "in respect of" are, in my opinion, words of the widest possible scope. They import such meanings as "in relation to", "with reference to" or "in connection with". The phrase "in respect of" is probably the widest of any expression intended to convey some connection between two related subject matters. [Emphasis added.]

**17** We can assume that Parliament chose not to limit s. 487(1) to evidence establishing an element of the Crown's prima facie case. To conclude otherwise would effectively delete the phrase "with respect to" from the section. While s. 487(1) is broad enough to authorize the search in question even absent this phrase, the inclusion of these words plainly supports the validity of these warrants.

**18** The respondents urged that s. 487(1) be given a restrictive reading in accordance with the principle that an ambiguous penal statute should be interpreted in a manner most favourable to an accused: see R. v. McIntosh, [1995] 1 S.C.R. 686, at para. 39. That argument was rejected as, in our opinion, this section is neither ambiguous, nor the type of penal provisions to which the rule should apply. Instead, s. 487 should be given a liberal and purposive interpretation; Interpretation Act, R.S.C., 1985, c. I-21, s. 12.

**19** While s. 487(1) is part of the Criminal Code, and may occasion significant invasions of privacy, the public interest requires prompt and thorough investigation of potential offences. It is with respect to that interest that all relevant information and evidence should be located and preserved as soon as possible. This interpretation accords with the purposes underlying the Criminal Code and the demands of a fair and expeditious administration of justice.

B. Purpose of the Search Warrant Provisions of the Criminal Code

**20** A primary, though not exclusive, purpose of the Criminal Code, and penal statutes in general, is to promote a safe, peaceful and honest society, This is achieved by providing guidelines prohibiting unacceptable conduct, and providing for the just prosecution and punishment of those who transgress these norms. The prompt and comprehensive investigation of potential offences is essential to fulfilling that purpose. The point of the investigative phase is to gather all the relevant evidence in order to allow a responsible and informed decision to be made as to whether charges should be laid.

**21** At the investigative stage the authorities are charged with determining the following: What happened? Who did it? Is the conduct criminally culpable behaviour? Search warrants are a staple investigative tool for answering those questions, and the section authorizing their issuance must be interpreted in that light.

**22** The purpose of s. 487(1) is to allow the investigators to unearth and preserve as much relevant evidence as possible. To ensure that the authorities are able to perform their appointed functions properly they should be able to locate, examine and preserve all the evidence relevant to events which may have given rise to criminal liability. It is not the role of the police to investigate and decide whether the essential elements of an offence are made out - that decision is the role of the courts. The function of the police, and other peace officers, is to investigate incidents which might be criminal, make a conscientious and informed decision as to whether charges should be laid, and then present the full and unadulterated facts to the prosecutorial authorities. To that end an unnecessary and restrictive interpretation of s. 487(1) defeats its purpose. See Re Church of Scientology and the Queen (No. 6) (1987), 31 C.C.C. (3d) 449, p. 475:

> Police work should not be frustrated by the meticulous examination of facts and law that is appropriate to a trial process... . There may be serious questions of law as to whether what is asserted amounts to a criminal offence... . However, these issues can hardly be determined before the Crown has marshalled its evidence and is in a position to proceed with the prosecution.

**23** Moreover, extrinsic factors such as the accused's motive or the failure to exercise due diligence are often relevant to determining whether the event which triggered the investigation in the first place is criminally culpable. Everyone, including accused persons, who lacks the means of obtaining and preserving evidence prior to trial has an interest in seeing that these facts are brought to light. It would be undesirable if a narrow reading of s. 487(1) resulted in either inculpatory or exculpatory evidence being lost because of the investigators' inability to secure it. See R. v. Storrey, [1990] 1 S.C.R. 241, per Cory J., at p. 254:

> The essential role of the police is to investigate crimes. That role and function can and should continue after they have made a lawful arrest. The continued in-

> vestigation will benefit society as a whole and not infrequently the arrested person. It is in the interest of the innocent arrested person that the investigation continue so that he or she may be cleared of the charges as quickly as possible.

**24** It is important that an investigation unearth as much evidence as possible. It is antithetical to our system of justice to proceed on the basis that the police, and other authorities, should only search for evidence which incriminates their chosen suspect. Such prosecutorial "tunnel vision" would not be appropriate: see The Commission on Proceedings Involving Guy Paul Morin: Report, vol. 1 (1998), per the Honourable F. Kaufman at pp. 479-82.

**25** In Nelles v. Ontario, [1989] 2 S.C.R. 170, Lamer J. (later C.J.C.) stated for the majority that:

> Traditionally the Crown Attorney has been described as a "minister of justice" and "ought to regard himself as part of the Court rather than as an advocate". (Morris Manning, "Abuse of Power by Crown Attorneys", [1979] L.S.U.C. Lectures 571, at p. 580, quoting Henry Bull, Q.C.) As regards the proper role of the Crown Attorney, perhaps no more often quoted statement is that of Rand J. in Boucher v. The Queen, [1955] S.C.R. 16, at pp. 23-24:
>
> > It cannot be over-emphasized that the purpose of a criminal prosecution is not to obtain a conviction, it is to lay before a jury what the Crown considers to be credible evidence relevant to what is alleged to be a crime. Counsel have a duty to see that all available legal proof of the facts is presented: it should be done firmly and pressed to its legitimate strength but it must also be done fairly. The role of prosecutor excludes any notion of winning or losing; his function is a matter of public duty than which in civil life there can be none charged with greater personal responsibility.

**26** The majority of the British Columbia Court of Appeal found that the word "commission" in s. 487(1) restricted its application to evidence that the accused had done those acts, or allowed those omissions, which constitute the elements of the offence. The criminal justice system is not solely concerned with whether a prima facie case can be made out against an accused, but whether he or she is ultimately guilty. The dissenting reasons of Southin J.A. are persuasive on both the purpose and meaning of s. 487(1). At para. 63 she stated:

> ... I would translate the words in issue to mean "touching upon whether a breach of the law involving a penal sanction has occurred". Whether or not there can be said to have been such a breach depends upon whether there can be a penal sanction and there can be no sanction without a conviction.

**27** In addition, as pointed out by the intervener Attorney General of Ontario, denying the Crown the ability to gather evidence in anticipation of a defence would have serious consequences on the functioning of our justice system. In order to be fair, the criminal process must "enable the trier of fact to 'get at the truth and properly and fairly dispose of the case' while at the same time providing the accused with the opportunity to make a full defence"; R. v. Levogiannis, [1993] 4 S.C.R. 475, at p. 486. This reciprocal fairness demands that the Crown be able to fairly seek and obtain evidence rebutting the accused's defences. If the respondents' submission on the interpretation of s. 487(1) were accepted, a search warrant would never be available for this purpose. This

narrow interpretation would frustrate the basic imperative of trial fairness and the search for truth in the criminal process.

C. Privacy Concerns

**28** There is no doubt that search warrants are highly intrusive, and that an investigation bearing on the issue of due diligence could, as Shaw J. pointed out in Re Domtar, supra, at p. 119, "entail a detailed inquiry into the affairs of a corporation over a period of several years". This Court has endorsed the importance of privacy and the need to constrain search powers within reasonable limits: Hunter v. Southam Inc., [1984] 2 S.C.R. 145; Descôteaux v. Mierzwinski, [1982] 1 S.C.R. 860, at p. 889; Thomson Newspapers Ltd. v. Canada (Director of Research and Investigation, Restrictive Trade Practices Commission), [1990] 1 S.C.R. 425, at pp. 520-22; Baron v. Canada, [1993] 1 S.C.R. 416, at pp. 436-37.

**29** The broad powers contained in s. 487(1) do not authorize investigative fishing expeditions, nor do they diminish the proper privacy interests of individuals or corporations. This is particularly true with respect to personnel records which may contain a great deal of highly personal information unrelated to the investigation at hand. Judges and magistrates should continue to apply the standards and safeguards which protect privacy from unjustified searches and seizures.

**30** In this case, however, the specific terms of the warrant were not at issue, as the respondents challenged only the underlying authority to grant warrants for the purpose of investigating the presence of negligence. In our opinion both a plain reading of the relevant section and consideration of the role and obligations of state investigators support the conclusion that s. 487(1) authorized the granting of the warrants at issue.

IV. Disposition

**31** The appeal is allowed, without costs, as agreed by counsel.

cp/d/hbb

# Tab 18

*Indexed as:*

# Nastamagu v. Axa Insurance (Canada)

**Between**
**Peter Nastamagu, applicant (appellant), and**
**Axa Insurance (Canada), respondent**

[1997] O.J. No. 2362

34 O.R. (3d) 29

148 D.L.R. (4th) 244

101 O.A.C. 67

27 M.V.R. (3d) 202

71 A.C.W.S. (3d) 1155

Docket No. C15767

Ontario Court of Appeal
Toronto, Ontario

**McMurtry C.J.O., Osborne and Charron JJ.A.**

Heard: February 6, 1997.
Judgment: June 10, 1997.

(10 pp.)

*Insurance -- Automobile insurance -- Accident benefits -- Death benefit, entitlement, exclusionary clauses, effect of -- Exclusions -- Payments by workers' compensation.*

This was an appeal from a judgment which determined that the appellant was not entitled to the no-fault benefits under his automobile insurance policy. The appellant was the named insured under the policy and the deceased, his daughter, was engaged in her employment when the accident occurred. The appellant submitted that he was entitled to both the death benefit and the funeral benefits prescribed in the policy because the workers' compensation exclusion in the policy did not ex-

clude entitlement to no-fault benefits when the insured person died as a result of the accident. The motions judge rejected the submission.

HELD: Appeal dismissed. In the case of a fatal accident, section 20 of the No-Fault Benefits Regulation under the Insurance Act provided that if an insured person, at the time of an accident, was entitled to workers compensation benefits, no-fault benefits would not be paid either to the insured person in cases of personal injury, or in respect of that person if the insured person died.

**Statutes, Regulations and Rules Cited:**

Insurance Act, R.S.O. 1990, c. I-8.
No-Fault Benefits Regulation 672/90, ss. 10, 11(2)(d), 20, 21.

**Counsel:**

Gloria Balaban, for the appellant.
Lawrence M. Foy, for the respondent.

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The judgment of the Court was delivered by

1 **OSBORNE J.A.**:-- This appeal requires the court to determine the scope of the workers' compensation exclusion in the no-fault section of the appellant's automobile insurance policy. This exclusion relieves an automobile insurer from any obligation to pay no-fault benefits in respect of a person who is entitled to receive workers' compensation benefits as a consequence of a motor vehicle accident. In particular, this appeal raises the issue of the application of the workers' compensation exclusion where a dependent of the named insured is killed. In this case, the appellant was the named insured and the deceased, his daughter, was engaged in her employment when the accident occurred. The appellant contends that he is entitled to be paid both the death benefit and the funeral benefits prescribed by his automobile insurance policy because, in the appellant's submission, the workers' compensation exclusion in his policy does not exclude his entitlement to these no-fault benefits when the insured person dies as a result of the accident. The motion's judge, O'Brien J., rejected this submission. He held that the workers' compensation exclusion applied and that the appellant was not entitled to no-fault benefits set out in the appellant's automobile insurance policy.

THE FACTS

2 The facts are agreed upon and can be dealt with in summary form. On August 5, 1992 the appellant's daughter was killed in a motor vehicle accident when she was directing traffic at a construction site, as an employee of a construction company. The driver of the motor vehicle that struck her was also engaged in the course of his employment at the time of the accident. Both he and the deceased were employed by employers covered by Schedule 1 of the Workers' Compensation Act, R.S.O. 1990, c. W.11.

3 The deceased lived at home and was a dependent of the appellant for purposes of the automobile insurance policy issued by the respondent AXA Insurance to the appellant. The appellant's policy included a provision for the payment of funeral expenses to a maximum of $7,500 and a death benefit of $20,000 on a no-fault basis in respect of his daughter's death. When the appellant

submitted a claim for these benefits, the insurer denied his claim. Its denial was based upon the fact that the deceased was entitled to workers' compensation benefits in that she worked for a Workers' Compensation Schedule 1 employer and she was engaged within the scope and course of her employment at the time of the accident. The deceased was an "insured person" for purposes of the no-fault benefit provisions of the appellant's policy.

**4** Following the insurer's denial, the appellant applied for mediation to the Ontario Insurance Commission pursuant to the provisions of the Insurance Act, R.S.O. 1990, c. I.8. After determining the positions of the parties, the mediator concluded that "mediation would fail."

**5** Once it was determined that mediation would not work, the appellant made application under Rule 14.05 for a declaration that he was entitled to payment of $27,500 (death benefit $20,000, funeral benefit $7,500) under the no-fault benefit provisions of his automobile insurance policy. The application came before O'Brien J. who dismissed it. It is from that order that the appellant appeals.

ANALYSIS

**6** The insurer's denial was based upon its interpretation of s. 20 of Part VII of the "No-Fault Benefit Schedule" of Ontario Regulation 672/90 of the Insurance Act, R.S.O. 1990, c. I.8. I set out below s. 20 as well as ss. 10, 11(2)(d) and 21 of Regulation 672/90.

> Funeral Expenses
>
> 10. The insurer will pay with respect to each insured person who dies as a result of an accident funeral expenses incurred up to $3,000 if Optional Benefit 1 has not been purchased, and up to $7,500 if it has been purchased.
>
> Death Benefits
>
> 11.(2) If, as a result of an accident, an insured person dies within the benefit period set out in subsection (3), the insurer will pay with respect to the insured person, if Optional Benefit 1 has been purchased,
>
> ...
>
> (d) if, at the time of the accident, the deceased was a dependant, $20,000,
>
> (i) to the person upon whom the deceased was dependent or, if that person is dead, to the surviving spouse of that person if the surviving spouse was the deceased's primary caregiver.
>
> Effect of Workers' Compensation Benefits
>
> 20. The insurer will not pay benefits under this Schedule in respect of any insured person who, as a result of an accident, is entitled to receive benefits under any workers' compensation law or plan.

Interim Payments

21.(1) Despite section 20, the insurer will pay full benefits under this Schedule to a person described in that section until the resolution of any action brought by the person in any court to recover for personal injuries resulting from the accident under which the workers' compensation claim arose or until the person receives payments under a workers' compensation law or plan if,

(a) the person makes an assignment to the insurer of any benefits under any workers' compensation law or plan to which he or she is or may become entitled as a result of the accident;
(b) the administrator or board responsible for the administration of the workers' compensation law or plan approves the assignment.

**7** Sections 10 and 11 of Regulation 672/90 provide that upon the death of an insured person the insurer will pay funeral expenses (s. 10) and a death benefit (s. 11(2)(d)(i). As I have said, the deceased was an insured person for purposes of the application of ss. 10 and 11.

**8** Section 20 of Regulation 672, set out above, is in Part VII of Regulation 672 which carries the general title, "Workers' Compensation" and the sub-title, "Effect of Workers' Compensation Benefits." The appellant's broad submission is that the language of s. 20 cannot be interpreted to apply to an insured person who is deceased. In particular, the appellant submits that an insured person who dies as a result of an automobile accident is not entitled to receive benefits. Rather, the person who is entitled to receive benefits, is "the person upon whom the deceased was dependent", that is the appellant. Thus, the appellant contends that the s. 20 workers' compensation exclusion does not apply when there is a fatality as occurred here.

**9** Section 20 reflects the general policy of the Legislature that in cases where an insured person is entitled to receive workers' compensation benefits, the workers' compensation plan, not the automobile insurance policy, must be looked to as a the source of payment of any no-fault benefits to which the claimant may be entitled. The question to be answered is whether its language extends the ambit of the exclusion to cases where the insured person is killed.

**10** Comparing the language of ss. 20 and 21 of the Regulation is, I think, helpful in determining the scope of the s. 20 exclusion. Section 21, which has nothing directly to do with this case, applies by its clear terms only to automobile accidents giving rise to personal injuries, not fatalities. In that context, it sets out a scheme for interim payments "to a person". By contrast, s. 20's language is more general. It does not refer to payment to a person but rather to the payment of benefits "in respect of any insured person." In my opinion, had the Legislature intended that the workers' compensation exclusion would apply only in circumstances where there was a personal injury as opposed to a death, the language used in s. 20 would have clearly said so in terms generally similar to the language used in s. 21, which as I have noted applies only to personal injury situations. The words "in respect of" in s. 20 are words of wide scope. See Nowegijick v. The Queen (1983), 144 D.L.R. (3d) 193 at 200 (S.C.C.). The words in s. 20 "... entitled to receive benefits," are descriptive in the sense that they identify an insured person who is entitled to receive workers' compensation benefits at the time of the accident. That entitlement, for purposes of the section, would exist if the insured person is injured or killed as a result of the accident. Thus, it seems to me that the Legisla-

ture recognized that s. 20, unlike s. 21, would apply to accidents resulting in either personal injuries or death.

**11** In my opinion, in a fatal accident context, s. 20 provides that if an insured person at the time of an accident is entitled to workers' compensation benefits, no-fault benefits under the Schedule will not be paid either to the insured person, in cases of personal injury, or "in respect of" that person, if the insured person dies. In my view, benefits payable or not payable "in respect of any insured person" as set out in s. 20, covers both personal injury and fatal accident situations.

**12** It seems to me that the threshold question to be answered when the application of s. 20 is considered is whether the insured person at the time of the accident is entitled to workers' compensation benefits. In this case the deceased, who was an insured person, was entitled to workers' compensation benefits at the time of the accident and it is clear to me that the workers' compensation exclusion applies. In my opinion, this interpretation of s. 20 does not expand the exclusion; it does no more than give effect to the language of the section in a way that is consistent with the section's purpose.

**13** The Ontario Insurance Commission (Mr. Guy Jones, Arbitrator) reached a different conclusion in Lupien v. General Accident Assurance Co. of Canada, December 28, 1995. In that case, the Arbitrator concluded that the "insured person" was the deceased and because a deceased person could not receive no-fault benefits, the s. 20 exclusion did not apply. Thus, the Arbitrator held that the applicants were entitled to the no-fault benefits that they claimed. In my view, the Arbitrator's interpretation of s. 20 is too narrow. It does not take into proper account the broad language of the section, having regard to its clear purpose.

**14** My analysis of the meaning to be given to s. 20 of Regulation 672 leads to a result that is consistent with the decision of Turnbull J. in Daigle v. Markel Insurance Co. of Canada (1991), 116 N.B.R. (2d) 403 (Q.B.). That court in Daigle concluded that because the deceased was entitled to workers' compensation benefits, his common law spouse could not recover no-fault benefits under the New Brunswick auto policy. The workers' compensation exclusion contained in the New Brunswick policy is worded differently from the workers' compensation exclusion in the relevant Ontario policy, however, in substance the two exclusions are similar.

**15** The appellant also submits that the payment of funeral and burial expenses under s. 35(9) of the Workers' Compensation Act is not the payment of a benefit for purposes of s. 20 (which refers to the entitlement to receive "benefits" under any workers' compensation plan) but rather the payment of an expense. I see no merit in this submission. The commitment to pay an expense incurred is a benefit to the recipient of the payment. Moreover, Part VI of the Regulation 672, titled "Optional Benefits", [emphasis added] includes both funeral expenses and death benefits as part of the optional benefits package.

CONCLUSION

**16** For these reasons, I think the motions judge was correct in concluding that the respondent insurer is not required to pay the benefits claimed. I would, therefore, dismiss the appeal with costs.

OSBORNE J.A.
McMURTRY C.J.O. -- I agree.
CHARRON J.A. -- I agree.

cp/d/ala/DRS/DRS/qlhjk

# Tab 19

*Case Name:*

# Arsenault v. Dumfries Mutual Insurance Co.

**Between**
**Evelyn Arsenault, plaintiff (appellant), and**
**Dumfries Mutual Insurance Company, defendant (respondent)**

[2002] O.J. No. 4

57 O.R. (3d) 625

152 O.A.C. 224

[2002] I.L.R. I-4086

20 M.V.R. (4th) 165

2002 CanLII 23580

110 A.C.W.S. (3d) 1138

Docket No. C35942

Ontario Court of Appeal
Toronto, Ontario

**Abella, MacPherson and Cronk JJ.A.**

Heard: November 23, 2001.
Judgment: January 8, 2002.

(22 paras.)

On appeal from the order of Justice Blenus Wright dated February 14, 2001.

**Counsel:**

David S. Wilson, for the appellant.
H. Wayne Snyder, for the respondent.

[Quicklaw note: A corrigendum was released by the Court January 9, 2002, and April 19, 2002. The corrections have been made to the text and the corrigendums are appended to this document.]

The judgment of the Court was delivered by

**1** ABELLA J.A.:-- The issue in this appeal is whether a claim for bad faith damages arising out of an insurer's termination of no-fault accident benefits is subject to the two-year limitation period set out in s. 281(5) of the Insurance Act, R.S.O. 1990, c. I.8, as amended.[1]

**2** The appellant, Evelyn Arsenault, was injured in a motor vehicle accident on May 1, 1993. She was 54 years old at the time of the accident, and had been employed as a receptionist/secretary at a medical centre.

**3** The insurer responsible for the payment of her statutory accident benefits was Dumfries Mutual Insurance Company. Pursuant to its obligations as set out in the Statutory Benefits Schedule - Accidents Before January 1, 1994,[2] the insurer paid weekly benefits of $405.52 to Ms. Arsenault until September 30, 1995.

**4** Early in 1994, Ms. Arsenault's family doctor suggested that she could probably work part-time by the end of February, 1994. On her return from a two-week holiday in Florida, Ms. Arsenault informed her rehabilitation counsellor that her condition had deteriorated due to depression. Consequently, the insurer arranged for a medical assessment in April, 1994, the result of which was a diagnosis that maximum medical recovery - and a return to part-time employment - would be possible with the assistance of anti-depressant medication and, if desired, psychiatric assistance.

**5** Accordingly, arrangements were made for Ms. Arsenault to begin working two hours daily with her former employer starting June 21, 1994. Since the employer had already hired another employee to do Ms. Arsenault's job, the insurer agreed that there would be no cost to the employer and that it would continue paying weekly income benefits.

**6** By August 16, 1994, Ms. Arsenault was working five days a week for five hours daily. Her family doctor referred her for psychological counselling and advised her to decrease her hours and days of work.

**7** By the time she left for a 3-4 week holiday in Florida in January, 1995, Ms. Arsenault was working four hours daily for two days a week. Both her family doctor and the insurer's doctor recommended on her return from Florida that she expand her work schedule. Ms. Arsenault agreed to these recommendations, along with a referral to a psychiatrist, in April, 1995.

**8** By mid-May, however, Ms. Arsenault was not complying with either the proposed home-based exercise program or the graduated return-to-work schedule. A new rehabilitation plan was therefore entered into in June, 1995. This amended plan too was not followed by Ms. Arsenault. Another doctor, arranged by the insurer, diagnosed Ms. Arsenault on August 31, 1995 as suffering from chronic pain syndrome and depression, but agreed with all the other medical assessments that she was able to return to work.

**9** The insurer notified Ms. Arsenault on September 8, 1995 that her weekly benefits would be discontinued. Around September 30, 1995, the payment of these benefits was terminated.

**10** In June 1996, Ms. Arsenault applied for mediation under s. 280 of the Insurance Act, disputing the termination of her weekly benefits. The mediation, conducted between August 12 and September 19, 1996, was unsuccessful. Ms. Arsenault took no further legal steps until she commenced an action on June 13, 2000, claiming damages for the insurer's "bad faith" conduct in prematurely terminating her weekly benefits.

**11** After all the pleadings had been filed, the insurer brought a motion under Rule 21.01(1)(a) for a determination of the following question of law raised in the Statement of Defence and for an order striking all paragraphs of the Plaintiff's Statement of Claim referable to the claim for bad faith damages on the ground that the claim was statute-barred by s. 279(1) and s. 281(5) of the Insurance Act.

> Is the Plaintiff's action for bad faith damages commenced on June 13, 2000 statute-barred by reason of s. 281(5) of the Insurance Act, R.S.O. 1990, c. I.8 (a two-year limitation period).

**12** On February 14, 2001, Justice B. Wright granted the relief requested. For the following reasons, I agree with his order.

**13** The dispute resolution scheme in the Insurance Act is found in ss. 279-283. Section 279(1) states that any disputes in respect of any insured person's entitlement to, or amount of, no-fault benefits are to be resolved in accordance with ss. 280 to 283. Section 280(1) provides that either the insured or the insurer may refer any such dispute to a mediator. If, and only if, mediation is unsuccessful, ss. 281(1) and (2) permit the insured either to bring a proceeding in court or to refer the mater to arbitration. Under s. 281(5), court or arbitration proceedings must be brought within two years of the insurer's refusal to pay the benefit claimed.

**14** In this case, the insurer terminated the weekly benefits on September 30, 1995. A plain reading of s. 281(5) yields the conclusion that court proceedings should have been commenced within two years of this triggering event. Ms. Arsenault, however, did not start her action until almost five years had elapsed since the insurer's refusal to continue paying benefits. She argues that this court's decision in Whiten v. Pilot Insurance Company (1999), 42 O.R. (3d) 641 (C.A.)[3] entitles her to bring a separate action for damages resulting from the insurer's bad faith conduct, and that the limitation period for this cause of action is six years.

**15** Section 279(1) is a mandatory provision for the resolution of disputes "*in respect of* any insured person's entitlement to no-fault benefits "*in respect of* of the amount of no-fault benefits to which an insured person is entitled". [Emphasis added.] There is no option for an insured but to proceed in accordance with the scheme outlined in ss. 280 to 283 if the dispute is in respect of entitlement issues. Section 281(5) states that a proceeding in a court or an arbitration ""*in respect of* no-fault benefits" must be commenced within two years after the insurer's refusal to pay the benefits claimed.

**16** In Nowegijick v. The Queen et al. (1983), 144 D.L.R. (3d) 193 at 200 (S.C.C.), Dickson J. attributed the "widest possible scope" to the words "in respect of":

> The phrase "in respect of" is probably the widest of any expression intended to convey some connection between two related subject-matters.

**17** Although Justice Dickson was dealing with language in the Income Tax Act, in my view, his observation is generic and equally applicable to the relevant Insurance Act provisions in this case. That means that any and all disputes about an insurer's refusal to pay no-fault benefits, including disputes which allege the insurer's bad faith in connection with that refusal, must be brought within two years of the refusal.

**18** I am prepared to assume, without deciding, that there can be an independent claim for bad faith conduct in respect of the insurer's refusal to pay or continue to pay no-fault benefits. In order to establish such a claim, the appellant would first have to establish that the insurer's termination of her benefits was improper. Such a claim must comply with the requirements outlined in ss. 280-283 of the Insurance Act, one of which is the two year limitation period for the institution of proceedings to determine this question. The appellant cannot, by the device of a claim for bad faith damages, extend threefold the length of that termination period.

**19** If I am wrong in concluding that bad faith claims in connection with no-fault benefits refusals are subject to the procedures and time limits set out in ss. 280 to 283 of the Insurance Act, I am nonetheless of the view, based on the pleadings, that this appellant's claim is not an independent, actionable wrong, but is in fact exactly the kind of dispute over no-fault benefits entitlements contemplated by the dispute resolution scheme in the Insurance Act. The allegation is that the insurer ought not to have terminated Ms. Arsenault's benefits when it did. This is the issue she attempted, unsuccessfully, to resolve through mediation. She then had the choice of either starting a court action or filing an application for the appointment of an arbitrator under s. 282 of the Insurance Act. Moreover, had the dispute been arbitrated, it was open to the arbitrator under s. 282(10), if it was found that the insurer had "unreasonably withheld or delayed payments", to award an additional lump sum.[4]

**20** Rather than proceeding with either court action or arbitration, Ms. Arsenault took no further steps for a number of years. When she did, she brought an action that was, on its face, clearly "in respect of" the insurer's refusal of further no-fault benefits. It was therefore an action that, under s. 281(5),[5] had to be started no later than two years after that refusal.

**21** Ms. Arsenault's characterization of the insurer's refusal as bad faith conduct is merely an attempt to circumvent the mandatory requirements of the dispute resolution scheme in the Insurance Act through the guise of linguistic reformulation. Her allegations, distilled, are that the refusal was inappropriate in the circumstances, the very issue contemplated for resolution under the scheme, and a claim that is clearly subject to the two year limitation period set out in s. 281(5).

**22** I would therefore dismiss the appeal with costs.

ABELLA J.A.
MacPHERSON J.A. -- I agree.
CRONK J.A. -- I agree.

* * * * *

APPENDIX

The Insurance Act, R.S.O. 1990, c. I.8

279.(1) Disputes in respect of any insured person's entitlement to statutory accident benefits or in respect of the amount of statutory accident benefits to which an insured person is entitled shall be resolved in accordance with sections 280 to 283 and the Statutory Accident Benefits Schedule.

...

280.(1) Either the insured person or the insurer may refer to a mediator any matter in dispute in respect of the insured person's entitlement to no-fault benefits or in respect of the amount of no-fault benefits to which the insured person is entitled.

(2) The party seeking mediation shall file an application for the appointment of a mediator with the Commission.

(3) The Director shall ensure that a mediator is appointed promptly.

(4) The mediator shall enquire into the issues in dispute and attempt to effect a settlement of as many of the issues as possible within the time prescribed in the regulations for the settlement of the type of dispute in question.

...

281.(1) If mediation fails, the insured person may bring a proceeding in a court of competent jurisdiction or may refer the matter to an arbitrator.

(2) No person may bring a proceeding in any court or refer a matter to arbitration unless mediation has first been sought and has failed.

(3) Subject to subsection (4), if mediation fails, the insurer shall pay no-fault benefits in accordance with the last offer of settlement that it had made before the failure until otherwise agreed by the parties or until otherwise ordered by a court, an arbitrator or the Director.

(4) If a dispute involves a no-fault benefit that the insurer is required to pay under subsection 268(8) and the insured has not commenced a proceeding in a court or an arbitration proceeding within forty-five days after the day mediation failed, the insurer shall pay the insured in accordance with the last offer made by the insurer before the failure until otherwise agreed by the parties or until otherwise ordered by a court, an arbitrator or the Director.

(5) A proceeding in a court or an arbitration proceeding in respect of no-fault benefits must be commenced within two years after the insurer's refusal to pay the benefit claimed or within such longer period as may be provided in the No-Fault Benefits Schedule.

282.(1) An insured person seeking arbitration under this section shall file an application for the appointment of an arbitrator with the Commission.

(2) The Director shall ensure that an arbitrator is appointed promptly.

(3) The arbitrator shall determine all issues in dispute, whether the issues are raised by the insured person or the insurer.

...

(10) If the arbitrator finds that an insurer has unreasonably withheld or delayed payments, the arbitrator, in addition to awarding the benefits and interest to which an insured person is entitled under the Statutory Accident Benefits Schedule, shall award a lump sum of up to 50 per cent of the amount to which the person was entitled at the time of the award together with interest on all amounts then owing to the insured (including unpaid interest) at the rate of 2 per cent per month, compounded monthly, from the time the benefits first became payable under the Schedule.

...

(16) The Arbitrations Act does not apply to arbitrations under this section.

283.(1) A party to an arbitration under section 282 may appeal the order of the arbitrator to the Director.

* * * * *

Corrigendum
Released: January 9 & April 19, 2002

January 9, 2002

Please note that a correction has been made on page 6, para. 17, 4th line where "insured's bad faith" has been corrected to read "insurer's bad faith".

April 19, 2002

Please note in para 6 the word "increase" should be corrected to read "decrease".

cp/e/nc/qlhcc/qlmjb/qlhjk/qlaxr

1 For accidents between June 22, 1990 and December 31, 1993.

2 R.R.O. 1990, Reg. 672 of the Insurance Act, R.S.O. 1990, c. I.8 as amended.

3 Appeal heard and reserved by the Supreme Court of Canada on December 14, 2000; decision pending.

4 S. 282.(10) If the arbitrator finds that an insurer has unreasonably withheld or delayed payments, the arbitrator, in addition to awarding the benefits and interest to which an insured person is entitled under the Statutory Benefits Schedule, shall award a lump sum of up to 50 per cent of the amount to which the person was entitled at the time of the award together with interest on all amounts then owing to the insured (including unpaid interest) at the rate of 2 per cent per month, compounded monthly, from the time the benefits first became payable under the Schedule.

5 S. 281(5): A proceeding in a court or an arbitration proceeding in respect of no-fault benefits must be commenced within two years after the insurer's refusal to pay the benefit claimed or within such longer period as may be provided in the No-Fault Benefits Schedule. 1990, c. 2, s. 65, part.

# Tab 20

*Indexed as:*

**R. v. Clark**

**Between**
**Her Majesty the Queen, appellant, and**
**Patrick David Clark, respondent**

[2000] A.J. No. 1099

2000 ABCA 246

[2000] 11 W.W.R. 595

84 Alta. L.R. (3d) 321

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148 C.C.C. (3d) 132

7 M.V.R. (4th) 34

47 W.C.B. (2d) 412

Docket: 9903-0459-A

Alberta Court of Appeal
Edmonton, Alberta

**Picard, Berger and Wittmann JJ.A.**

Heard: April 6, 2000.
Judgment: filed September 15, 2000.

(78 paras.)

On appeal from the judgment of Binder J. Sitting on Appeal from the Alberta Court of Queen's Bench. Dated the 19th day of October, 1999.

**Counsel:**

J. Watson, Q.C., for the appellant.
D. Vigen, for the respondent.

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REASONS FOR JUDGMENT RESERVED

Reasons for judgment were delivered by Picard J.A. Separate concurring reasons were delivered by Berger J.A. (para. 18). Separate dissenting reasons were delivered by Wittmann J.A. (para. 30).

**1** PICARD J.A.:-- I have had the opportunity to read the reasons of Mr. Justice Wittmann. With respect, I find I must come to a different conclusion. I do not agree that it was Parliament's intention to exclude a disqualification under s. 17 of the Motor Vehicle Administration Act, R.S.A. 1980, c. M-22 (the "M.V.A.A.") from s. 259(4) of the Criminal Code. Moreover, there is a sufficient legal nexus between the Respondent's original conviction for impaired driving and his continuing disqualified status to justify a criminal conviction.

**2** Justice Wittmann has set out the facts and the legislation. I will not repeat them.

**3** As Wittmann J.A. aptly stated, this appeal is about the statutory construction of the word "disqualified" in s. 259(4) of the Code and specifically, whether it was the intention of Parliament that the criminal sanctions in that section for driving while disqualified apply to a continuing disqualification under s. 17 of the M.V.A.A. To that end, it must be determined whether such a continuing disqualification is a disqualification "in respect of a conviction" for the purposes of s. 259(5) of the Code.

**4** The Crown submits that Parliament envisioned legal restrictions outside of an initial suspension. As a result, it was intended that continuing disqualifications under provisions like s. 17 of the M.V.A.A., where the conditions for reinstatement are designed to force disqualified drivers to prove that they have improved their driving skills or attitudes, fall within the ambit of a disqualification or other legal restriction in s. 259 of the Code. I agree that this was the intention of Parliament. The plain and ordinary meaning of the phrase "a disqualification or any other form of legal restriction of the right or privilege to operate a motor vehicle" in defining "disqualification" in s. 259(5)(b) of the Code supports this interpretation. The definition seems to be designed to ensure that the section provides broad coverage of all the provincial consequences with respect to a restriction or disqualification from driving privileges flowing out of a Code offence.

**5** The decision of the lower courts in this case to separate the disqualifications in the M.V.A.A. under s. 109 (the original mandatory suspension for impaired driving) and s. 17 (the continuing suspension conditional on the requisite steps being taken by the offender) essentially divides the disqualification into two constituent parts. In effect, the legal status of the offender with respect to driving is changed from prohibited to merely unlicenced. With respect, this does not accord with the language of the M.V.A.A. itself. Section 17 provides that until the requisite steps are taken, a person's licence "remains suspended notwithstanding that the period of suspension has expired," and that a "disqualification remains in effect, notwithstanding that the period of disqualification has expired." In other words, the legal status of the person with respect to their ability to legally operate a motor vehicle remains unchanged.

**6** The real crux of this case lies in the proper role of the phrase "in respect of a conviction" in s. 259(5)(b) of the Code, for it is this phrase which not only in part repaired the finding of unconstitutionality of this provision's predecessor in R. v. Boggs, [1981] 1 S.C.R. 49, but which also provides the necessary legal nexus in this case. A provincial disqualification of a licence does not fall within the meaning of disqualification under the Criminal Code, unless it is "in respect of a conviction" of a designated offence. In essence, the connection to the original offence under the Code becomes an element of the offence under s. 259(4). If the original suspension is a result of a designated Code provision, then the offence is made out (provided that all of the other elements are proven); if not, then there can be no conviction.

**7** It should be noted that courts have given a wide interpretation to the phrase "in respect of" in various contexts, taking it to mean a broad connection or relationship between two subject matters: Nowegijick v. The Queen, [1983] 1 S.C.R. 29, Trustees Executors & Agency Co. Ltd. v. Reilly, [1941] V.L.R. 110 (Victoria S.C., Aust.). In order to fully give effect to Parliament's intention, a similarly broad interpretation of "in respect of a conviction" must be given in s. 259 of the Code.

**8** The Respondent argues, and the lower courts agreed, that a continuing disqualification under s. 17 of the M.V.A.A. is a result, not of the original Code offence, but rather of the offender's failure to take the requisite administrative steps, and therefore the necessary legal nexus is lost. The argument is that because s. 17 also applies to disqualifications unrelated to offences under the Code, and that because some of the requirements in the section are administrative in nature, a continuing disqualification's link to the original offence is severed so that it can no longer be considered "in respect of" a Code conviction. I do not agree.

**9** Rather than severing the link to the original offence, the requirements in s. 17 augment that connection both by highlighting the seriousness of the original offence to the driver, and by ensuring that the public safety interest is served before the reissuing of a licence is permitted. A requirement to take a course respecting alcohol use or driver awareness pursuant to s. 17, for example, is directly related to an offender's original Code offence if that offence is impaired or dangerous driving, two of the designated Code offences in s. 259. Even the payment of a fee for reinstatement could be viewed as a form of rehabilitation of a person convicted under a designated Code offence.

**10** The requisite steps prescribed in s. 17 must be viewed as part of a larger process or scheme that Parliament intended to serve public safety ends relating to driving offences. This process begins with the finding of guilt for the original offence under the Code and is completed once the offender is permitted to be reinstated as a licenced driver. The requirements under s. 17 are not simply administrative steps unrelated to the original offence, but are rather the final steps in the process before full reintegration into "driving society." Driving while disqualified within that period is contrary to the process and is a serious matter, not unlike a prisoner escaping from gaol: R. v. Gaehring (1956), 20 W.W.R. 189 at 191. The final steps before re-licencing is permitted are the final consequences of the original Code offence.

**11** Section 17 of the M.V.A.A., of course, has a wider application than simply to Code offences. It also applies to suspensions and disqualifications arising by an order or judgement made under any other Provincial Act. It was argued that this creates the possibility that a person could be criminally convicted under s. 259(4) of the Code, for example, for failing to satisfy a civil judgment. The answer is that the requisite element of s. 259(5)(b) that the disqualification be "in respect of a conviction" of a designated offence would not be made out in such a case.

**12** The Supreme Court, in R. v. Boggs, supra addressed the problem associated with the previous version of this legislation which failed to make a distinction between disqualifications arising out of a Code offence, and one arising out of a provincial statute (at 66):

> This difficulty was recognized by Turcotte D.C.J. in R. v. Gaehring (1956), 20 W.W.R. 189 at pp. 191-2 (decided when subs. (1) was still in s. 238) where he observed that driving during the period of suspension of licence ordered by a Court as part of the punishment for an offence against a Code provision or a provincial statute was a serious matter and "amounts to a contempt of the decision of the Court." Later in the judgment the Judge observed:
>
> > On the other hand, if it had been proved before me that this was a suspension as a result of a failure to provide proof of financial responsibility, perhaps I would have taken a different view of the matter. (at p. 192)
>
> Unfortunately, the Code makes no such distinction, and as a practical matter, the trial Judge will not always be able to discern the type of conduct which underlay the provincial suspension.

**13** The new Code provision (s. 259) enacted in response to Boggs now makes this distinction, and also addresses the practical problem the Court highlighted. Where the type of conduct underlying the provincial suspension is not discernable, a conviction under s. 259(4) could not be supported because an essential element of the offence would be left unproven.

**14** There may be rare instances where disqualifications for criminal reasons and disqualifications for civil reasons overlap. One example is where a person has been disqualified from driving as a result of a conviction for impaired driving, and is simultaneously disqualified from driving as a result of non-satisfaction of a civil judgment against him for injuries caused by that impaired driving. It is possible that criminal charges under s. 259(4) of the Code could arise in such a scenario. However, whether the suspension is "in respect of a conviction" in that case is an element of the offence that must be proven. Even where the possibility of overlap exists, however, there could still remain a connection to the original offence sufficient to justify consequences under s. 259(4) of the Code.

**15** In any event, this problem does not arise in this case. The Respondent's disqualification arose as a result of a conviction under s. 253(b) of the Code (operating a vehicle with a blood alcohol level exceeding eighty milligrams per one hundred millilitres of blood) [A.B. 2]. The agreed facts at the Provincial Court trial admitted a "factual nexus" between the Code offence and the disqualification the Respondent was under [A.B. 31]. There is no indication that the disqualification was in place for any other reason than the original Code offence.

**16** Where a person has committed a Code offence designated in s. 259, Parliament intended that there be consequences with respect to the driving privileges of the offender. A continuing provincial disqualification under s. 17 of the M.V.A.A., falls within those intended consequences and is therefore within the meaning of "in respect of a conviction". The reinstatement requirements are a direct result of the criminal conviction and are consistent with Parliament's overall scheme to respond to serious driving offences. There is a legal nexus.

**17** Therefore, I find that for the purpose of s. 259(5)(b) of the Code, a continuing disqualification under s. 17 of the M.V.A.A. can constitute a disqualification "in respect of a conviction", and does so in this case. The blanket removal of s. 17 from the ambit of s. 259 of the Code by the Provincial Court and the Court of Queen's Bench constituted an error of law insofar as it did not adequately give effect to the intention of Parliament. I would therefore allow the Crown's appeal, substitute a conviction for the acquittal and remit the matter to the trial Court for sentencing.

PICARD J.A.

The following is the judgment of:

**18** BERGER J.A. (concurring):-- The issue in this appeal is whether an "extended" disqualification pursuant to s. 17 of the Motor Vehicle Administration Act R.S.A. 1980, c.M-22 ("M.V.A.A.") satisfies the definition of "disqualification" for the purposes of s. 259(4) of the Criminal Code.

**19** Both the provincial court trial judge and the summary conviction appeal judge answered that question in the negative. On the facts of this case, I hold otherwise, allow the Crown appeal and direct the entry of a conviction.

**20** Following his impaired driving conviction, the Respondent was prohibited from driving for three months by virtue of s. 259(1)(a) of the Criminal Code. This period of prohibition was concurrent with the one year suspension imposed pursuant to s. 109 of the M.V.A.A.

**21** Section 17(1) of the M.V.A.A. provides for an "extended" disqualification beyond the period of one year set out in s. 109. Section 17(1) reads as follows:

> "17(1) When, under this Act or by any order or judgment made under this or any other Act,
>
> (a) a person's operator's licence is suspended, that licence remains suspended, notwithstanding that the period of suspension has expired, or
> (b) a person is disqualified from holding an operator's licence, that disqualification remains in effect, notwithstanding that the period of disqualification has expired,
>
> until that person does one or more of the following as required by the Minister:
>
> (c) passes a physical examination that indicates that the person is, to the satisfaction of the Minister, physically competent to drive a motor vehicle without endangering the safety of the general public;
> (d) completes a course respecting alcohol or drug abuse, driver training, driver competence, driver awareness or motor vehicle operation as directed by the Minister;
> (e) demonstrates, to the satisfaction of the Minister, by examination or otherwise, that the person is competent to drive a motor vehicle without endangering the safety of the general public.
>
> . . .

(5) This section applies to, but is not limited to, suspension by or pursuant to section 106, 109 or 111, or by accumulation of demerit points, notwithstanding that the period of suspension has expired."

**22** In R. v. Boggs (1981), 58 C.C.C. (2d) 7 (S.C.C.) the Court held that it was not open to Parliament in the exercise of its criminal law power "to attach penal consequences, by means of a Criminal Code provision such as s. 238(3), to a breach of an order made administratively or judicially under a valid provincial statute without any necessary relationship to the conduct that led to such order." [Emphasis added]

**23** The relevant inquiry is to ascertain whether a disqualification results from a provincial administrative action in response to the commission of a Criminal Code offence or whether it results from a purely provincial administrative violation. The underlying foundation or trigger for the disqualification governs.

**24** The learned summary conviction appeal judge held that: "An individual who drives a motor vehicle following expiry of the mandatory periods of disqualification under the Code and provincial legislation without having first complied with the licence reinstatement requirements is essentially in the same position as any other driver found driving a motor vehicle without a valid driver's license." I respectfully disagree. It is true that, having regard to the wording of s. 17(5), a continued disqualification under s. 17(1) may result from a conviction from driving a vehicle which is uninsured (s. 71 of the M.V.A.A.). But those are not the facts of this case. It is also true that a continued disqualification may result from an individual's failure to satisfy a judgment for damages arising out of a motor vehicle accident (s. 62 of the M.V.A.A.). Those are also not the facts of this case.

**25** Indeed, this latter scenario was specifically addressed by the Supreme Court of Canada in R. v. Boggs, supra. Estey, J. reasoned as follows (at p. 14):

> "It is obvious that a suspension of an owner's licence for the non-payment of a judgment arising out of the driving of an authorized driver, or suspension or revocation by reason of the non-payment of a fuel oil bill relating to domestic heating oil, have no relationship in practice or in theory to the owner's ability to drive and hence to public safety on the highways of the nation."
>
> [Emphasis added]

**26** He added at p. 16:

> "It is to be observed at once that here we have a situation wherein the Province does not seek to subject the citizen to a quasi-penal punishment in the sense that the fine or imprisonment or other disadvantage is scaled to the nature of the offence, but rather, at least in the case where administrative action is taken in response to the non-payment of a provincial tax or fee under a provincial regulatory scheme, the imposition of the suspension is directed towards compelling payment of the fee rather than punishing an offence."
>
> [Emphasis added]

**27** The language of the enactment and the pronouncements of the Supreme Court of Canada in R. v. Boggs, supra, establish clearly and unequivocally that a conviction for driving while disqualified contrary to s. 259(4) of the Criminal Code will be sustained if:

1. there is an underlying Criminal Code conviction that triggers the disqualification.
2. there is a "necessary relationship between the administrative disqualification and the conduct that led to such [disqualification]."
3. there is a relationship in practice or in theory (or in both) between the provincial administrative requirements and the driver's ability to drive and "hence to public safety on the highways of the nation."
4. the administrative action order or regulation is not in response to the non-payment of a provincial tax or made under a provincial regulatory scheme.

**28** In my opinion, all of the conditions precedent are made out in the case at bar. The Crown proved the underlying Criminal Code offence. It was acknowledged that following the one year period of suspension the Respondent failed to have his licence reinstated. But no evidence was called by the Respondent as to the reason for his inaction. The Court is invited to speculate that the Respondent's only failing may have been a failure to pay a fee. The Court is also urged to consider that because suspensions for non-criminal related matters could give rise to a prosecution pursuant to s. 259(4) of the Criminal Code, the conviction of this Respondent cannot stand. But, as explained supra, those are not the facts of this case. It was certainly open to the Respondent to adduce evidence that he was now a safe driver and had satisfied the conditions set out in s. 17(1)(c), (d) and (e) of the M.V.A.A. This he chose not to do. Instead, his trial posture, reiterated on appeal, was that purely administrative impediments, wholly unconnected to his underlying conviction for impaired driving, denied him a licence. Speculative defences carry with them a certain risk. The risk is that the underlying facts may not support the speculation. Nor can it be expected of the Crown to negative facts which are uniquely within the knowledge of the Respondent.

**29** For these reasons, I would allow the Crown's appeal, substitute a conviction and remit the matter to the trial Court for sentencing.

**29A** Counsel will note that this judgment is styled "Reasons for Judgment Reserved". The label "Reserved" no longer has the significance it once had. The Court's policy set out in Hutterian Brethren Church of Starland v. Starland No. 47 (Municipal District), (1993) 9 Alta.L.R. (3d) 1, at 15 and R. v. Bonneteau (1995), 24 Alta.L.R. (3d) 153, at 158 was abolished on September 1, 1999.

**29B** The effect of the new policy, which still permits circulation of draft reasons to members of the Court off the panel (for comment only), was stated as follows by Hetherington, J.A. in R. v. Fash (cited as R. v. D.M.F.) [1999] A.J. No. 1086:

> "In the past this court has said that, so far as statements of law or principle are concerned, a reserved judgment which is not a dissenting judgment sets out views accepted by a majority of the members of the court. (See Hutterian Brethren Church of Starland v. Starland No. 47 (Municipal District) (1993), 9 Alta. L.R. (3d) 1, at 15, and R. v. Bonneteau (1994), 24 Alta. L.R. (3d) 153, at 158.) However, this is no longer the case. The practices of the court have changed.

> Now so far as statements of law or principle are concerned, a reserved judgment which is not a dissenting judgment sets out the views of a majority of the panel which heard the appeal. It can not be inferred that a majority of the members of the court share those views."

BERGER J.A.

The following is the judgment of:

WITTMANN J.A. (dissenting):--

INTRODUCTION

**30** This appeal concerns the interpretation of "disqualification" under of s. 259(5) of the Criminal Code, R.S.C. 1985, Chap. C-46 (Code).

FACTS

**31** The respondent Clark was convicted on March 14, 1994 of operating a motor vehicle with a blood alcohol content in excess of the legal limit, contrary to s. 253(b) of the Code. A three month mandatory driving prohibition was imposed on Clark by the trial judge by virtue of s. 259(1)(a) of the Code. In addition, he became disqualified from holding a licence to drive and his licence was suspended for one year under s. 109(1) of the Motor Vehicle Administration Act R.S.A. 1980, c.M-22 ("MVAA"). Following the one year disqualification and suspension, s. 17 of the MVAA required Clark to meet certain requirements before his licence could be reinstated, failing which Clark remained disqualified and his licence suspended. Clark failed to meet these requirements. Subsequently, on December 24, 1997, Clark was found operating a motor vehicle and was charged under s. 259(4) of the Criminal Code with operating a vehicle while disqualified from doing so.

DECISIONS BELOW

**32** It was held by both the provincial court trial judge and the summary conviction appeal judge that the extension of the provincial disqualification under s. 17 of the MVAA is not "disqualification" for the purposes of s. 259(4) of the Criminal Code. Therefore, Clark was not, at the material time, driving while "disqualified" and was acquitted of the charge.

RELEVANT LEGISLATION

**33** Criminal Code, R.S.C. 1985, Chap. C-46.

> 259(1) Where an offender is convicted of an offence committed under section 253 or 254 or discharged under section 730 of an offence committed under section 253 and, at the time the offence was committed or, in the case of an offence committed under section 254, within the two hours preceding that time, was operating or had the care or control of a motor vehicle, vessel, aircraft or railway equipment or was assisting in the operation of an aircraft or of railway equipment, the court that sentences the offender shall, in addition to any other punishment that may be imposed for that offence, make an order prohibiting the offender from operating a motor vehicle on any street, road, highway or other public place, or from operating a vessel, aircraft or railway equipment, as the case may be.

(a) for a first offence, during a period of not more than three years plus any period to which the offender is sentenced to imprisonment, and not less than three months;

. . .

259(4) Everyone who operates a motor vehicle, vessel, aircraft or railway equipment in Canada while disqualified from doing so

(a) is guilty of an indictable offence and liable to imprisonment for a term not exceeding two years; or
(b) is guilty of an offence punishable on summary conviction.

259(5) For the purposes of this section, "disqualification" means

(a) a prohibition from operating a motor vehicle, vessel, aircraft or railway equipment ordered pursuant to subsection (1) or (2); or
(b) a disqualification or any other form of legal restriction of the right or privilege to operate a motor vehicle, vessel or aircraft imposed
(i) in the case of a motor vehicle, under the law of a province . . .

in respect of a conviction or discharge under section 730 of any offence referred to in subsection (1) or (2).

Motor Vehicle Administration Act, R.S.A. 1980, c. M-22

109(1) When a person is found guilty under section 253 or 254 of the Criminal Code (Canada) anywhere in Canada,

(a) that person thereupon becomes disqualified from holding an operator's licence, and
(b) any operator's licence held by that person thereupon becomes suspended,

for a period of 1 year from the date of the finding of guilt.

17(1) When, under this Act or by any order or judgment made under this or any other Act,

(a) a person's operator's licence is suspended, that licence remains suspended, notwithstanding that the period of suspension has expired, or
(b) a person is disqualified from holding an operator's licence, that disqualification remains in effect, notwithstanding that the period of disqualification has expired,

until that person does one or more of the following as required by the Minister:

(c) passes a physical examination that indicates that the person is, to the satisfaction of the Minister, physically competent to drive a motor vehicle without endangering the safety of the general public;
(d) completes a course respecting alcohol or drug use, driver training, driver competence, driver awareness or motor vehicle operation as directed by the Minister;
(e) demonstrates, to the satisfaction of the Minister, by examination or otherwise, that the person is competent to drive a motor vehicle without endangering the safety of the general public.

. . .

17(5) This section applies to, but is not limited to, suspension by or pursuant to section 106, 109 or 111, or by accumulation of demerit points, notwithstanding that the period of suspension has expired.

Interpretation Act, R.S.C. 1985 c. I-21

12 Every enactment is deemed remedial, and shall be given such fair and liberal construction and interpretation as best ensures the attainment of its objects.

Interpretation Act, R.S.A. 1980, c. I-7

10 An enactment shall be construed as being remedial, and shall be given the fair, large and liberal construction and interpretation that best ensures the attainment of its objects.

ISSUE

Did the lower court judges err in their interpretation of ss. 17 and 109(1) of the MVAA, and ss. 259(4) and (5) of the Code?

**34** As the summary conviction appeal judge noted, the issue is to be determined on the basis of statutory construction: [A.B. 5]. The issue before this Court, and the courts below, is whether Clark was "disqualified" from operating a motor vehicle for the purposes of s. 259(4) of the Code. Clark was found operating a motor vehicle in December of 1997, almost three years after the expiration of his mandatory driving prohibition under s. 259(1)(a) of the Code and the expiration of a one year provincial prohibition on holding a license. The question this Court must decide is whether it was the intention of Parliament that even after the expiration of a mandatory disqualification period under s. 259(1) of the Code and the expiration of the provincial disqualification period set out in the MVAA, an accused remains disqualified "in respect of a conviction" for the purposes of s. 259(5).

ANALYSIS

**35** Section 259 of the Code, as it currently stands, was amended by Parliament after a constitutional challenge in the early 1980s. In R. v. Boggs, [1981] 1 S.C.R. 49, the accused questioned s. 238 of the Code [now s. 259] which allowed the federal government to add a criminal consequence to driving with a provincial licence suspension. On August 5, 1977, Boggs was convicted of impaired driving and for refusing to take a breath test. Consequently, his driver's licence was automatically suspended pursuant to the Highway Traffic Act, R.S.O. 1970, c. 202. Two years later, on August 11, 1979, Boggs was charged under s. 238 of the Code with driving while disqualified by reason of suspension of his licence. At that time, s. 238 read as follows:

> 238(3) Every one who drives a motor vehicle in Canada while he is disqualified or prohibited from driving a motor vehicle by reason of the legal suspension or cancellation, in any province, of his permit or licence or of his right to secure a permit or licence to drive a motor vehicle in that province is guilty of
>
> (a) an indictable offence and is liable to imprisonment for two years; or
> (b) an offence punishable on summary conviction.

At trial, 1 M.V.R. 78, Boggs challenged the constitutionality of s. 238 arguing that it was ultra vires the jurisdiction of the federal government to legislate criminal consequences for breach of a provincial statute. The Ontario Court of Appeal, [1979] O.J. No. 1796, upheld the decision of the trial judge and dismissed the accused's appeal of his conviction.

**36** Estey, J. framed the issue in Boggs at p.60 as follows:

> . . . can Parliament validly exercise its criminal power under s. 91(27) by attaching penal consequences by means of a Criminal Code provision (here s. 238(3)) to a breach of an order made administratively or judicially under a valid provincial statute, without any necessary relationship to the conduct that led to such an order?

Estey, J. carefully reviewed the provincial legislation at issue and noted that a breach of s. 238(3) could stem from two possible sources: criminal offences or administrative offences. Therefore, the effect of s. 238 was twofold: if a suspension resulted from a provincial administrative action in response to a criminal offence under the Code, then s. 238 operated to create a new offence under the Code in addition to the provincial offence of driving while disqualified. If, however, suspension or cancellation resulted from a provincial administrative offence, s. 238 had the effect of creating a new punishment under the Code.

**37** Estey, J. found that the effect of a lack of distinction between the offences with criminal or administrative roots meant that Parliament could impose criminal sanctions for breaches of administrative offences which had no nexus to the criminal law or to the community interest behind s. 238, that of safety on the highway. Because the section could not be severed so as to preserve the constitutionally sound section of the provision, the Court struck down s. 238 and the accused's conviction was set aside.

**38** In response to Boggs, supra, Parliament re-drafted s. 238 and amended the Code to restrict the disqualified driver offence, where the suspension arises from provincial offences, to instances where an accused had been prohibited, disqualified from driving, or restricted "in respect of a conviction" for specific Code offences.

**39** However, the issue before this Court appears to fall beyond the ambit of Boggs, supra. The fact situation here is unique. The mandatory Code prohibition imposed against Clark expired well before December 24, 1997, the day the Police discovered Clark driving, and so too had the one year companion provincial disqualification and suspension of Clark's licence. Clark had not obtained his licence as required under s. 17 of the MVAA. It is not clear that this was the same situation in Boggs, supra. In Boggs, supra, Estey, J. notes that Boggs was convicted of driving while impaired and for failing to take a breath test in August of 1977. His second charge, for driving while disqualified, was laid in August of 1979. The judgment does not indicate that whether his licence suspension, provincial or otherwise, was in effect at the time of the second arrest. The suspension periods under s. 20(1) of the Highway Traffic Act, R.S.O. 1970, c. 202 [rep. & sub. 1977, c. 54, s. 2; am. 1978, c. 90, s. 2], ranged from three months to three years depending upon the number of previous convictions of the accused. Additionally, the Highway Traffic Act, supra, did not contain any specific provisions addressing the steps an individual must take at the expiration of the suspension and disqualification to have his or her licence reinstated.

**40** It is possible that the provincial suspension period imposed on Boggs had expired when he was charged with driving while disqualified; although, there is not enough detail in the written decision of Estey, J. to state this with absolute certainty. However, the applicability of the fact situation in Boggs, supra, to this appeal is really secondary to the constitutional comments made by the Court. Not only are the facts in Boggs, supra, unclear, but the Code has been amended since that decision to overcome any jurisdictional hurdles. This Court must interpret the new legislation in light of the constitutional comments made in Boggs, supra.

**41** It should be noted that the parties have not directly challenged the constitutionality of s. 259. Rather, they have confined the issue to an interpretation of the meaning of "disqualification" in s. 259. I therefore proceed on the basis urged upon us by both counsel - to decide on the basis of statutory interpretation only, and express no opinion on any constitutional issue.

**42** The Crown makes three main submissions with respect to its position on Clark's acquittal. First, it claims the summary conviction appeal judge erred in applying the strict construction rule to an interpretation of the Code. The effect of this application was to divide the driving disqualification into two constituent parts: one under s. 109 of the MVAA and one under s. 17 of the MVAA. It is the position of the Crown that the language of the MVAA does not support this interpretation. Second, the Crown contends that the intention of Parliament in enacting this legislation was to fix the defect revealed in Boggs, supra, and to allow federal legislation on disqualified drivers to co-exist constitutionally with provincial legislation. It is argued this intention should have been considered by the summary conviction appeal judge when he made his decision. Third, Parliament was within its powers to incorporate provincial driver disqualification by reference in the Code and it is not, as was assumed by the summary conviction appeal court judge, beyond the Legislature's powers.

(a) What rule of statutory construction is to be applied by this Court when interpreting s. 259(4) and (5) of the Code?

**43** The Crown contends that, in interpreting s. 259(4) and (5) of the Code, the summary conviction appeal judge, after considering the penal nature of the statute, erred in employing a strict rule of construction: [A.B. 5 at para. 16-17]. In applying this rule, it is the Crown's position that the judge overlooked authority against the employment of such a rule. Section 12 of the federal Interpretation

Act, supra, provides that enactments are to be given "fair and liberal construction" so as to "ensure the attainment of its objects". Furthermore, Cory, J. states in R. v. Hasselwander, [1993] 2 S.C.R. 398 at 412-413, that the rule of strict construction is to be used only when neutral interpretation leaves reasonable doubt as to the meaning of the statute. Therefore, the intention of Parliament must be determined in order to interpret the legislation within the scope of its goals, even in the case of penal statutes. The Crown submits that because the statutory provisions are not ambiguous in this case, they should be construed to include the continued suspension and disqualification.

**44** Clark, on the other hand, submits that the rule of strict construction was properly applied by the summary conviction appeal judge. In support of this position, Clark relies on Hasselwander, supra, and Marcotte v. Canada (A.G.), [1976] 1 S.C.R. 108. Dickson, J., writing for the Court in Marcotte, supra, states in obiter that where ambiguities are found in penal statutes, they are to be interpreted in favor of the person against whom it is sought to be enforced: see also Ruth Sullivan, Driedger on the Construction of Statutes, 3rd ed. (Toronto: Butterworths, 1994) at 357.

**45** In recent years, this rule has attracted critical attention largely because it is difficult to reconcile with federal and provincial Interpretation Acts that deem legislation to be remedial and to require a liberal and purposive approach to interpretation. The strict construction rule has been rejected by the Supreme Court of Canada on many occasions: see for example R. v. Ogg-Moss, [1984] 2 S.C.R. 173 at 183; R. v. Pare, [1987] 2 S.C.R. 618 at 329-33; R. v. Lightfoot, [1981] 1 S.C.R. 566 at 575; R. v. B.(G.)(No. 1), [1990] 2 S.C.R. 3; Sullivan, Driedger on the Construction of Statutes, supra, at 360-61. In Hasselwander, supra, Cory, J. tried to strike a balance between the rights of the accused and the strict construction rule, and the interests of society in legislative interpretation. Cory, J. stated that, even where ambiguities appear in penal statutes, a neutral interpretation should be employed by the courts and the real intention of the legislature should be considered in determining the meaning of the legislation.

**46** Sullivan, in Driedger on the Construction of Statutes, supra, questions whether the strict construction rule should be treated by the courts as a test of last resort. She states that Cory, J. expresses two distinct ideas in Hasselwander, supra: strict construction as a final option and strict construction as one factor among many. Sullivan favours the latter approach. She writes at 362: "the values of fair notice and liberty of the subject are an important part of the legal context in which legislation is drafted, read and applied; the values are relevant, though not necessarily controlling, in every case."

**47** While the summary conviction appeal judge referred to the strict construction rule in his judgment, it was not the only aid he resorted to with regard to the interpretation of the statute. In his decision, he refers to other rules governing statutory interpretation including the following: a consideration of the grammatical and ordinary meaning of the words in the context of the statute; a determination of the purpose of the statute; the ability of an interpreting judge to read in words or to ignore words to prevent unintelligible, absurd, or unreasonable interpretations; and, the ability of an interpreting judge to resort to aids to construction and presumptions. Only then did he note that the strict construction rule was a "further rule of statutory construction.": [A.B. 5, para. 15-16].

**48** It appears that the Crown is incorrect in claiming that the summary conviction appeal judge relied on the strict construction rule. While he did not cite the authorities that modify the rule, it appears that he considered other elements in interpreting s. 259 of the Code, such as the ordinary meaning of the statute and Parliament's intention. Therefore, it appears that the summary conviction

appeal judge did not err in applying a strict construction rule to the interpretation of s. 259(4) and (5) of the Code, because he neither isolated it, nor applied it in isolation.

(b) What was the intention of Parliament in enacting s. 259 of the Code?

**49** As noted above, the previous version of the Code provision was struck down by the Supreme Court of Canada in Boggs, supra, because it did not distinguish between provincial disqualification in response to convictions under the Code, and disqualification imposed for breach of administrative provincial offences. The legislation was then re-drafted and a new offence was introduced by Minister of Justice, John Crosbie, to Parliament. In a debate on the subject, Mr. Crosbie commented that the new legislation was in response to the Boggs, supra. He stated:

> In addition, we are proposing that a new offence of driving while disqualified be enacted. We know that dozens of cases of people whose licences have been lifted by the provincial authorities but who drive and are picked up again. We will create a new offence of driving while disqualified. We expect that the wording of the new offence will rectify the problems that were presented to the Supreme Court of Canada decision in the case of Boggs versus The Queen, where the Supreme Court ruled that the current offence of driving while disqualified was ultra vires, "beyond our power", because the criminal sanction could be imposed for the violation of a provincial licence suspension pursuant to a conviction for a non-criminal highway traffic offence.
>
> In order to get around that, the new offence will apply only to violations of a new judicial order of prohibition which is contained in this legislation, upon which I will expand later, and violations of provincial licence suspensions that are imposed pursuant to a criminal driving offence. That will get around this difficulty that the Supreme Court of Canada found.
>
> [House of Commons Debates, December 20th, 1984 at p.1385.]

It was clear from this statement that the intention of the then Minister of Justice was to restrict the offence of disqualified driving to occasions where an accused's licence had been suspended under provincial law pursuant to a conviction under the Code.

**50** I am mindful of the authority pertaining to the exclusion of legislative debates as a valid extrinsic aid in interpreting a statute.

**51** In R. v. Morgentaler [1993] 3 S.C.R. 463, Sopinka, J. stated at 484:

> The former exclusionary rule regarding evidence of legislative history has gradually been relaxed . . ., but until recently the courts have balked at admitting evidence of legislative debates and speeches . . . The main criticism of such evidence has been that it cannot represent the "intent" of the legislature, an incorporeal body, but that is equally true of other forms of legislative history. Provided that the court remains mindful of the limited reliability and weight of Hansard evidence, it should admitted as relevant to both the background and purpose of the legislation.

**52** This Court in Tschritter v. Alberta (Children's Guardian for Alberta) (1989), 57 D.L.R. (4th) 579 (Alta. C.A.) referred to considering legislative debate as assisting a determination of legislative intent. Hetherington, J.A. wrote at p.587:

> It is clear, therefore, that at least when it is alleged that a statute is inconsistent with the Charter and therefore of no force or effect, a court is entitled to consider legislative debate in an effort to determine the purpose or intention of the legislature in enacting the statute. It is an acceptable aid in the interpretation of the statute. Is there any reason for forbidding such a practice in other cases? In my view there is not. If legislative debate is an acceptable aid in interpreting a statute when its constitutionality is in issue, why should it not be an acceptable aid in the interpretation of a statute in other cases? I can think of no reason.
>
> . . .
>
> Statements made in the legislature are not, of course, conclusive as to the intention of the legislature. They constitute evidence to be weighed. The factors relevant to weight will vary from case to case.

**53** In Tschritter, the other two member of this Court, although agreeing in the result, expressly declined to comment on the ability of the Court to consider Hansard as an extrinsic aid.

**54** More recently, in R. v. Heywood (1995), 94 C.C.C. (3d) 481 (S.C.C.), the word "loiter" in s. 179(1)(b) of the Code was in issue. Cory, J., speaking for the majority, after indicating that the admissibility of legislative debates to determine legislative intent in interpreting statutes is doubtful, went on to state that legislative history may be admissible for the more general purpose of showing the mischief Parliament was attempting to remedy with the legislation. In addition, he stated more flexible rules allowed the admission of legislative history to appreciate the constitutional validity of the provisions at issue in constitutional cases. He concluded at p.513:

> Despite the apparent merits of the rule that legislative history is inadmissible to determine legislative intent in statutory construction, this court has on occasion made use of such materials for this very purpose: see R. v. Vasil (1981), 58 C.C.C. (2d) 97 at pp. 110-1, 121 D.L.R. (3d) 41 at p.55, [1981] 1 S.C.R. 469; Paul v. The Queen (1982), 67 C.C.C (2d) 97, 138 D.L.R. (3d) 455, [1982] 1 S.C.R. 621.

**55** Thus, legislative debate may be considered as a factor in the interpretation of the impugned legislation, but I prefer not to call it evidence, which may denote a necessity to follow traditional rules of admissibility. For the purposes of this case, the statements of Mr. Crosby, the then Minister of Justice, are noted.

**56** The Nova Scotia Court of Appeal interpreted Parliament's legislative intention in R. v. Buchanan (1989), 46 C.C.C. (3d) 468 at 473 (N.S.C.A.). Pace, J.A., stated:

> The purpose of s. 242(4) and (5)(b)(i) is to deter by criminal sanction all drivers who have lost their driving privilege as a result of driver-related Criminal Code convictions from continuing to drive while prohibited, the over-all objective be-

> ing to keep dangerous drivers off the highways and thus reduce the danger to the public of death, injury, and property damage occasioned by their presence.

The Crown further submits, however, that this intention extends to legal restrictions outside the initial suspension imposed upon a driver. The definition of "disqualification" under s. 259(5)(b) includes "a disqualification or any other form of legal restriction" against a driver under provincial law imposed "in respect of a conviction": [emphasis added]. It is the Crown's position that this means that a driver subject to a provincial licence suspension and disqualification as a result of a Code offence will remain disqualified until such time as he or she has met the requirements for reinstatement - a form of legal restriction - under s. 17(1) of the MVAA, in spite of the fact that the suspension and disqualification time has expired pursuant to s. 109 of the MVAA.

**57** Clark recognizes that public safety and protection is an obvious and valid objective of the federal criminal law power. However, it is his position that it cannot be used to justify the inclusion of a disqualification period imposed under s. 17 of the MVAA within the meaning of s.259(5) of the Code. He advances several reasons.

**58** First, s. 17 of the MVAA is not truly concerned with a criminal law issue, that of public safety. Clark points out, in Regulations made under s. 17 of the MVAA, the payment of a reinstatement fee is required if a suspended driver wishes to be re-licensed. It may be that a suspended driver is not able to pay that fee even though he or she has completed the other requirements set out in s. 17(1). Although an alcohol awareness course (s. 17(1)(c)), or a driver's examination (s. 17(d)), might be linked to public safety, it is Clark's argument that a reinstatement fee has no relation to the issue of public safety. This is an issue related to licensing, and not public safety, and if an individual's only failing is not to pay the fee, it cannot be said that he or she is a less safe driver and warrants a criminal charge: see R. v. Slobodian, [1999] A.J. No. 1434. (Prov. Ct.) and R. v. Letki (July 6, 1998, Alta. Prov. Ct. Docket: 80187628-P1-0101).

**59** Second, Clark submits the failure to comply with s. 17 could result in criminal sanctions for a non-criminal offence. In particular, Clark makes note of s. 17(5) of the MVAA, which provides that s. 17(1) applies to, but is not limited to, suspensions pursuant to ss. 106, 109 or 111. It is his position that because these sections provide for suspensions in non-criminal as well as criminal matters, such as non-payment of civil judgments for impaired driving causing bodily harm, they could result in an individual being charged with disqualified driving if, for example, a civil judgment was not paid.

**60** Third, Clark submits that if the Crown's position is accepted, it would be possible for an individual, whose license is suspended, and who is disqualified from driving in Alberta, to be labelled a safe driver in British Columbia and obtain a driver's licence in that province. This would only be applicable where the license is suspended but the suspension time has been served and renewal has not been granted.

**61** There are two weaknesses to Clark's arguments. First, Clark's claim that a reinstatement fee removes the public safety aspect from s. 17 of the MVAA requires a very simplistic reading of the Act. The restriction on the return to the road of Code convicted drivers is in the interest of public road safety. The payment of the fee is merely one step in a series of several aimed at improving the operation skills, abilities and attitude of the convicted driver. Admittedly, fees for licensing are not limited to suspended and disqualified operators. They are required for many administrative tasks including first applications for licences ($8 to $40), renewals ($8), and duplicate licences ($10):

MVAA Regulations, s. 1. However, the renewal fee for drivers suspended and disqualified under s. 109 of the MVAA is much higher than in other instances ($140.00). It could be argued that such a significant payment is part of the rehabilitation of the offending driver.

**62** Second, Clark's argument, that the failure to pay a civil judgment arising from a criminal event could lead, if unpaid, to a criminal charge for driving while disqualified, is not clear. If an individual was convicted for driving while impaired, he or she would receive a driving prohibition and a licence suspension under the Code and the MVAA respectively. Any suspension for non-payment of a civil judgment pursuant to s. 62 MVAA, stemming from the events that led to the criminal charges, would be a separate issue and would result in a provincial suspension under the MVAA only, as opposed to s. 259 of Code. Even if a conviction was not entered, the accused could be sued in a civil action for the same events. Therefore, it could be argued that there is no connection between the criminal conviction and the civil judgment such that a s. 259 charge for driving while disqualified would result.

**63** The intention of Parliament in enacting s. 259 seems to be quite clear: the Federal Government, concerned with public road safety, responded to the direction of the Supreme Court of Canada in Boggs, supra, and extended its criminal law power to include within its jurisdiction provincial licence offences that were rooted in driving offences contained in the Code. The use of the phrase "any other form of legal restriction" in s. 259(5)(b) is broad enough to include the legal/administrative restrictions set out in s. 17(1). However, the matter does not end there. The real issue is whether a violation of s. 17 of the MVAA is "in respect of" the driving conviction under the Code.

> (c) Are the requirements of s. 17 of the MVAA "in respect of" the driving conviction under the Code?

**64** As a matter of interpretation, if the requirements of s. 17 of the MVAA are "in respect of" the driving conviction under the Code, failure to comply with the requirements of s. 17 may result in a conviction for driving while disqualified pursuant to s. 259 of the Code.

**65** The phrase "in respect of" has been considered by many courts. The thread of consistency attached to this phrase is that the words have a broad import connoting a connection or relationship between two subject matters.

**66** For example in Trustees Executors & Agency Co. Ltd. v. Reilly [1941] V.L.R. 110, Mann, C.J. stated at p.111:

> The words "in respect of" are difficult of definition, but they have the widest possible meaning of any expression intended to convey some connection or relation between the two subject-matters to which the words refer.

**67** In interpreting s. 87 of the Indian Act, R.S.C. 1970, c.I-6, Dickson, J. (as he then was) considered the phrase "in respect of any such property" in Nowegijick v. The Queen, [1983] 1 S.C.R. 29 and stated at p. 39:

> The words "in respect of" are, in my opinion, words of the widest possible scope. They import such meanings as "in relation to", "with reference to" or "in connec-

> tion with". The phrase "in respect of" is probably the widest of any expression intended to convey some connection between two related subject matters.

**68** In this Court, the phrase has been interpreted in the context of the Builders' Lien Act in Alberta Gas Ethylene Co. Ltd. v. Noyle et al., [1980] 2 W.W.R. 507 (Alta. C.A.) and Peter Hemingway Architect Ltd. and Abacus Cities Ltd. et al. (1980), 113 D.L.R. (3d) 705 (Alta. C.A.) Both cases considered the meaning of "in respect of an improvement" under s. 4(1) of the Builders' Lien Act R.S.A. 1970 c.35 which contained the phrase "upon or in respect of an improvement" referring to a person doing work or furnishing material who may claim a lien. These cases provide examples of the wider meaning of "in respect of" when used in addition to the word "upon".

**69** When reviewing and considering the previous judicial interpretation of the phrase, it is to be remembered that the phrase here is being used to connect what is in reality a deeming provision in s. 17, to the driving conviction, so that the conduct complained of is a crime in the context. The essence of the deeming provision is to define the condition of suspension or disqualification to exist when it would not otherwise, but for the provisions in the definitions in the form of restrictions in s. 17(1) of the MVAA. Thus, in my view, caution must be exercised in giving the words "in respect of" a broad and wide meaning. Even if, however, such meaning is properly attributed in the context of the interpretation of s. 259 of the Code, there must still be some necessary connection or relationship. In other words, in my view, the s. 17 disqualification must be "in respect of" the Code driving conviction in the context of the facts of this case.

**70** The Crown submits that Parliament has the ability to incorporate provincial law by reference: Coughlin v. Ontario Highway Transport Board, [1968] S.C.R. 569; R. v. Furtney (1991), 66 C.C.C. (3d) 498. However, the Supreme Court of Canada in Boggs, supra, cautioned Parliament against incorporating provincial legislation in a disqualified driving offence if it did not have a nexus or connection to the Code itself. In the head note to the decision, it is stated: "It is not open to Parliament in the exercise of its criminal law power under s. 91(27) of the British North America Act, 1867 to attach penal consequences, by means of a Code provision such as s. 238(3), to a breach of an order made administratively or judicially under a valid provincial statute without any necessary relationship to the conduct that led to such order". The issue this Court must determine is whether s. 17 continued suspension and disqualification is sufficiently connected to the Code conviction so as to be "in respect of" the Code conviction in the context of the facts of this case.

**71** The summary conviction appeal judge found that s. 17 does not have the necessary nexus. He wrote:

> [28] Section 17(5) of the M.V.A.A. indicates that the provisions of s. 17(1) apply but "are not limited" to a suspension pursuant to ss. 106, 109 and 111 of the Act or by accumulation of demerit points. Sections 106 and 111 impose a licence suspension in respect of convictions not only for various Code offences but also for offences under other Alberta statutes, municipal by-laws and federal regulations. Given the wording of s. 17(5), a continued disqualification under s. 17(1) may be imposed in relation to a suspension arising from a conviction for driving a vehicle which is uninsured (s. 71 M.V.A.A.) Or

> one which is imposed as a result of an individual's failure to satisfy a judgment for damages arising out of a motor vehicle accident (s. 62 M.V.A.A.). The latter is precisely the situation used by the Supreme Court of Canada in R. v. Boggs, supra, to illustrate why what was then 238(3) of the Code was ultra vires.
> [A.B. 8-9]

He then concluded that s. 17(5) is administrative and regulatory in nature and cannot be incorporated into the Code. Clark agrees with this conclusion. As noted above, he additionally contends that because fees are required to reinstate a suspended licence, s. 17(5) is administrative in nature.

**72** It is argued that, even though s. 17 must be met for offences that are not under the Code, in other words for purely provincial offences, there is no risk, as there was in Boggs, supra, that a driver will be convicted of a Code offence for failing to meet the requirements of s. 17. Only if the initial offence was the result of a conviction set out in s. 259(1) and (2) of the Code will a driver face a disqualified driving charge. As stated earlier, s. 259(5) defines "disqualification" as "a disqualification or any other form of legal restriction of the right or privilege to operate a motor vehicle . . . under the law of a province . . . in respect of a conviction ... of any offence referred to in subsection (1) or (2)": [emphasis added]. This provision was calculated to impose a Code offence for suspended and disqualified drivers caught driving during the provincial suspension period but after the expiry of the mandatory Code period.

**73** In my view, the disqualification loses its quality of being "in respect of" the Code conviction when the s. 109 disqualification ends and the s. 17 disqualification begins. In terms of a connection or relationship, the s. 17 disqualification is too remote so as to be "in respect of" the conviction. The disqualification under s. 17(5) in the case of Clark gives rise to a provincial, regulatory offence, not a Code offence. Many s. 17 requirements are administrative in nature and not related to the purpose of criminal law. The requirements for licence reinstatement in s. 17 arise independently of any requirement of a prior Code conviction. The relationship or connection must be substantial. That proximity is lacking here.

**74** Pursuant to s. 17, the origin of the suspension and disqualification need not arise by virtue of a Code conviction. It may arise, according to s. 17(1), "under this Act". But it may also arise "by any order or judgment made under this or any other Act". The phrase "any other Act can only refer to another Act of the Legislature of the Province of Alberta.

**75** Moreover, in s. 17(5), it is stated that s. 17 "applies to, but is not limited to, suspension by or pursuant to ss. 106, 109 or 111, or by accumulation of demerit points, notwithstanding that the period of suspension has expired".

**76** At best, the requirements of s. 17 may be triggered as the result of a s. 109 disqualification and suspension. But they also may be triggered by many other sections not only of the MVAA but also of "any other Act". Thus, the s. 17 suspension and disqualification is not "in respect of" a Code conviction. In short, the s. 109 suspension and disqualification under the MVAA is "in respect of" the Code conviction. The s. 17 suspension and disqualification is not.

CONCLUSION

**77** The proper interpretation of s. 259 of the Code in the context of s. 109 and s. 17 of the MVAA is that a s. 17 disqualification after the expiry of the period of disqualification in s. 109 does not have the necessary connection to a Code conviction pursuant to ss. 253 or 254 so as to bring itself within the meaning of "disqualifications" in s. 259(5), notwithstanding that the disqualification occurred under s. 109 of the MVAA.

**78** The appeal is therefore dismissed.

WITTMANN J.A.

cp/i/qljpn/qlhcs/qlsxs

# Tab 21

*Indexed as:*

# Johal v. Harstad (B.C.C.A.)

**Between**
**Joginder Kaur Johal, Plaintiff, (Respondent), and**
**Wayne Martin Harstad, Defendant, (Appellant)**

[1988] B.C.J. No. 240

47 D.L.R. (4th) 636

24 B.C.L.R. (2d) 61

8 A.C.W.S. (3d) 438

Vancouver Registry: CA007239

British Columbia Court of Appeal

**Seaton, Aikins and Macdonald JJ.A.**

February 12, 1988

*Limitation of actions -- Statutory extension of limitation period -- Cause of action confirmed by payment made by defendant insurer -- Statute provided that limitation period to restart on date of confirmation of cause of action -- Limitation Act, R.S.B.C. 1979, c. 236, s. 5.*

This was an appeal from an order dismissing an application to dismiss an action as barred by the Limitation Act. An action was commenced by the plaintiff on February 20, 1986 for damages arising out of an automobile accident that occurred on February 8, 1984. The defendant insurer, I.C.B.C., had made payments out on the claim to several doctors on account of medical reports filed by them. There had also been an oral acceptance of liability and several offers to settle.

HELD: The appeal was dismissed. Section 5 of the Limitation Act stated that where a person confirmed a cause of action while the limitation period was still running by a payment in respect of the cause of action, the limitation period was deemed to begin to run from the date of confirmation. The payments in question were made by I.C.B.C. on behalf of the defendant in the course of negotiating settlement of the plaintiff's claim against the defendant for damages arising out of the motor vehicle accident. The statute provided that such payments confirmed the cause of action. The action was therefore not barred.

Counsel for the Appellant: J.S. Carfra, Q.C.
Counsel for the Respondent: J.W. Horn.

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**SEATON J.A.** (for the Court, dismissing the appeal):-- This action was commenced on February 20, 1986 for damages arising out of a motor vehicle accident that occurred on February 8, 1984. The defendant applied to dismiss the action as barred by the Limitation Act, R.S.B.C. 1979, c. 236, but Hutchinson, L.J.S.C. dismissed the application. This appeal results.

The arguments focus on payments made by the Insurance Corporation of British Columbia as insurer of the defendant and on s. 5 of the Limitation Act:

> 5.(1) Where, after time has commenced to run with respect to a limitation period fixed by this Act, but before the expiration of the limitation period, a person against whom an action lies confirms the cause of action, the time during which the limitation period runs before the date of the confirmation does not count in the reckoning of the limitation period for the action by a person having the benefit of the confirmation against a person bound by the confirmation.
>
> (2) For the purposes of this section,
>
> (a) a person confirms a cause of action only if he
>
> (i) acknowledges a cause of action, right or title of another; or
> (ii) makes a payment in respect of a cause of action, right or title of another;

I have emphasized the language that is particularly important to this case.

The defendant's argument put the issue this way:

> The real issue here is whether this loss will fall on I.C.B.C. or on the solicitor who failed to issue the Plaintiff's Writ of Summons in compliance with the statutory time limitations.

That expresses the reality of this case.

The argument went on to emphasize that I.C.B.C. should be encouraged to make interim payments in the discharge of its duty as statutory insurer. I accept that, but reject the defendant's approach. The interpretation we put on s. 5 must be an interpretation applicable generally, not just to cases in which the plaintiff is represented by a solicitor and the defendant insured by I.C.B.C.

For similar reasons the facts that there had been an oral acceptance of liability and that there were several offers to settle, must be given weight only to the extent that they assist in answering the proper question: Was there a payment in respect of the cause of action?

The payments that the plaintiff says fall within s. 5(2)(a) (ii) were of $416, made on July 9, 1985, and $430, made on January 28, 1986. They were made to the plaintiff's solicitor to reimburse him for the cost of medical reports.

The first payment followed a letter from the plaintiff's solicitor in which he said:

> I enclose the following:
>
> 1) Dr. Harris' report of June 20th, 1985;
> 2) Photocopy of Dr. Harris' account.
>
> As we have paid Dr. Harris' account directly, I would appreciate receiving your draft in the amount of $416.00.
>
> Simultaneously, I am sending this report to Mrs. Johal requesting that she attend at my office next Thursday to see me and discuss the possible settlement of this action.

The statement attached to the cheque said under "REASON", "YOUR FILE ..."

The second payment followed this letter:

> I enclose the following:
>
> (1) Report of Dr. David Ellis dated November 18, 1985;
>
> (2) West Coast General Hospital letter regarding physiotherapy.
>
> As well I am enclosing the accounts for both of those reports which our office has paid directly.
>
> I would appreciate receiving your draft made payable to our firm in the amount of $430.00.

The statement said under "REASON", "REFUND OF MEDICAL REPORT FEES ON JOGINDER JOHAL ..."

The payments were not made pursuant to the no fault scheme but as liability insurer of the defendant. They were voluntary payments in the sense that the plaintiff could not require payment except as part of the plaintiff's costs of the action. The affidavits demonstrate that I.C.B.C. sometimes pays for medical legal reports even when liability is in issue in order to facilitate settlement.

The question in this case is whether the payments were "in respect of" the plaintiff's "cause of action".

In Desrosiers v. Wharton et al., [1984] B.C.J. No. 830, Vancouver Registry Nos. H823031 and C827130, November 29, 1984, Macdonald, J. after commenting on the disclaimer in that case said (at p. 5): "Confirmation within the meaning of s. 5(2)(a)(ii) of the Limitation Act is not the equivalent of an admission of liability." I agree with that view. A defendant might acknowledge the existence of a claim and make a payment on account of it without specifically admitting liability. The plaintiff might thereby be lulled into thinking that his claim would be paid if he was patient. I think

that the legislature intended to protect a plaintiff in those circumstances by s. 5(2)(a)(ii) and that we should interpret the section to encompass such a case.

I do not question the correctness of Podovinikoff v. Montgomery (1984), 58 B.C.L.R. 204. That case dealt with s. 5(2)(a)(i) and held that the provision was activated by an acknowledgment that admitted some liability. A payment in respect of a claim will normally indicate an admission of some liability. Thus my interpretation of s. 5(2)(a)(ii) is consistent with Podovinikoff's interpretation of s. 5(2)(a)(i).

The legislature needed the term "cause of action" to describe claims which survived a limitation period. The word claim can be too broad or too narrow. Cox v. Robert Ltd. et al. (1973), 1 O.R. (2d) 333 (Ont. C.A.), demonstrates the difficulty. So does this language in the Report on Limitations, Part 2 General, of the British Columbia Law Reform Commission (1974) (at p. 8):

> The function of a limitation period is to bar the bringing of an action after a specific length of time has passed from the alleged (by a potential plaintiff) occurrence of events which, if those events could be proved, would amount to a cause of action.

In this case "cause of action" must mean the plaintiff's claim against the defendant for damages arising out of the motor vehicle accident that occurred on February 8, 1984.

The breadth of the words "in respect of" was explained by Dickson, J. (as he then was) speaking for the Supreme Court of Canada in Nowegijick v. Her Majesty the Queen and The Grand Council of the Crees (of Quebec et al., [1983] 1 S.C.R. 29 (at p. 39):

> The words "in respect of" are, in my opinion, words of the widest possible scope. They import such meanings as in relation to", "with reference to" or "in connection with". The phrase "in respect of" is probably the widest of any expression intended to convey some connection between two related subject matters.

The payments in question were made by I.C.B.C. on behalf of the defendant in the course of negotiating settlement of the plaintiff's claim against the defendant. I conclude that the payments were made in respect of the plaintiff's claim against the defendant for damages arising out of the motor vehicle accident of February 8, 1984. The statute provides that such payments confirm the cause of action.

I agree with Hutchinson, L.J.S.C. that the Limitation Act does not bar this action, and would dismiss the appeal.

SEATON J.A.
AIKINS J.A.:-- I agree.
MACDONALD J.A.:-- I agree.

# Tab 22

sharing in profit and loss. • The phrase referred to one test for determining whether a partnership existed.

**contribution.** (14c) **1.** The right that gives one of several persons who are liable on a common debt the ability to recover proportionately from each of the others when that one person discharges the debt for the benefit of all; the right to demand that another who is jointly responsible for a third party's injury supply part of what is required to compensate the third party. — Also termed *right of contribution*. [Cases: Contribution ⇨1–6.] **2.** One tortfeasor's right to collect from joint tortfeasors when — and to the extent that — the tortfeasor has paid more than his or her proportionate share to the injured party, the shares being determined as percentages of causal fault. [Cases: Contribution ⇨5–7.] **3.** The actual payment by a joint tortfeasor of a proportionate share of what is due. Cf. INDEMNITY. **4.** *Maritime law.* A share of the loss resulting from a ship's sacrifice of cargo, payable by each party whose property was spared to the party whose property was sacrificed. **5.** WAR CONTRIBUTION.

**contribution agreement.** See SUPPORT AGREEMENT.

**contribution bar.** Preclusion of a defendant having contribution rights against other defendants, who have settled their dispute with the plaintiff, from seeking contribution from them. • The bar is usu. allowed in exchange for a credit against any judgment the plaintiff obtains against the nonsettling defendant. [Cases: Contribution ⇨8.]

**contribution clause.** See COINSURANCE CLAUSE.

***contributione facienda*** (kon-tri-byoo-shee-**oh**-nee fay-shee-**en**-də). [Latin "writ for making contribution"] *Hist.* A writ to compel a tenant in common to contribute to a fellow tenant who has paid more than the tenant's share of a sum for which all the tenants are liable.

> "*Contributione facienda* is a writ that lieth in case where more are bound to one thing, & one is put to the whole burden. . . . If tenents in comon or joynt, hold a mill (*pro indiviso*) & equally take the profits therof, the mill falling to decay, & one or more of them refusing to contribute toward the reparation therof, the rest shall have this writ . . . ." John Cowell, *The Interpreter* (1607).

**contribution margin.** The difference between a product's selling price and its variable production costs. • The contribution margin measures the amount of funds available for profit and payment of fixed costs.

**contributory** (kən-**trib**-yə-tor-ee), *adj.* (15c) **1.** Tending to bring about a result. **2.** (Of a pension fund) receiving contributions from both the employer and the employees. [Cases: Labor and Employment ⇨500.]

**contributory,** *n.* (15c) **1.** One who contributes or who has a duty to contribute. **2.** A contributing factor. **3.** *Hist.* A person who, as a result of being or representing a past or present member of a corporation, is liable to contribute to the corporation's debts upon its winding up.

**contributory infringement.** See INFRINGEMENT.

**contributory negligence.** See NEGLIGENCE.

**contributory-negligence doctrine.** (1911) *Torts.* The principle that completely bars a plaintiff's recovery if the damage suffered is partly the plaintiff's own fault. • Most states have abolished this doctrine and have adopted instead a comparative-negligence analysis. See FAULT; NEGLIGENCE. Cf. COMPARATIVE-NEGLIGENCE DOCTRINE. [Cases: Negligence ⇨547.]

**contributory pension plan.** See PENSION PLAN.

**control,** *n.* (16c) The direct or indirect power to govern the management and policies of a person or entity, whether through ownership of voting securities, by contract, or otherwise; the power or authority to manage, direct, or oversee <the principal exercised control over the agent>.

***superintending control.*** The general supervisory control that a higher court in a jurisdiction has over the administrative affairs of a lower court within that jurisdiction. [Cases: Courts ⇨204.]

***working control.*** The effective control of a corporation by a person or group who owns less than 50% of the stock. [Cases: Corporations ⇨174.]

**control,** *vb.* (15c) **1.** To exercise power or influence over <the judge controlled the proceedings>. **2.** To regulate or govern <by law, the budget office controls expenditures>. **3.** To have a controlling interest in <the five shareholders controlled the company>.

**control group.** (1937) The persons with authority to make decisions on a corporation's behalf.

**control-group test.** (1969) A method of determining whether the attorney–client privilege protects communications made by corporate employees, by providing that those communications are protected only if made by an employee who is a member of the group with authority to direct the corporation's actions as a result of that communication. • The U.S. Supreme Court rejected the control-group test in *Upjohn Co. v. United States*, 449 U.S. 383, 101 S.Ct. 677 (1981). Cf. SUBJECT-MATTER TEST. [Cases: Privileged Communications and Confidentiality ⇨123.]

**controlled company.** See COMPANY.

**controlled corporate groups.** See CONTROLLED GROUP.

**controlled corporation.** See CORPORATION.

**controlled debate.** See DEBATE.

**controlled foreign corporation.** See CORPORATION.

**controlled group.** *Tax.* Two or more corporations whose stock is substantially held by five or fewer persons. • The Internal Revenue Code subjects these entities (such as parent-subsidiary or brother-sister groups) to special rules for computing tax liability. IRC (26 USCA) §§ 851(c)(3), 1563(a). — Also termed *controlled corporate groups*. [Cases: Internal Revenue ⇨3633, 3870–3880.]

**controlled-securities-offering distribution.** See *securities-offering distribution* (1) under DISTRIBUTION.

**controlled substance.** (1970) Any type of drug whose possession and use is regulated by law, including a



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# Tab 23

## Bill Clause No. 105
## Section No. CCAA s.2
## Topic: Definitions

### Proposed Wording

**"equity claim" means a claim that is in respect of an equity interest, including a claim for, among others,**

- **(*a*) a dividend or similar payment,**
- **(*b*) a return of capital,**
- **(*c*) a redemption or retraction obligation,**
- **(*d*) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or**
- **(*e*) contribution or indemnity in respect of a claim referred to in any of paragraphs (*a*) to (*d*);**

**"equity interest" means**

- **(*a*) in the case of a company other than an income trust, a share in the company — or a warrant or option or another right to acquire a share in the company — other than one that is derived from a convertible debt, and**
- **(*b*) in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt.**

### Rationale

The definition of "**equity claim**" is added to provide greater clarity in subsequent provisions that deal with the rights of shareholders. An equity claim is defined to include any claim that is related to an equity interest.

The definition of "**equity interest**" is added to provide greater clarity in subsequent provisions that deal with the rights of shareholders. An equity interest is defined to include shares in corporations and units in income trusts and the right to acquire those except where the right is derived from a debt that is convertible into a share or unit. For example, a debenture witnessing a debt obligation that may, at the option of the holder, be converted into equity, should not be considered an equity interest - unless the holder has taken the steps necessary to have the conversion occur.

### Present Law

None.

# Tab 24

*Indexed as:*

# Tasko v. Canada

**Between**
**John Tasko, Appellant, and**
**Her Majesty the Queen, Respondent**

[1997] T.C.J. No. 9

[1997] A.C.I. no 9

[1997] G.S.T.C. 5

5 G.T.C. 1028

Court File No. 96-175(GST)I

Tax Court of Canada
Kamloops, British Columbia

**Bowman T.C.J.**

Heard: November 5, 1996
Judgment: January 8, 1997

(12 pp.)

*Sales and service taxes -- Goods and services tax -- Collection and enforcement -- Refundable tax credit.*

This was an appeal of a denial of a goods and services tax assessment. The appellant, Tasko, sought a new housing rebate of the GST. Tasko and four other people hired a contractor to build a five-unit townhouse complex. The units shared a roof and common walls. Each person occupied a unit in the complex and paid one-fifth of the complex cost. Tasko applied for the new housing rebate of 36 per cent of the GST on the cost of his unit's construction. The respondent Minister denied the application on the basis that the rebate was only available for a single unit residential complex. Tasko appealed the denial of his rebate application on the ground that he constructed a single residential unit for his own housing purposes.

HELD: The appeal was allowed. Tasko built his own condominium unit for use as his own residence. He was entitled to a rebate of the GST on the cost of the unit's construction.

**Statutes, Regulations and Rules Cited:**

Condominium Act, R.S.B.C. 1979, c. 61
Excise Tax Act, R.S.C. 1985, c. E-15, ss. 123(1), 254(2), 255, 256(1), 256(2)(a).
Indian Act, R.S.C. 1970, c. I-6, ss. 3(1), 14(2)(a), 14(2) (b).
Indian Timber Regulations, C.R.C. 1978, c. 961.
Interpretation Act, R.S.C. 1985, c. I-23, ss. 14, 15(2).

Evelyn Tasko, for the Appellant.
Elizabeth Junkin, for the Respondent.

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JUDGMENT:-- The appeal from the assessment made under the Excise Tax Act, notice of which is dated May 31, 1995 and bears number 950411816129P 8 is allowed and the assessment is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the appellant is entitled to the rebate under subsection 256(2).

The appellant is entitled to his costs, if any.

REASONS FOR JUDGMENT

**1** BOWMAN T.C.J.:-- This is an appeal from an assessment made under the Excise Tax Act whereby the appellant was denied the new housing rebate of Goods and Services Tax ("GST"). The appellant and his wife, together with four other couples, hired a contractor, Vic Van Isle Construction Ltd. ("Vic Van") to construct a five-unit townhouse complex. They each became owners of one of the units in the complex and the appellant and his wife still occupy their unit. It is not contested that the contractor, Vic Van, carried out the physical construction of the complex or, if they had constructed a single family dwelling, they would have been entitled to the rebate.

**2** The facts are not particularly in dispute and are set out in paragraphs 8(b) to (p) of the Reply, as follows:

> b) the Appellant is not registered under Part IX of the Excise Tax Act, R.S.C. 1985, c. E-15, as amended (the "Act");
> c) on or about May 31, 1993, the Appellant and his spouse, Evelyn Tasko, along with 4 other couples, purchased four parcels of vacant land for the purpose of constructing a five unit townhouse complex (the "Complex");
> d) the 4 other couples were Albert and Sherrian Van Goor, Jacob and Mary Van Goor, Donald and Josephine Hawker, and Donald and Grace Gillespie (all 5 couples together shall be referred to as the "Owners");
> e) the Owners hired Vic Van Isle Construction Ltd. (the "Builder") to build the Complex and they paid the Builder by monthly progress payments

from November 1993 until May 1994, by which time the Complex was substantially completed;

f) payments to the Builder were made through Glacier Place Strata Development;

g) each of the 5 couples paid approximately one fifth of the development and construction costs of the Complex;

h) the Complex is comprised of five residential units on one level which share a roof and are joined together by a common wall between each unit;

i) on or about February 23, 1994, the Owners consolidated the 4 parcels of land into one lot (the "Lot"). Legal title for the Lot was in Donald and Grace Gillespie's name;

j) the Lot was legally described as Parcel Identifier 018-621-848, Lot A, Section 34, Township 23, Range 2, West of the 6th Meridian, Kootenay District Plan NEP21053, and had a civic description of 404 West 5th Street, Revelstoke, B.C.;

k) on or about October 26, 1994, the Owners applied to strata-title the Complex, and on November 3, 1994, the strata plan of the Complex was registered as Strata Plan NES 172 pursuant to the Condominium Act, R.S.B.C. 1979, c.61, as amended;

l) on or about November 3, 1994, legal title of the strata lot legally described as:

> Parcel Identifier 018-979-360, Strata Lot 5, Section 34, Township 23, Range 2, West of the 6th Meridian, Kootenay District, Strata Plan NES 172.

and with a civic description of 408 West 5th Street, Revelstoke, B.C. (the "Strata Unit"), was transferred from Donald and Grace Gillespie to the Appellant and his spouse for $21,000;

m) all 5 residential units in the Complex are strata-titled under Condominium Act and each of the units is, and at all material times was intended to be, a bounded space in a building designated or described as a separate unit on Strata Plan NES 172;

n) the Appellant paid $7,657.84 in G.S.T. with respect to construction of the Strata Unit, and claimed a New Housing Rebate of 36% of that amount ($7,657.84 x 36% = $2,756.82);

o) the Strata Unit is a residential condominium unit within the meaning of subsection 123(1) of the Act; and

p) the Complex is not a single unit residential complex within the meaning of section 256 of the Act.

**3** The appellant accepts the correctness of these "assumptions" except that he does not admit the conclusions of law in (o) and (p).

**4** Initially there was some concern about the fact that the payments were made to the construction company through the condominium corporation, Glacier Place Strata Development Corpora-

tion. Nothing turns on this. That company was simply the strata corporation referred to in section 13 of the Condominium Act of British Columbia. The appellant and the other four couples were the builders and payments made by the strata corporation to Vic Van were made on their behalf.

**5** The essential question is whether a person who participates with others in building a condominium complex and ultimately becomes the owner of one of the residential condominium units for use as his or her primary place of residence is entitled to the rebate of GST provided by subsection 256(2). That such a person should be entitled to such a rebate is obvious and the denial of the rebate is patently absurd. A person who builds a single family residential unit for his or her own primary place of residence is entitled to the rebate under subsection 256(2), as is the purchaser from a builder of a residential condominium unit under subsection 254(2)[1].

**6** Subsection 256(2) requires that the Minister pay a rebate of GST to an individual who builds his or her own single unit residential complex for use as that individual's primary place of residence. The rebate is calculated in accordance with a formula based upon the fair market value of the residential complex and 36% of the GST paid by the individual. A similar rebate is available under subsection 254(2) to the purchaser from a builder of a single unit residential complex or a residential condominium unit, and, under section 255, to a shareholder of a co-operative housing corporation. The position of the respondent is that the appellant simply falls between these provisions.

**7** The portion of subsection 256(2) with which we are concerned here is found in paragraph 256(2)(a):

> Where
> (a) a particular individual constructs or substantially renovates, or engages another person to construct or substantially renovate for the particular individual, a single unit residential complex for use as the primary place of residence of the particular individual or a relation of the particular individual,
> ...

**8** "Single unit residential complex" is defined in subsection 123(1) as:

> a residential complex that does not contain more than one residential unit, but does not include a residential condominium unit.

**9** "Single unit residential complex" in subsection 256(1):

> includes a multiple unit residential complex that does not contain more than two residential units. (emphasis added)

**10** In subsection 123(1) "multiple unit residential complex" is defined to mean:

> a residential complex that contains more than one residential unit, but does not include a condominium complex.

**11** "Residential complex" is defined in subsection 123(1) to mean:

> (a) that part of a building in which one or more

residential units are located, together with
(i) part of any common areas and other appurtenances to the building and the land immediately contiguous to the building that is reasonably necessary for the use and enjoyment of the building as a place of residence for individuals, and
(ii) that proportion of the land subjacent to the building that that part of the building is of the whole building,

(b) that part of a building that is (i) the whole or part of a semi-detached house, rowhouse unit, residential condominium unit or other similar premises that is, or is intended to be, a separate parcel or other division of real property owned, or intended to be owned, apart from any other unit in the building, and (ii) a residential unit, together with that proportion of any common areas and other appurtenances to the building and the land subjacent or immediately contiguous to the building that is attributable to the unit and that is reasonably necessary for its use and enjoyment as a place of residence for individuals,

(c) the whole of a building described in paragraph (a), or the whole of a premises described in subparagraph (b)(i), that is owned by or has been supplied by way of sale to an individual and that is used primarily as a place of residence of the individual, an individual related to the individual or a former spouse of the individual, together with
(i) in the case of a building described in paragraph (a), any appurtenances to the building, the land subjacent to the building and that part of the land immediately contiguous to the building, that are reasonably necessary for the use and enjoyment of the building, and
(ii) in the case of a premises described in subparagraph (b)(i), that part of any common areas and other appurtenances to the building and the land subjacent or immediately contiguous to the building that is attributable to the unit and that is reasonably necessary for the use and enjoyment of the unit,

(d) a mobile home, together with any appurtenances to the home and, where the home is affixed to land (other than a site in a residential trailer park) for the purpose of its use and enjoyment as a place of residence for individuals, the land subjacent or immediately contiguous to the home that is attributable to the home and is reasonably necessary for that purpose, and

(e) a floating home, but not including a building, or that part of a building, that is a hotel, a motel, an inn, a boarding house, a lodging house or other similar premises, or the land and appurtenances attributable to the building or part, where the building is not described in paragraph (c) and all or substantially all of the supplies of residential units in the building or part by

way of lease, licence or similar arrangement are, or are expected to be, for periods or less than sixty days.

**12** "Residential unit" is defined in subsection 123(1) as:

> (a) a detached house, semi-detached house, rowhouse unit, condominium unit, mobile home, floating home or apartment, (b) a suite or room in a hotel, a motel, an inn, a boarding house, a lodging house or a residence for students, elderly persons, infirm persons or other individuals, or (c) any other similar premises, or that part thereof that (d) is occupied by an individual as a place of residence or lodging, (e)is supplied by way of lease, licence or similar arrangement for the occupancy thereof as a place of residence or lodging for individuals, (f) is vacant, but was last occupied or supplied as a place of residence or lodging for individuals, or (g) has never been used or occupied for any purpose, but is intended to be used as a place or residence or lodging for individuals. (emphasis added)

**13** "Residential condominium unit" is defined as:

> a residential complex that is, or is intended to be a bounded space in a building designated or described as a separate unit on a registered condominium or strata lot plan or description, or a similar plan or description registered under the laws of a province, and includes any interest in land pertaining to ownership of the unit.

**14** "Condominium complex" is defined as:

> a residential complex that contains more than one residential condominium unit.

**15** Subsection 15(2) of the Interpretation Act reads as follows:

> Where an enactment contains an interpretation section or provision, it shall be read and construed
> (a) as being applicable only if a contrary intention does not appear; and
> (b) as being applicable to all other enactments relating to the same subject-matter unless a contrary intention appears. R.S., c. I-23, s.14.

**16** Can it be said in light of these provisions that Parliament intended that an individual who builds a detached single family dwelling for his or her own personal residence, or a person who buys from a builder a condominium unit should be entitled to the rebate, but an individual who with others hires a contractor to construct a condominium complex of which one unit will be that person's residence is not similarly entitled to the rebate?

**17** The result on the face of it is absurd and one should not readily assume that Parliament intended to perpetrate an absurdity. In City of Victoria v. Bishop of Vancouver Island, [1921] 2 A.C. 384 Lord Atkinson, speaking for the Judicial Committee of the Privy Council, said at p. 388:

> There is another principle in the construction of statutes specially applicable to this section. It is thus stated by Lord Esher in Reg. v. Judge of the City of London Court (3): "If the words or an Act are clear, you must follow them, even though they lead to a manifest absurdity. The Court has nothing to do with the question whether the legislature has committed an absurdity. In my opinion, the rule has always been this: -- if the words of an Act admit of two interpretations, then they are not clear; and if one interpretation leads to an absurdity, and the other does not, the Court will conclude that the legislature did not intent to lead to an absurdity, and will adopt the other interpretation."

**18** If the words are clear I cannot avoid an absurd result by ignoring them. Robertson J.A. said in Her Majesty The Queen v. Paxton (F.C.A., A-513-94, December 12, 1996):

> At the outset I wish to make clear that I am acutely aware of the prohibition against employing the purposive approach in the context of statutory language which admits of no ambiguity and where the legal and practical effect of a transaction is undisputed: see Canada v. Antosko, [1994] 2 S.C.R. 312 at 326-27, per Iacobucci J.

**19** If there is however another interpretation that leads to a result that is not absurd, that interpretation must be adopted.

**20** There are other principles of interpretation that must be observed as well:

(a) The teleological approach: CUQ v. Corporation Notre-Dame de Bon-Secours [1994] 3 S.C.R. 3 at 17. This approach of course requires the identification of the telos at which the statute is aimed. Here the telos is to give a rebate to individuals who build their own residence as the appellant did.

(b) The "functional" as opposed to the "purely mechanical" approach: The Queen v. Swantje, 94 D.T.C. 6633 (F.C.A.); affirmed 96 D.T.C. 6310 (S.C.C.). This approach requires a consideration of the scheme as a whole, taking into account the intent of the legislation, its object and spirit and what it actually accomplishes.

(c) The "words-in-total-context" approach: Lor-Wes Contracting Ltd. v. The Queen, 85 D.T.C. 5310 (F.C.A.). This approach would reject the narrow focus which the respondent urges. In the context of the Act as a whole the appellant should be entitled to the rebate.

(d) Object and spirit: Stubart Investments Ltd. v. The Queen, [1984] 1 S.C.R. 536. The object and spirit of the legislation is the same as that stated in (a).

(e) Clear words: Ville de Montréal v. ILGWU Center et al., [1974] S.C.R. 59 at 66 (F.C.A.); The Queen v. Coopers & Lybrand Limited, 94 D.T.C. 6541 at 6546. Clarity is not something which one would routinely ascribe to the GST provisions of the Excise Tax Act and any ambiguity should be resolved in favour of the taxpayer (Fries v. The Queen, 90 D.T.C. 6662 (S.C.C.); Stubart (supra)). In any event we have here a perfectly understandable expression "single unit residential complex" which in its plain

meaning includes a condominium unit and an attempt to restrict that meaning by reference to a definition it is clear was not intended to be used for the purpose of denying the new housing rebate.

(f) The scheme of the legislation: Highway Sawmills Ltd. v. M.N.R., 66 D.T.C. 5116 at 5120 (S.C.C.). The overall scheme is to grant a rebate to persons who build their own homes.

**21** By any of these rules the appellant should obtain the rebate. On the other hand a purely mechanical approach would deny the rebate on the basis that:

(a) the definition of a single unit residential complex in subsection 123(1) (even in its extended version in subsection 256(1)) excludes a residential condominium unit; and

(b) a multiple unit condominium complex is not a single unit residential complex within the meaning of section 256 of the Act because it contains more than two residential units; and

(c) a multiple unit residential complex does not include a condominium complex within the definition of that term.

**22** This, notwithstanding the fact that a "residential unit" includes a "condominium unit" and a "residential complex" includes a "residential condominium unit". One could, if it were not for the definition in subsection 123(1) of "single unit residential complex" logically proceed from the definitions of "residential unit" and "residential complex" to the conclusion that a single condominium unit would be a "single unit residential complex" and that each of the 5 couples was, in essence, constructing its own residential unit within the building. Is the definition of "single unit residential complex" in subsection 123(1) an insuperable obstacle to such a conclusion? I cannot ignore the definition unless it is possible to conclude that it is not applicable because a contrary intention appears (subsection 15(2) of the Interpretation Act).

**23** I think that the view that conforms more closely to the object, spirit and scheme of the legislation is that a contrary intention is apparent where the expression "single unit residential complex" is used in subsection 256(2). One can readily see why it may have been necessary to draw a distinction between a "single unit residential complex" and a "residential condominium unit" for the purposes of section 191 and section 254. In section 255, which deals with rebates payable to shareholders in a co-operative housing corporation, no distinction is made and the term "residential unit" (which is an all-embracing term) is used. I can, however, see no purpose in excluding from the ordinary meaning of "single unit residential complex" a residential condominium unit for the purpose of denying the rebate to a person who builds his or her own condominium unit. While I acknowledge that this in itself is not a reason for ignoring a definition, it does at least lead me to conclude that such an exclusion, for the purposes of subsection 256(2), was both inadvertent and inconsistent with the context of the new housing rebates.

**24** Section 15 of the Interpretation Act directs us, in forceful and unequivocal terms, not to apply interpretation sections mechanically. I regard the words "as being applicable only if a contrary intention does not appear" (emphasis added) or, in French, "n'ont application qu'à défaut d'indication contraire" as requiring the use of definitions only where there is no contrary intention. The granting of a rebate in all other circumstances, with no apparent reason for denying it to a per-

son who builds his or her own condominium in a condominium complex, appears to me to indicate a statutory context from which a contrary intention may be inferred.

**25** In Quemont Mining Corp. Ltd. et al. v. M.N.R., 66 D.T.C. 5376 at 5387, Mr. Justice Cattanach of the Exchequer Court considered section 34 of the Interpretation Act, R.S.C. 1952 c.158, which at that time read as follows:

> 34. Definitions or rules of interpretation contained in any Act, unless the contrary intention appears, apply to the construction of the sections of the Act that contain those definitions or rules of interpretation, as well as to the other provisions of the Act.

**26** In the result he excluded the application of a definition "income derived from mining operations in a province" contained in paragraph 701(2)(a) of the Income Tax Regulations from a formula under which the amount of provincial mining taxes deductible were to be calculated. Mr. Justice Cattanach's judgment was affirmed by the Supreme Court of Canada, sub nom. Rio Algom Mines Ltd. v. M.N.R., 70 D.T.C. 6046. The majority of the Supreme Court of Canada did not refer to the Interpretation Act. Rather they based their decision upon "the plain meaning of the regulation" and the fact that any other construction would produce an anomaly. The wording of the present subsection 15(2) appears to me to express the statutory restriction on the use of definitions more strongly than did former section 34.

**27** In Regina v. Scory, (1965), 51 W.W.R. 447 (Sask QB) Davis J. said at p. 448:

> To hold that the definition is exhaustive and must prevail would do violence to the recognized rules of grammar and would render the subsection meaningless. The law is that if a defined expression is used in the context which the definition will not fit, the context must be allowed to prevail over the "artificial conceptions" of the definition clause and the word must be given its ordinary meaning: Maxwell on Interpretation of Statutes, 11th ed., p.31; Strathern v. Padden [1926] SC (J) 9.

**28** This observation was quoted with approval by Rip J. of this court in Taylor v. M.N.R., 88 D.T.C. 1571. To the same effect Esson J.A. in the British Columbia Court of Appeal said in Cadillac Explorations Ltd. v. Procan Exploration Company et al., 53 B.C.L.R. 353 said at p. 357:

> I will assume that a contrary intention can be established not only by express words but also by the context and other considerations requiring a different interpretation. In Pac. Simpson Lbr. Ltd. v. Kaisha, [1982] 3 W.W.R. 194, 129 D.L.R. (3d) 236, this court applied such an approach in considering the words "unless a contrary intention appears" in s. 3(1) of the same Act in construing the words "year" in the regulations [Indian Timber Regulations, C.R.C. 1978, c. 961] under the Indian Act, R.S.C. 1970, c. I-6. The court gave a number of reasons for holding that "year" in those regulations did not have the meaning set out in the Interpretation Act. That conclusion was based upon the history of the legislation, the absurdity and impracticability which would result if the definition in the Interpretation Act was to be applied, and the fact that the word appeared in a phrase

(year of issue) in which it would be reasonable to think that a different meaning was intended from if it had been used alone. Those reasons, taken together, were held to require the finding that a contrary intention appeared.

The difference between "only if the contrary intention does not appear" in s. 14(2)(a) and "unless the contrary intention appears" in s. 14(2)(b)and s. 3(1) of the same Act is puzzling but I can see no reason to think that any difference in meaning was intended. The question must still be whether the context and other considerations require the conclusion that a contrary intention appears. I cannot find that, in this case, they do.

**29** The GST provisions of the Excise Tax Act are a particularly striking example of the judicially criticized practice of enacting under the guise of definition. We not infrequently encounter, in interpreting this statute, cases in which the object of the legislation could be defeated if the substantive dog is allowed to be wagged by the definitional tail. I shall not repeat the criticisms that have been made of the practice beyond noting that in Craies on Statute Law, Seventh Edition, at pages 212-216, a number of cases are cited in which the practice is deplored and the dangers of indiscriminate use of interpretation provisions are expressed. The problem in this case stems from Parliament's giving to "single unit residential complex" a meaning that is inconsistent with its ordinary meaning for certain purposes and from the Department's applying that definition in a context to which the restriction plainly could not have been intended to apply.

**30** In this case I think that a contrary intention is apparent, and that the builder of his own residential condominium unit to be used as his personal residence is entitled to the rebate provided under subsection 256(2).

**31** The appeal is allowed and the assessment is referred back to the Minister of National Revenue for reassessment on the basis that the appellant is entitled to the rebate under subsection 256(2).

qp/d/scl/mjb/DRS

1 It is evident that the government recognizes the anomalous position created by its view of the application of subsection 256(2). Subsection 66(1) of the April 23, 1996 Notice of Ways and Means Motion extends the rebate to owner built residential condominium units. Of course I cannot take into account subsequent legislation in construing a statute and a fortiori I cannot take into account proposed legislation that is not yet law: The Queen v. Specialties Distributors Ltd., 54 D.T.C. 1139 at 1141. In any event the proposed legislation, if it ever becomes law, unless it is changed before final reading, will only be effective in respect of applications made on or after April 23, 1996.

# Tab 25

*Case Name:*

# Caressant Care Nursing Home of Canada Ltd. v. London and District Service Workers' Union, Local 220

**Between**
**Caressant Care Nursing Home of Canada Limited, applicant, and**
**London and District Service Workers' Union, Local 220 and Pay Equity Hearings Tribunal, respondents**

[2005] O.J. No. 1560

197 O.A.C. 238

32 Admin. L.R. (4th) 129

138 A.C.W.S. (3d) 858

2005 CarswellOnt 1618

Court File No. 528/02

Ontario Superior Court of Justice
Divisional Court

**G.D. Lane, P.T. Matlow and A.M. Molloy JJ.**

Heard: February 2 and 4, 2005.
Judgment: April 12, 2005.

(91 paras.)

*Human rights law -- Legislation -- Employment and pay equity legislation -- Statutory interpretation -- Statutes -- Construction -- Strict interpretation -- Legislative intent -- Operation of -- Amendment -- Purpose of -- Aids -- Extrinsic -- Administrative law -- Standard of review -- Correctness -- Reasonableness -- Judicial review and statutory appeal -- When available -- Error of mixed law and fact.*

Application by Caressant Care Nursing Home for judicial review of two decisions by the Pay Equity Hearings Tribunal finding that Caressant fell within the definition of a public sector employer

under the Pay Equity Act, and that its entire operation was subject to the proxy method of wage comparison pursuant thereto, and refusing reconsideration of the decision. Caressant was a private corporation that owned and operated a nursing home and retirement home in separate wings of the same building. The nursing home received government funding and was subject to strict regulation. The retirement home operated as a private business. The Tribunal held that any corporation that operated a licensed nursing home was a public sector employer. It concluded that because the same legal entity operated both the nursing home and the retirement home, Caressant was a public service employer in respect of both facilities. It further held that the operation of both facilities was inextricably intertwined. Following the Tribunal's decision, the provincial government enacted a regulation to clarify that the applicable statutory definition applied only in respect of an employer's nursing home beds. Following the amendment, the Tribunal refused to exercise its discretion to reconsider its decision at the behest of Caressant. The Tribunal held that the amendment did not have retrospective effect and therefore had no bearing on its initial decision.

HELD: Application allowed. The finding that the amendment was not retrospective was a pure question of law and was thus reviewable on a standard of correctness. The Tribunal's decision not to reconsider its initial decision was correct because there was no implication that the amendment applied retrospectively. The initial issue before the Tribunal was a question of mixed law and fact that involved principles of statutory interpretation, and attracted a measure of deference to its expertise. As such, the initial decision was reviewable on a standard of reasonableness simpliciter. The findings that Caressant was the actual employer of both businesses, and that both businesses were part of the same establishment were reasonable. However, the determination that the term "public sector employer," if applicable to any aspect of an employer's business, was appropriate for all aspects of an employer's business, was unreasonable. The Tribunal's approach of a literal interpretation created an unfair and absurd result by creating different conditions for Caressant, as an owner of a private retirement home, by virtue of the fact that it also owned a publicly funded nursing home. A review of extrinsic materials was consistent with an interpretation that the proxy method of comparison was never intended to apply to private sector businesses. Accordingly, the Tribunal's decision was quashed and remitted for a new hearing.

**Statutes, Regulations and Rules Cited:**

Interpretation Act itself, R.S.O. 1990, c. I-11, ss. 10, 17.

Nursing Home Act, R.S.O. 1990, c. N-7.

Pay Equity Act, R.S.O. 1990, c. P-7, as amended ss. 1(1), 22.12(2), 30(1), 36(2).

Pay Equity Act, R.S.O. 1990, c. P-7, as amended, Regulation 396/93 s. 2(1), 2(3).

Pay Equity Act, R.S.O. 1990, c. P-7, as amended, Regulation 37/ 02 "public sector employer.

Pay Equity Act, R.S.O. 1990, c. P-7, as amended, Schedule and Appendix s. 1(b), 1(i).

**Counsel:**

David M. Golden, Irv Kleiner and Lisa Corrente, for the applicant

Cathy Lace, for the respondent union

Leslie A. Leroux, for the respondent tribunal

REASONS FOR JUDGMENT

The judgment of the Court was delivered by

A.M. MOLLOY J.:--

A. INTRODUCTION

**1** The applicant ("Caressant Care") is a private corporation which owns a nursing home and retirement home in St. Thomas, Ontario. The two homes are on the same property and are essentially separate wings of the same building, separated by a door. The nursing home side is licensed under the Nursing Home Act, R.S.O. 1990, c. N-7, receives government funding for its operations and is subject to strict government scrutiny and controls. The retirement home side is strictly a private business operation, receives no government funding, and is not subject to any controls beyond those imposed on any business operating in the province. Both aspects of Caressant's business have a predominantly female workforce and are subject to wage adjustment under the Pay Equity Act, R.S.O. 1990, c. P-7, as amended ("the Act"). It is clear the nursing home side of Caressant's business falls within the broader public sector and as such is subject to the "proxy method" for purposes of wage comparison. Likewise, it is clear that private businesses are not subject to the proxy method of comparison. The issue in the case before the court is whether, in the particular circumstances of this business, the retirement home side of Caressant Care is also subject to the proxy method of comparison.

**2** In a decision dated December 17, 2001, the Pay Equity Hearings Tribunal decided that Caressant Care fell within the definition of public sector employer under the Act and that its entire operation, both the nursing home and retirement home aspects, were subject to the proxy method of comparison. That decision was based on an Appendix to the Schedule to the Act, which provided that the public sector included "any corporation ... that operates or provides a nursing home, under the authority of a licence issued under the Nursing Homes Act".

**3** On February 6, 2002, the Ontario Legislature enacted a regulation which amended the applicable part of the definition by adding to it, "but, for greater certainty, only in respect of its nursing home beds with respect to which funding is received from the Province of Ontario". Following this amendment, Caressant asked the Tribunal to reconsider its earlier decision. By decision dated May 6, 2002, the Tribunal refused to exercise its discretion to reconsider its decision.

**4** Caressant Care now seeks judicial review of both Tribunal decisions.

B. THE STATUTORY SCHEME

**5** The Pay Equity Act came into force on January 1, 1988. The purpose of the legislation is to redress historic and systemic gender discrimination in the workforce, which has resulted in women being paid less than men for work of equal value. The Act applies to the public sector and to private employers with more than 10 employees. However, there are distinctions within the legislation between public and private employers as to the applicability of certain provisions.

**6** Under the legislative scheme, employers are required to identify job classes based on a neutral set of criteria and to determine if there is gender predominance in those job classes. The value of the work performed by each job class is then determined based on skill, effort, responsibility and

working conditions. Under the scheme as first introduced, the remaining step required the employer to carry out a "job-to-job" comparison, comparing the remuneration paid to female job classes with that paid to equal or comparably valued male job classes. The employer was then required to increase the salaries of female employees who were receiving less than their male counterparts in comparable male job classes.

**7** There were difficulties applying the job-to-job comparison method in predominantly female workplaces. In 1993, the Act was amended to include two alternative methods of comparison for situation in which the job-to-job method was not workable: the proportional value method and the proxy method.

**8** The proportional value method applies to any situation in which there are not sufficient males or male job classes in the workplace to compare using the job-to-job method. Under the proportional method, the employer is required to determine the ratio between the remuneration paid for male job classes and the value of the work performed. The same exercise is then carried out for the female job classes. If the ratio of pay to value of work is lower for a female job class than for male job classes, the female wages are required to be raised to achieve equity.

**9** If an employer is unable to apply either of the job-to-job or proportional value methods of comparison, the employer is obliged to notify the Pay Equity Office. The matter is then referred to a Review Officer who considers whether, in fact, there is any female job class within the employer's establishment that cannot be compared using those two methods of comparison. If so, and if the Review Officer determines "that the employer is a public sector employer", then the Review Officer may make an order declaring the employer to be a "seeking employer": s. 22.12(2) of the Act. The seeking employer is required to determine the relationship between the value of work performed in its female job classes and the remuneration paid for that work. This pay/value ratio is then compared to that of a proxy employer, based on a list set out in Regulation 396/93 of the Act. The Regulation contains a list of categories of seeking employers and matches them to a list of proxy employers. The proxy employers are for the most part public hospitals, school boards or facilities operated by a municipality. Seeking employers who operate nursing homes, homes for the aged or who provide other services for seniors are compared to "a home for the aged operated by one or municipalities under the Homes for the Aged and Rest Homes Act". A seeking employer that does not fit within any of the categories listed must be compared to a hospital or municipality: s. 2(1) and (3) of the Regulation.

**10** It is a precondition to the application of the proxy method of comparison that the Review Officer determine the employer to be a "public sector employer". The Act includes both a Schedule and an Appendix to that Schedule. "Public sector employer" is defined in the Act to mean any employer listed in the Schedule to the Act. In turn, s. 1(i) of the Schedule provides that the public sector includes any corporation "set out in the Appendix to this Schedule". The Appendix is organized under the headings of various Government of Ontario Ministries. Under the heading "Ministry of Health", the Appendix sets out a number of employers deemed to be part of the public sector, including:

> 1. Any corporation ... that operates or provides,
>
> (b) a nursing home, under the authority of a licence under the Nursing Homes Act (R.S.O. 1990, c. N-7).

**11** There is no other clarification in the Act as to which employers are public sector and which are not. "Private sector" is defined to mean all of the employers who are not in the public sector and an employer is deemed to be in the "public sector" if it is listed in either the Schedule or Appendix.

**12** An employer's "establishment" is defined in s. 1(1) of the Act to mean "all of the employees of an employer employed in a geographic division. The relevant portion of the definition of "geographic division" is "county, territorial district or regional municipality".

**13** An employer subject to an order made by a Review Officer may request a hearing before the Pay Equity Hearings Tribunal. That Tribunal is protected by a privative clause, s. 30(1) of the Act, which states:

> The Hearings Tribunal has exclusive jurisdiction to exercise the powers conferred upon it by or under this Act and to determine all questions of fact or law that arise in any matter before it and the action or decision of the Hearings Tribunal thereon is final and conclusive for all purposes.

C. THE DECISION OF THE TRIBUNAL

The Initial Decision (December, 2001)

**14** Caressant Care reported to the Pay Equity Office that it had a predominantly female workforce at its retirement home and was unable to use either of the job-to-job or proportional value methods of comparison in order to develop a pay equity plan. The Review Officer confirmed that Caressant Care was in fact unable to use those methods and went on to determine that Caressant Care fell within the term "public sector employer", such that the proxy method of comparison would apply. Caressant Care sought a hearing before the Tribunal with respect to that determination. The Tribunal hearing proceeded before a three-person panel and occupied 35 days of testimony and argument over a period of two-and-a-half years. The Tribunal issued a 67 page written decision on December 17, 2001. The Tribunal heard this case together with four others in similar circumstances. However, only the decision with respect to Caressant Care is before this court on judicial review.

**15** The Tribunal first reviewed some of the general background facts. The Tribunal accepted evidence before it that there are 500 retirement homes in Ontario and 300 nursing homes licensed under the Nursing Homes Act. Of the retirement homes, 70 have adjoining nursing homes (of which Caressant Care's facility in St. Thomas is one). The Tribunal noted the substantial differences between nursing homes and retirement homes. Nursing homes are highly regulated by the Ministry of Health and governed by statute; anyone who wants may build and operate a retirement home subject only to laws of general application such as zoning by-laws and fire codes. Nursing homes are subject to mandatory service standards, government monitoring and inspections; retirement homes have no such restrictions and are not inspected even if they have an adjoining nursing home that is inspected. Nursing homes receive considerable government funding in three notional envelopes (accommodation, nursing, and programs) and may also receive some funds from the residents; retirement homes receive no government funding. Nursing homes must account strictly for all funds received and are permitted to earn a profit only on the accommodation aspect of its business with any monies unspent in respect of nursing and programs being returned yearly to the government; retirement homes are businesses operated for a profit without government controls. Nursing homes are required to comply with a government design standard for their physical facilities; retirement homes are only required to meet minimum building code standards. Admissions to nursing homes

are controlled by a government agency and applicants are placed on waiting lists and placed in facilities based on Ministry of Health eligibility criteria; admissions to retirement homes are based solely on choices made by the residents and their families. A resident of a retirement home adjacent to a nursing home has no right to admission to the nursing home, but must go through the same process of eligibility selection through the Ministry. Nursing home regulations specify certain numbers of employees with certain qualifications and mandatory staff/resident ratios; retirement homes are free to hire any type or number of employees they wish. Nursing homes are treated as part of the public sector for pay equity purposes; retirement homes are not.

**16** The Tribunal noted that the Act makes substantial distinctions between the public and private sector. The Tribunal held that the interpretation to be ascribed to "public sector" and "private sector" can only be based on how those terms are used in the Pay Equity Act itself. It found case law based on how those terms are used in other contexts to be of no assistance in this analysis. The Tribunal reviewed the definitions in the Act and held that this created a "hierarchy of inquiries" in that one must first consider whether an employer is listed in the Schedule. If so, the employer is public sector. If not, by the process of exclusion, it is private sector. The Tribunal further held that the Act "sets up a binary scheme", in that an employer has to be in one category or the other, and held that the Act "does not contemplate the existence of 'hybrid' employers": Reasons para. 64. The Tribunal then reviewed the various categories of employers listed in the Schedule and Appendix and concluded it was simply a catalogue of entities rather than a functional examination of activities performed. It therefore rejected the possibility of a jurisprudential definition of "public sector" based on the nature of the employer's operations and determined that it is the identity of the employer and whether it is listed in the Schedule that is the sole determinant of public sector status: Reasons paras. 71-73.

**17** Next, the Tribunal looked at the Schedule and Appendix and held that the provision with respect to operators of nursing homes was clear and unambiguous. A corporation that operates a nursing home under a license under the Nursing Homes Act falls within the public sector. The Tribunal held that since the language was unambiguous, it should be given its plain meaning without resort to extraneous aids to interpretation such as legislative debates: Reasons paras. 57 and 75. Thus, the Tribunal determined that the question before it was whether the corporation that operated the nursing home also operated the retirement home.

**18** To answer that question, the Tribunal turned to established jurisprudence dealing with how "employer" status is determined under the Act. Reference was made to Hilton Works (No. 3) (1994), 5 P.E.R. 34, in which a tribunal under the Act held that theoretically a non-legal entity could be an "employer" for purposes of the Act, but where there is a relationship between the non-legal entity and a legal entity, "the existence of only one legal entity may be a sufficient indicator that the non-legal entity does not enjoy sufficient independence and autonomy to be capable of being a separate employer": Reasons para. 78.

**19** The Tribunal found that the existence of only one legal entity operating the nursing home and the retirement home was sufficient to determine the Caressant Care corporation to be the employer for both facilities. The Tribunal then reasoned that since that employer holds a nursing home license, it is a public sector employer for purposes of the Act.

**20** The Tribunal then went on to find, in the alternative, that when all the relevant factors developed under previous jurisprudence are taken into account, the Caressant Care corporation is the employer in respect of both the nursing home and retirement home. The criteria considered were:

who has overall financial responsibility; who has responsibility for compensation practices; what is the nature of the business, service or enterprise; and what is most consistent with achieving the purposes of the Act: Reasons at para. 83. Although the finances of both aspects of the business are separately accounted for, overall financial supervision and control of both businesses is by the Caressant Care head office personnel. Likewise, the corporation is responsible for compensation practices at both workplaces. There are separate staff rooms for each side of the business, separate employee requirements and separate bargaining units. However, there is also considerable overlap in functions. For example, there is only one central office and only one phone number, which could be answered by staff in either facility. Some of the food preparation and related services are shared. Employees on the retirement home side do the laundry for both facilities. A registered nurse employed on the nursing home side is in charge of the entire facility at night. Based on these and other facts of a similar nature, the Tribunal concluded that there was a single employer for both sides of the business. The Tribunal stated, at para. 86, "In these Applications the employment practices of the Nursing Home and the Retirement Home in each Retirement Community are so intertwined on a regular basis that they are inconsistent with the notion of separate employer status."

**21** Finally, the Tribunal considered whether the nursing home and retirement home sides of the business were part of the same "establishment". It ruled that under the Act this designation is based on geographic divisions, regardless of whether the work performed in different locations is similar in nature. Therefore, all employees of the employer in a municipality would be part of the same establishment for purposes of the Act. The Tribunal held that it is not necessary to find a community of interest among employees in order to determine either the identity of the employer or the scope of the establishment. The Tribunal rejected the argument that this would result in an absurd result by bringing employees of the retirement home into the public sector. The Tribunal recognized the logical consequences of its decision for radically different business operations, stating at para. 90, "Consequently, if a single legal entity operates a gas station, a retirement home and a pizza parlour within the same municipality, the workers of all three comprise the employer's establishment."

**22** The Tribunal concluded its analysis by holding, in para. 95:

> The Applicants also suggested strongly and repeatedly that the Legislature never intended to make proxy applicable to the Retirement Homes. The flaw in this argument, of course, is that the Tribunal must interpret the language actually employed in the Act, and to give effect to the Applicants' position would require us to read language into the Schedule so that a corporation is part of the public sector if it operates a nursing home pursuant to a license "but only to the extent of its nursing home operations". In any event, the Legislature has the ability to amend the Act. We note it did so after some early Tribunal decisions identified the Crown as the employer of persons working in agencies listed in the Schedule.

The Reconsideration Decision (May, 2002)

**23** The Tribunal's initial decision was released on December 17, 2001. On February 6, 2002, Regulation 37/02 under the Act was proclaimed. It addressed only that section of the Appendix to the Schedule dealing with operators of nursing homes and amended it by adding the words "but, for greater certainty, only in respect of its nursing home beds with respect to which funding is received from the Province of Ontario." This language is strikingly similar to that which the Tribunal had

said in its initial ruling would have to be read into the provision in order to achieve the result for which Caressant Care and other applicants had argued.

**24** Caressant Care requested the Tribunal to reconsider its initial decision, submitting that the amendment to the Appendix constituted a change in circumstances and that the decision was wrong in law. The reconsideration was heard by the same panel that issued the initial decision. The Tribunal held, consistent with other jurisprudence of the Board, that reconsideration was a discretionary matter and would be exercised only where: (i) there was new evidence not available at the time of the hearing that would likely make a substantial difference to the outcome; (ii) there had been a change in circumstances; or (iii) it was established that the earlier decision was wrong in law.

**25** The Tribunal held that the amendment to the Appendix did not have retrospective effect and therefore had no bearing on its decision. It declined to consider the new provision as an interpretive aid, holding that it had already decided the language of the Act was plain and unambiguous and it was therefore not relevant to consider extraneous evidence on its interpretation. Other arguments made by the applicants as to the earlier decision being wrong in law were found to be simply a re-hashing of arguments made earlier and already rejected in the initial decision. The Tribunal therefore refused to reconsider its initial decision.

D. STANDARD OF REVIEW

**26** There are three potential standards of review: correctness, reasonableness simpliciter, and patent unreasonableness. The Supreme Court of Canada has held that the determination of the appropriate standard of review for a particular decision of an administrative tribunal should be based on a "pragmatic and functional approach" based on four factors: (i) the existence or absence of a privative clause; (ii) the purpose of the legislation and of the particular provision; (iii) the expertise of the tribunal relative to that of the reviewing court on the issue in question; and (iv) the nature of the question before the tribunal: Pushpanathan v. Canada (Minister of Citizenship and Immigration), [1998] 1 S.C.R. 982.

**27** The Pay Equity Tribunal is protected by the "strong" privative clause in s. 30(1) of the Act: Haldimand-Norfolk (Regional Municipality) Commissioners of Police v. ONA, [1989] O.J. No. 1995 (Div.Ct.), upheld on appeal, (1990) 41 O.A.C. 148 (C.A.); Wentworth County Board of Education v. Wentworth Women Teachers' Association, [1991] O.J. No. 723 (Div.Ct.). This is a factor that suggests a standard of review at the highest level of deference, patent unreasonableness.

**28** The purpose of the Act is to redress systemic gender discrimination in compensation for work. The public interest is clearly engaged and there is a high policy-driven component to decisions under the Act. Decision makers under the Act are required to balance multiple sets of competing interests. The particular legislative provisions at issue in this case are definitional sections of the Act which will determine whether the employees of the retirement home side of the business will be considered as part of the broader public sector for purposes of pay equity. There has already been a determination that a job-to-job comparison is not workable in this workplace. If the employees do not fall within the public sector, they will not receive pay equity adjustments, even though the employees in the adjacent nursing home will. On the other hand, the employer runs a private business in competition with hundreds of other retirement homes in the province. Designating this business as part of the public sector would require the employer to increase the wage levels of its employees by comparing them to the wage levels at publicly owned and funded nursing homes without receiving any government funding toward its costs. The Tribunal's decision, therefore, af-

fects the public interest as well as the private interests of the employer and employees. This weighing of competing interests in a policy-laden public interest field is another factor attracting a standard of review at the more deferential end of the scale: Dr. Q. v. College of Physicians and Surgeons of British Columbia, [2003] 1 S.C.R. 226 at para. 31.

**29** The question before the Tribunal involves the interpretation of its home statute. An understanding of the policy and practical implications of such a determination must necessarily inform the decision. The Tribunal has considerable expertise in the subject area of pay equity. In Ontario Nurses' Assn. v. Ontario (Pay Equity Hearings Tribunal) (1995), 23 O.R. (3d) 43 (C.A.), Abella J.A. (as she then was) recognized the special expertise of the Tribunal at page 56, as follows:

> The language of the statute makes it clear that the overall responsibility for when, whether and how pay equity is achieved lies with the Pay Equity Commission, and its adjudicative branch, the Pay Equity Hearings Tribunal. The tripartite membership of the Tribunal consists of representatives from labour, management, and legal spheres whose backgrounds and continuing exposure to the legislation gives them a unique expertise. And it is clear from the privative clause and the legislation as a whole that the purpose of the Tribunal is to serve as the exclusive adjudicative body dealing with the redress of systemic gender discrimination in compensation for work, or pay equity.

**30** To the extent that the Tribunal is engaged in technical pay equity matters (such as the application of various methods of wage comparison and the identification of job classes), the Tribunal's special area of expertise is clearly engaged. Likewise, application of many of the legal principles developed in pay equity jurisprudence (such as who is the "employer" for the purposes of pay equity and the meaning of "establishment"), may also engage that special expertise, although to a somewhat lesser extent. On the other hand, questions of pure law not requiring a deep understanding of the operation of pay equity schemes, will not engage the Tribunal's expertise to the same degree. Depending on the nature of the particular question before it, the Tribunal's expertise will not be greater than that of the Court.

**31** The question before the Tribunal in this case required it to interpret the definition of "public sector employer" within the context of the legislation. Upon interpreting that definition as plain and unambiguous, the Tribunal concluded that if a corporation held a nursing home license it was by definition a public sector employer. That, in my view, is primarily a question of law involving principles of statutory interpretation. However, the provision in question must be interpreted in context, which requires an understanding of the statutory scheme and, as I will develop later, the legislative intent of the particular provision involved. In that regard, the Tribunal clearly has an expertise beyond that of the Court. In addition, in considering the implications of its interpretation of the definition, and particularly in determining who was the employer and what was the establishment, the Tribunal was applying pay equity concepts in the area of its special expertise.

**32** On the whole, the question before the Tribunal in its initial decision was a question of mixed fact and law, but one that is more law-driven than fact-driven. This is a factor that would suggest less deference.

**33** Determining the appropriate standard of review requires this Court to weigh each of the four factors identified in Pushpanathan in the context of the particular tribunal and the particular question before that tribunal. The starting point is usually a consideration of the standard applied by oth-

er reviewing courts. However, a review of previous cases dealing with the standard of review for this Tribunal is not determinative in this case. The Court of Appeal in Ontario Nurses' Assn. v. Ontario (Pay Equity Hearings Tribunal), supra, applied a standard of patent unreasonableness. However, that case turned on whether the issue determined by the Tribunal was jurisdictional in nature and whether the applicable standard was either correctness or patent unreasonableness. This was before the Supreme Court of Canada's decisions in Canada (Director of Investigation and Research) v. Southam, [1997] 1 S.C.R. 748 and Pushpanathan (in 1998), and therefore did not involve a consideration of the four factors and the possibility of a reasonableness simpliciter standard in addition to the other two standards. The same comment, and therefore the same caution, applies to the decisions of the Divisional Court and Court of Appeal in Haldimand-Norfolk (Regional Municipality) Commissioners of Police, supra.

**34** Counsel for the Tribunal and counsel for the Union rely on Employees at the Queen Street Mental Health Centre v. Ontario (Management Board Secretariat), [2001] O.J. No. 2255 (Div.Ct.) and General Health Services Inc. (c.o.b. Circle of Life Health Services) v. Buchanan, [2004] O.J. No. 1567 (Div.Ct.) as having established an applicable precedent for the standard of patent unreasonableness. I do not agree. The Queen Street Mental Health Centre case was subsequent to Pushpanathan. However, the Court in that case did not set out any analysis of the factors identified in Pushpanathan, but rather relied on the Court of Appeal decision in Ontario Nurses' Association v. Ontario (Pay Equity Hearings Tribunal) as authority for imposing a standard of patent unreasonableness. Further, that decision is distinguishable on its facts. The issue before the Tribunal in that case was the applicants' contention that a pay equity plan did not comply with the Act because the methodology used for valuing jobs was not gender neutral. That is an issue which goes to the heart of the Tribunal's specialized expertise. In the Circle of Life case, it would appear that the issue of the appropriate standard to be applied was not argued, but rather that all counsel conceded the standard of review was patently unreasonable. Again, this decision is distinguishable because of the nature of the decision before the Tribunal, which had a significant factual component.

**35** Wellington (County) v. Butler (2001), 56 O.R. (3d) 271 (Div.Ct.), was a judicial review of a Pay Equity Tribunal decision interpreting the word "employee". The Tribunal held that the individuals involved (who provided day care in their homes) were employees of the County, rather than independent contractors, and therefore entitled to pay equity under the Act. The Divisional Court three-member panel was split on the appropriate level of review. The majority members (Aston and Wright JJ.) were both of the view that the Tribunal decision should be quashed, and both stated they would have quashed the decision no matter what standard of review was applied. Aston J. appears to have leaned somewhat towards the reasonableness simpliciter standard, based on a determination that although the Tribunal had expertise it was not engaged in the same way, relative to the court, as would be the case in considering other aspects of the complex statutory scheme. He saw the question of whether the individuals were employees as being, ultimately, a legal conclusion. However, he then went on to hold that the applicable standard did not affect the outcome of his decision and ruled that the Tribunal decision should be quashed as patently unreasonable. Wright J. agreed in the result with Aston J., but for separate reasons in which he stated that the issue before the Tribunal was a question of law and that the Tribunal had no expertise to determine it. Lane J., in dissent, would have imposed a patently unreasonable standard of review, and would not have interfered with the Tribunal decision.

**36** The only other decision of which I am aware dealing with the application of the Pushpanathan principles to determine the standard of review for this Tribunal is a decision of this

Court, which was released just a few days before the argument of this case: Bucyrus Blades of Canada Ltd. v. McKinley, [2005] O.J. No. 231 (Div.Ct.). The applicant in that case (Ms. McKinley) had been dismissed by her employer, Bucyrus Blades. She accepted a termination package and signed a release which released all claims including "any claim under the 'Employment Standards Act of Ontario', the 'Human Rights Code of Ontario', or any other similar legislation governing or related to the employment of the Releasor". Thereafter she proceeded with a complaint under the Pay Equity Act seeking an adjustment of her wages. The Review Officer decided that since the Pay Equity Act was not specifically listed, Ms McKinley had not released her rights under that legislation. The Tribunal confirmed the Officer's decision. On judicial review, the majority of the Divisional Court considered the Pushpanathan factors and held that the appropriate standard of review on this issue was correctness, but that a standard of reasonableness applied to a further decision as to whether, apart from Ms. McKinley's situation, the employer was subject to pay equity. Crane, J. (writing on behalf of himself and Ferrier J.) held at paras. 59 and 60:

> It is clear from its Reasons that the Tribunal decided to engage in a legal interpretation of the parties' agreement. It did an analysis of the wording of their contract and came to a conclusion on the intention of the parties. In my view, this is the application of the common law of contract. The review standard of correctness applies.
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> The Tribunal also engaged in a policy determination as to whether the employer (absent Ms. McKinley) was subject to the provisions of the Pay Equity Act, and in particular s. 7. This issue is, on this Record, one of mixed fact and law to which a standard of reasonableness could apply.

**37** The minority judge in Bucyrus Blades (Pitt J.) would have applied a standard of patent unreasonableness.

**38** I am mindful, also, of the Supreme Court of Canada's further elucidation of the Pushpanathan principles in Voice Construction Ltd. v. Construction & General Workers' Union, Local 92, [2004] 1 S.C.R. 609, in which the decision under review involved a labour arbitrator's interpretation of a collective agreement. All nine judges of the Court held that the applicable standard of review was reasonableness simpliciter. Major J. (writing the unanimous opinion of the Court on these points) held at para. 18:

> ... Where little or no deference is directed by the legislature, the tribunal's decision must be correct. Where considerable deference is directed, the test of patent unreasonableness applies. No single factor is determinative of that test. A decision of a specialized tribunal empowered by a policy-laden statute, where the nature of the question falls squarely within its relative expertise and where that decision is protected by a full privative clause, demonstrates circumstances calling for the patent unreasonableness standard. By its nature, the application of patent unreasonableness will be rare. A definition of patently unreasonable is difficult, but it may be said that the result must almost border on the absurd. Between correctness and patent unreasonableness, where the legislature intends some deference to be given to the tribunal's decision, the appropriate standard will be reasonableness. In every case, the ultimate determination of the applicable standard

> of review requires a weighing of all pertinent factors: see Pushpanathan, supra, at para. 27.
>
> (Emphasis added)

**39** In Voice Construction, the Supreme Court noted the legislation shielded the decisions of arbitrators from review to some extent, but not with a full privative clause. The Court also noted that the existence of numerous cases imposing a standard of patent unreasonableness in reviewing decisions of labour arbitrators, but nevertheless concluded that a reasonableness simpliciter standard was applicable. The Court found that the interpretation of contracts is within the normal expertise of courts, although labour arbitrators have special expertise in collective agreements, which favours "a certain degree of curial deference": per Major J. at para. 27.

**40** On the issue of the nature of the legislation, Major J. noted the difference between the Labour Relations Board (which is more policy based) and a labour arbitrator (who decides disputes between parties). He held at para. 28:

> The LRC [Alberta Labour Relations Code] seeks to regulate and resolve labour disputes in the most efficacious and least disruptive way. Generally, the resolution of labour relations disputes by the Labour Relations Board requires "polycentric" decision making which means it involves a number of competing interests and considerations, and calls for solutions that balance benefits and costs among various constituencies: see Pushpanathan, at para. 36. By contrast, proceedings before an arbitrator do not require the consideration of broad policy issues. Instead, the role of the arbitrator is to resolve a two-party dispute. In this appeal, that dispute related to the employer's obligation to hire dispatched workers. Even so, this factor suggests a deferential standard of review.

**41** Finally, the Court in Voice Construction examined the nature of the question before the arbitrator, concluded that the interpretation of the collective agreement was a question of law, and held, at para. 29:

> Generally speaking, questions of law are subjected to a more searching review than are other questions, and frequently require the standard of correctness. Nevertheless, the interpretation of collective agreements, as noted in para. 27, is at the core of an arbitrator's expertise and this, in turn, points to some deference.

**42** The Supreme Court of Canada's decision in Barrie Public Utilities v. Canadian Cable Television Association (2003), 225 D.L.R. (4th) 206 is also instructive. In that case the CTRC had interpreted the words "supporting structure of a transmission line" in a particular way, which supported its order that cable television companies could attach their cables to distribution poles owned by electric power utilities. The Supreme Court of Canada held that the appropriate standard of review for this particular question was correctness. The Court described the question as one of "statutory interpretation" and held, at para. 16:

> Deference to the decision maker is called for only when it is in some way more expert than the court and the question under consideration is one that falls within the scope of its greater expertise (Dr. Q., at para. 28). In my view, this is not such

> a case. The proper interpretation of the phrase "the supporting structure of a transmission line" in s. 43(5) is not a question that engages the CRTC's special expertise in the regulation and supervision of Canadian broadcasting and telecommunications. This is not a question of telecommunications policy, or one which requires an understanding of technical language. Rather, it is a purely legal question and is therefore, in the words of La Forest J., "ultimately within the province of the judiciary" (Ross v. New Brunswick School District No. 15, [1996] 1 S.C.R. 825, at para. 28). This Court's expertise in matters of pure statutory interpretation is superior to that of the CRTC. This factor suggests a less deferential approach.

**43** In addressing the nature of the question, the Supreme Court again stated that the problem was a "purely legal one" and noted that it was a "question of general importance to the telecommunications and electricity industries", which was a factor in determining that this was "not a case calling for deference to the decision of the CRTC": Barrie Public Utilities at paras. 18-19.

**44** I turn then to the application of the Pushpanathan principles to the particular circumstances of this case. At the heart of the Tribunal's initial decision is a question of statutory interpretation which is not outside the normal expertise of the courts. Therefore, less deference is required than would otherwise be the case. That said, the provision in question must be interpreted within the context of the Act as a whole, and the Tribunal unquestionably has special expertise in that area relative to the Court. The presence of a privative clause, the nature of the legislation and of the particular provision involved also support a deferential standard of review. Notwithstanding that the question before the Tribunal was largely legal in nature, the other factors mandate a level of deference beyond correctness. The Tribunal was interpreting its home statute and its decision had policy implications as well as the determination of the rights of parties before it.

**45** In my opinion, the question of statutory interpretation that was before the Tribunal in this case requires a more deferential standard than the issue of interpreting a release (which was before the Tribunal in Bucyrus Blades and which was found to attract a standard of correctness). The nature of the question, within the context of the legislation and policy elements involved, is somewhat similar to the situation in Voice Construction. Statutory interpretation is a matter not unfamiliar to courts (as is the interpretation of contracts), but the Tribunal here has special expertise to apply to that process (like a labour arbitrator interpreting a collective agreement). The Tribunal was essentially resolving a dispute between parties (the employer and its employees/union), as is the case with a labour arbitrator interpreting a collective agreement. I recognize, however, a major distinguishing factor between this case and Voice Construction is the existence of a strong privative clause, implying a greater level of deference.

**46** There are also similarities between this case and the Barrie Public Utilities case in which the Supreme Court of Canada imposed a standard of correctness. However, the question before the CTRC in that case was somewhat more tangential to its core expertise than is the question before this Tribunal. Also, there was a right of appeal in the governing legislation, whereas the CRTC is protected by a privative clause. Therefore, a level of deference higher than correctness is called for here.

**47** There will no doubt be cases in which decisions of the Pay Equity Tribunal will be entitled to the highest level of deference, as for example where its decision is policy-laden and squarely within its core expertise under the legislation. In this case, however, the nature of the question be-

fore the Tribunal tips the scales away from that most deferential of standards. In my view, the standard of review for the initial decision is reasonableness simpliciter.

**48** With respect to the reconsideration decision, the issue of whether the amendment to the Regulation is retrospective in effect is a pure question of law. The Tribunal is required to be correct on that point. On the other issues, the Tribunal was exercising discretion with respect to issues already before it in the initial decision. This Court ought not to interfere with that discretion unless it is patently unreasonable.

E. PRINCIPLES OF STATUTORY INTERPRETATION

**49** The central and determinative issue in this case is one of statute interpretation. Various principles of statute interpretation arise, and all must be considered in conjunction to arrive at the proper construction of the provisions in question.

Overarching Principles and The Interpretation Act

**50** The starting point for any exercise of statutory interpretation is the Interpretation Act itself, R.S.O. 1990 c. I-11, and in particular in this case, s. 10 which states:

> 10. Every Act shall be deemed to be remedial ... and shall accordingly receive such fair, large and liberal construction and interpretation as will best ensure the attainment of the object of the Act according to its true intent, meaning and spirit.

**51** Elmer Driedger synthesized the overarching principles of statutory interpretation as follows in Construction of Statutes (2nd Ed. 1983) at p. 87:

> 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.

**52** Needless to say, all of the elements identified by Mr. Driedger do not always coincide, such that sometimes, for example, the ordinary words are not harmonious with the object of the Act, or with the intention of Parliament. Resort must often be had to some rules of special application.

Liberal Purposive Construction

**53** The Pay Equity Act is human rights legislation, remedial in nature, and as such must be given a broad and liberal construction consistent with its purpose: Ontario (Human Rights Commission) v. Simpsons Sears Ltd., [1985] 2 S.C.R. 536. Thus, although courts must be guided by the plain meaning of the words used in such legislation, they "should not search for ways and means to minimize those rights and enfeeble their proper impact": CNR v. Canada (Human Rights Commission), [1987] 1 S.C.R. 1114, at para. 24.

**54** Generally speaking, where words are open to more than one interpretation, courts should choose the one that advances the remedial purpose of human rights legislation. Thus, provisions granting or extending rights should be read generously; provisions restricting those rights should be read strictly: Berardinelli v. Ontario Housing Corp. (1978), 90 D.L.R. (3d) 481 (S.C.C.).

Intention of the Legislation

**55** As a general rule, the intention of the legislation is to be gleaned from the words used in the provision at issue, when seen within the context of the legislation itself. Where the language used is plain and unambiguous, there is generally no basis for looking outside the legislation to determine its intention.

**56** The objective of statutory interpretation, however, is to achieve what the legislature intended, if that can be done without unduly straining the language used. Judges used to be reluctant to consider outside sources, such as legislative debates, as an aid to interpreting statutes. However, in more recent years, particularly in constitutional cases, many courts have recognized the usefulness of historical evidence, including legislative debates, in determining the purpose and intent of legislation. The Supreme Court of Canada held in Rizzo & Rizzo Shoes Ltd. (Re), [1998] 1 S.C.R. 27, at para. 31, that "the use of legislative history as a tool for determining the intention of the legislature is an entirely appropriate exercise." The Court further held at para. 35:

> Although the frailties of Hansard evidence are many, this Court has recognized that it can play a limited role in the interpretation of legislation. Writing for the Court in R. v. Morgentaler, [1993] 3 S.C.R. 463, at p. 484, Sopinka J. stated:
>
> > ... until recently the courts have balked at admitting evidence of legislative debates and speeches ... The main criticism of such evidence has been that it cannot represent the "intent" of the legislature, an incorporeal body, but that is equally true of other forms of legislative history. Provided that the court remains mindful of the limited reliability and weight of Hansard evidence, it should be admitted as relevant to both the background and the purpose of legislation.

**57** Thus, in determining the intention of the legislation it may be helpful for a decision maker to look at historical sources such as legislative debates, provided of course that the references are relevant and the decision maker remains mindful of weight and reliability.

**58** Finally, it should also be noted that extrinsic evidence may be admissible to demonstrate that there is a latent ambiguity in statutory language which appears on its face to be clear and straightforward. The following excerpt from Leitch Gold Mines Ltd. v. Texas Gulf Sulphur Co. (Incorporated), [1969] 1 O.R. 469 (H.C.J.) at p. 524, deals with the admission of extrinsic evidence to interpret a contract but is, in my opinion, equally applicable to statutory interpretation:

> Extrinsic evidence may be admitted to disclose a latent ambiguity, in either the language of the instrument or in its application to the facts, and also to resolve it, but it is to be noted that the evidence allowed in to clear up the ambiguity may be more extensive than that which reveals it. Thus, evidence of relevant surrounding circumstances can be accepted to ascertain the meaning of the document and may clarify the meaning by indirectly disclosing the intention of the parties.

The Absurdity Rule

**59** Statutory terms ought not to be interpreted in a manner that would create an absurd result. Dreidger on the Construction of Statutes, 3rd ed. (Toronto: Butterworths, 1994) states (at p. 85-86) that the modern absurdity rule may be summarized by the following propositions:

(1) It is presumed that legislation is not intended to produce absurd consequences.
(2) Absurdity is not limited to logical contradictions and internal incoherence; it includes violations of justice, reasonableness, common sense and other public standards. Also, absurdity is not limited to what is shocking or unthinkable; it may include any consequences that are judged to be undesirable because they contradict values or principles that are considered important by the court.
(3) Where the words of the legislative text allow for more than one interpretation, avoiding absurd consequences is a good reason to prefer one interpretation over another. Even where the words are clear, the ordinary meaning may be rejected if it would lead to an absurdity.
(4) The more compelling the reason for avoiding the absurdity, the greater the departure from the ordinary meaning that may be tolerated. However, the interpretation that is adopted should be plausible.

**60** The general rule that statutes be given there "ordinary meaning" is subject to the limiting application of the absurdity rule in order "to prevent unjust and unreasonable consequences". Thus, the ordinary meaning of words used may be rejected, even if it is plain, in order to avoid absurd consequences: Axa Insurance v. Ahmed Nuur (2000), 52 O.R. (3d) 70 (S.C.J.).

**61** Dreidger notes that one of the most frequently recognized forms of absurdity is an interpretation of a provision which would result in "irrational distinctions". Thus, a particular interpretation should be avoided if it would result in persons "receiving different treatment for inadequate reasons, or for no reason at all": Dreidger on the Construction of Statutes, ibid, at p. 86. Dreidger cites a number of cases which have applied this principle, including the Supreme Court of Canada decision in Hills v. Canada (Attorney-General) (1988), 48 D.L.R. (4th) 193 (S.C.C.) in which the issue was whether a member of a union whose union dues were used, in part, by the international union to pay strike pay to other workers could be said to have "financed" the strike, such that he would be disentitled to unemployment benefits under the applicable legislation. The Supreme Court observed that union dues might be administered by the international union "out of sheer convenience" and could just as well have been administered by the local union to which the applicant belonged or kept in a separate account. If the latter had happened, then the applicant could certainly not be said to have "financed" the strike. The Court therefore chose to interpret "financed" as having a direct or deliberate element, stating (at p. 226), "Could the legislature really have intended disentitlement to be dependant upon such a trivial fact? I think not."

**62** The decision of the Supreme Court of Canada in Berardinelli v. Ontario Housing Corp., supra, provides another illustration of this principle. In that case, the plaintiff had sued the owner of his housing complex for damages sustained when he slipped and fell because of ice and snow on the common areas of the complex. The complex was owned by the Ontario Housing Corporation under the authority of the Housing Development Act, R.S.O. 1970, 213, which gave Ontario Housing the statutory power and duty "to plan, construct and manage any building development". Ontario Housing took the position that in managing this complex it was exercising a statutory power and as such was protected by a six-month limitation period under the Public Authorities Protection Act, R.S.O. 1970, c. 374, which applied to acts done in execution "of any statutory or other public duty". The Ontario Court of Appeal had held that Ontario Housing was acting in execution of its statutory duty to manage the building and any default in that duty (as, for example, the failure to properly clear ice and snow) was subject to the protection of the six-month limitation period. This was re-

versed by the Supreme Court of Canada based, in part, on the illogical consequences of such an interpretation. Estey J. (writing for the majority), held at p. 492:

> The Court is here confronted with at least two possible, but quite different interpretations of s. 11. The one would impose on all actions involving the execution of powers undertaken pursuant to s. 6(2) of the Housing Development Act, however minor or miniscule, the protection of the limitation period established by s. 11. The imposition of this limitation period for this special class would have the direct result of producing two categories of housing units in the community: the one operated by persons having a statutory mandate to which a six-month limitation period would extend; and the other operated by a person without statutory authority to which the general limitation period would apply. Of course both housing projects would appear identical in fact to the attending public whose rights are directly affected by the distinction.
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> (emphasis added)

**63** In order to prevent this seemingly irrational distinction, the Supreme Court of Canada adopted an interpretation of the language in the statute that went beyond its literal, plain meaning and held the six-month limitation period would only apply to acts taken under a statutory power which had a public aspect or connotation. The Court reasoned that to do otherwise would "create different conditions of owner liability for two apparently similar housing facilities": Berardinelli at p. 495.

**64** A similar rationale prompted the Supreme Court of Canada to reject a strict and literal interpretation of certain provisions of Ontario's Employment Standards Act in Rizzo & Rizzo Shoes Ltd. (Re), supra. The legislation provided that employees whose employment was "terminated by an employer" were entitled to specified termination pay. At issue was whether employees who lost their jobs when a creditor petitioned the employer into bankruptcy were terminated "by the employer", or rather by operation of law. The Supreme Court acknowledged that the "plain meaning" of the words used would appear to suggest that the bankruptcy situation did not fit within the provision, as had been found by the Court of Appeal. However, Iacobucci J. (writing the unanimous decision of the Supreme Court) went on to apply the absurdity rule to this situation, stating that "an interpretation can be considered absurd if it leads to ridiculous or frivolous consequences" or "if it is extremely unreasonable or inequitable": para. 27. If the termination pay provisions did not apply to a bankruptcy situation, employees terminated the day before the bankruptcy would be entitled to the payments, whereas those kept on (ironically, likely the most senior employees) would not. In order to avoid the absurdity of that consequence, the Court interpreted the term "terminated by the employer" to include a situation in which the employee was terminated as a result of the bankruptcy of the employer.

The Presumption Against Retrospective Effect

**65** Statutes are presumed to look forward from the date of their enactment and to affect only rights in the future. There is a presumption against interpreting a statute as having retrospective effect unless the statute stipulates this is to be the case or such an interpretation arises by necessary implication. Declaratory statutes are an exception to the general rule against retrospective or retroactive effects. Declaratory statutes are those meant to remove doubt as to the common law or the

meaning or effect of a statute. However, it must still be clear that a retrospective effect is intended: Quebec (Attorney General) v. Healey, [1987] 1 S.C.R. 158.

**66** The mere fact that a statutory amendment follows a judicial or quasi-judicial interpretation of that statute is not sufficient, in and of itself, to require a retrospective interpretation of the amendment. On the contrary, s. 17 of the Interpretation Act states, "The repeal or amendment of an Act shall be deemed not to be or to involve any declaration as to the previous state of the law."

**67** In Rizzo & Rizzo Shoes Ltd. (Re), (see para. 64 above), the legislation was amended after the Rizzo bankruptcy, but before the appeal was heard in the Supreme Court of Canada. The amended version of the legislation specifically provided that where employment is terminated by operation of law as a result of the bankruptcy of the employer, the employer will be deemed to have terminated the employment. Iacobucci J. noted the fact of this amendment at para. 42 of his Reasons, then cited s. 17 of the Interpretation Act and stated, "As a result, I note that the subsequent change in the legislation has played no role in determining the present appeal."

F. ANALYSIS

**68** I turn now to consider whether the Tribunal's interpretation of the Act in this case can stand.

Reconsideration Decision

**69** On reconsideration, the Tribunal determined that the amendment to the public sector definition in the Act did not have retrospective application. On this issue, which is a pure question of law, the Tribunal was required to be correct. In my view, the Tribunal was correct on this point.

**70** The amendment does not specifically state that it is to have retroactive effect. It is worth noting that the Act specifically contemplates the possibility of some Regulations having retroactive effect in s. 36(2), which states, "(2) Retroactivity - A regulation made under clause (1)(f.1) [not at issue here] is, if it so provides, effective with reference to a period before it was filed." (emphasis added)

**71** Further, there is no necessary implication that the provision was intended to be applied retrospectively. Given the timing of the amendment, it may well be logical to conclude that the Legislature was responding directly to the Tribunal's initial decision in this particular case. However, it does not necessarily follow that the Legislature thereby intended to affect all those cases already resolved prior to the amendments and alter the rights of employees and employers prior to that time. It was open to the Legislature to specify retroactive application. It did not do so. There is some merit to the applicant's argument that the language used in the amendment suggests a declaratory intent. It is not a completely new definition. Rather, there is simply an addition to it preceded by the words "but for greater certainty". However, I do not see such wording as sufficient to take this out of the application of s. 17 of the Interpretation Act. In my view, the Supreme Court of Canada's decision in Rizzo Shoes is directly applicable. The amendment to the legislation cannot be deemed to have any declaratory effects as to the previous state of the law, and the Reconsideration Tribunal ought not to have taken it into account.

**72** There is no need to consider whether the Reconsideration Tribunal erred in failing to reverse its earlier decision as being wrong in law. Apart from the amendment to the legislation, there was nothing before the Tribunal that had not been part of the earlier hearing. The real issue, therefore, is whether the Tribunal's initial decision can stand.

The Tribunal's Initial Decision

**73** The nub of this case is the Tribunal's interpretation of the definition of "public sector employee". On this point, the Tribunal's interpretation must be reasonable. It is not required to be correct. Further, the issue is not whether I would have decided the point in the same manner, or whether there are other interpretations of the provision that might, in my view, be more reasonable than the one chosen by the Tribunal. If the Tribunal's interpretation is a reasonable one that can be rationally supported by the legislation, that is sufficient. An unreasonable decision is one that "is not supported by any reasons that can stand up to a somewhat probing examination": Law Society of New Brunswick v. Ryan, [2003] 1 S.C.R. 247 at paras. 48-56; Canada (Director of Investigation and Research) v. Southam, supra. As stated by Iacobucci J. in Ryan at para. 55:

> A decision will be unreasonable only if there is no line of analysis within the given reasons that could reasonably lead the tribunal from the evidence before it to the conclusion at which it arrived. If any of the reasons that are sufficient to support the conclusion are tenable in the sense that they can stand up to a somewhat probing examination, then the decision will not be unreasonable and a reviewing court must not interfere (see Southam, at para. 56). This means that a decision may satisfy the reasonableness standard if it is supported by a tenable explanation even if this explanation is not one that the reviewing court finds compelling (see Southam, at para. 79).

**74** In my view, the Tribunal reached a reasonable conclusion that Caressant Care was the "employer" of the employees in the retirement home. Typically the pay equity jurisprudence on determining who is the "employer" for purposes of pay equity has arisen in a different context, usually where a large employer seeks to argue that smaller divisions or branch operations are the actual employer. Notwithstanding this different context, it was not unreasonable for the Tribunal to conclude in this case that the same corporation was the actual employer for both parts of the business and should be treated as the "employer" for purposes of pay equity.

**75** Similarly, the Tribunal was reasonable in determining that both the retirement home and the nursing home were part of the same "establishment" as that term is used in the legislation, referring to a geographic region. Again, the issue arises in a somewhat different context in this case, but the Tribunal was reasonable in taking a consistent approach and applying the established jurisprudence on the point.

**76** Where the problem arises is in the Tribunal's determination that a strict interpretation of the term "public sector employer" was appropriate and that once an employer was found to be a public sector employer in any aspect of its business, it was a public sector employer for all purposes under the Act and with respect to all of its employees in the relevant geographic boundaries. The Tribunal itself identified the consequences of that determination at para. 90 when it noted, "Consequently, if a single legal entity operates a gas station, a retirement home, and a pizza parlour within the same municipality, the workers of all three comprise the employer's establishment." Since all of these would be in the private sector, this is not problematic. However, if one adds a nursing home to the businesses owned by that legal entity, the same result applies. All will be part of the same establishment for pay equity purposes, and all will be deemed, on the Tribunal's interpretation, to be part of the public sector. Thus, the pizza parlour employees and the gas station attendants will be compared, for pay equity purposes, to the employees of hospitals or municipalities. This, in my opinion, creates an absurd result in that it is perfectly clear that a pizza parlour is not part of the broader public sector and was never intended to be treated as such.

**77** The Act, as noted by the Tribunal, makes distinctions between public and private sector employers in various ways. One of the consequences of the Tribunal's interpretation of "public sector employer" is to bring within the ambit of the public sector aspects of the Act, businesses and employees who are plainly not part of the public sector, no matter how one would logically define it. It therefore sets up a completely artificial designation, deeming businesses and employees to be in the public sector, when common sense would say otherwise. In this instance a private sector retirement home will be forced to use a proxy method of comparison designed to be used only for public sector employers for the sole reason that the owner of the retirement home also happens to own a nursing home in the same area. At the same time, that retirement home's competitors will not be treated in the same manner unless they also have common ownership with a nursing home. There are 500 retirement homes in Ontario and only 70 of those owners also own a nursing home. The remaining 430 retirement home owners will be treated as private sector employers in respect of their retirement home business; the other 70 will be treated as public sector employers. In my view, this is an irrational distinction based on "sheer coincidence", similar to the situation before the Supreme Court of Canada in Hills v. Canada (Attorney-General).

**78** The Tribunal's interpretation may also create an extremely unfair result for the employer. For example, a company that has a total of 1000 employees in its retirement homes and only 10 employees in a small nursing home section would be treated as a public sector employee for all purposes and all employees, merely because it holds a nursing home license in respect of a small portion of its business. The employer receives no government funding for the retirement home salaries, but must nevertheless be compared to government-funded nursing homes for purposes of setting salaries in the retirement home. The retirement home facilities are private for-profit entities competing against other retirement homes in the province, of which there are hundreds. However, operators of retirement homes who do not also have a nursing home license will not be subject to such a requirement. That is not a level playing field, particularly since the employer whose private sector retirement home is brought into the public sector aspects of the Act will not have the government funding that goes with that public sector status. The Tribunal's interpretation creates different conditions for owners of retirement homes depending on whether or not they also happen to own a nursing home (or, for that matter, any other facility listed in the Appendix). This is precisely the result that the Supreme Court in Berardinelli sought to avoid.

**79** Also, on the Tribunal's strict reading of the definition, it would apply only to the "corporation" that holds the nursing home license. Therefore, business owners who have incorporated separate entities for their nursing home facilities would not have their other businesses caught by the Tribunal's interpretation of the definition. This would result in a different application of the pay equity rules based solely on corporate organization, with businesses having both operations under the same corporation being subject to an entirely different pay equity methodology than businesses with separate corporate structures.

**80** The absurd consequences of a literal reading of the section assumes even greater significance when examined in light of the intention of the legislation and of the provision in particular. The Tribunal refused to consider extrinsic evidence to inform its interpretation of the section, maintaining that the provision was clear and unambiguous. However, even looking simply at the legislation, it is apparent that this interpretation is at odds with the scheme of the Act. The legislation draws clear distinctions between private sector and public sector employers and stipulates that the proxy method of comparison applies only to public sector employers. It is also part of the scheme of the Act to compare "like" to "like". There is a fundamental absence of logic and fairness in com-

paring a private retirement home to a publicly run and funded nursing home. Given this context and the odd consequences of a literal interpretation, it was incumbent upon the Tribunal to consider whether there was any extrinsic reliable evidence to serve as a guide to interpretation. To refuse to even consider such evidence was, in my view, unreasonable.

**81** In Service Employees International Union, Local 204 v. Ontario (Attorney General) (1997), 35 O.R. (3d) 508 (Div.Ct.), this Court had occasion to consider the proxy method provisions of the Act, although in a different context. The issue in that case was the constitutionality of a 1996 amendment to the Act, which purported to cap proxy pay equity payments at 3% of payroll and to eliminate the proxy method of comparison for future adjustments. In the course of its decision, however, the Court considered the genesis of the proxy method of comparison and what it was intended to achieve. The Court noted that prior to the introduction of the proxy method, comparisons were only made between job classes within the same organization. This did not work for organizations that had no male job classes to be used as a comparison. The proxy method therefore permitted comparisons between organizations. The Court then (at page 512) cited the following excerpt from a January 1989 Report from the Pay Equity Commission to the Minister of Labour:

> The effectiveness of proxy comparisons in providing redress for predominantly female sectors would depend on how far it is extended. Potentially, this approach could be used for all target sectors. However, an effective argument for allowing proxy comparisons can be made more easily for broader public sector organizations than for private sector organizations ... organizations in ... [the broader public] sector are closely connected to the provincial government via funding, regulation and legislation ...

**82** In a later report in October, 1989, the Pay Equity Commission stated, at p. 54, that the proxy method was only feasible for the public sector. At p. 76 of the same report it stated that "proxy comparison was not acceptable to the private sector.": S.E.I.U., Local 204, at p. 513.

**83** In 1993, the Legislature proposed Bill 102 to amend the Act to add, among other things, the proxy method of comparison. The Bill was introduced into the House on November 26, 1992, by the Hon. Bob Mackenzie, who stated at the time, "Proxy is designed to be used only in the broader public sector and only after all other methods of achieving pay equity have been attempted.": Ontario, Legislative Assembly, Standing Committee on Pay Equity in Debates, No. 86 (26 November 1992) at 3533.

**84** On May 12, 1993, Ms Sharon Murdock (the Member for Sudbury) moved third reading of the Bill. In her speech at that time she stated, "I can't help but reinforce that the proxy provision under Bill 102 does not go to the private sector - it only applies to the public sector." On June 7, 1993, Ms Murdock is quoted in Hansard as stating, "In terms of proxy, for instance, the proxy method of comparison only applies to the private sector; it doesn't apply to the private sector at all, so that's important.": Ontario, Legislative Assembly, Standing Committee on Pay Equity in Debates, No. 18 (12 May 1993) at 732 and No. 28 at 1221.

**85** These excerpts from Hansard are consistent and were made by Members with responsibility for explaining the legislation to the House. Further, they echo the Commission's own report and recommendations to the Minister. These are highly reliable sources as to the intention of the Legislature in respect of the application of the proxy method of comparison. It is clear the proxy method was never intended to apply to the private sector, and even more certainly, was never contemplated

to force a privately operated and funded business to use the proxy method to compare its employees to government employees in publicly funded facilities. These comments are also consistent with the scheme of the legislation generally.

**86** It was, therefore, particularly unreasonable for the Tribunal to insist on a rigid, literal reading of the provision in question when reliable sources were available to facilitate an interpretation more in keeping with the intention of the legislation. It is apparent when one looks at the Debates that it was never contemplated that a private business such as a retirement home would find itself in this situation. This creates an uncertainty about the meaning of the provision that ought to have required the Tribunal to look further for its meaning. When this is considered together with the absurdity of the consequences and the unfairness of their application, it is not possible, in my view, to characterize the Tribunal's interpretation as a reasonable one.

**87** I recognize that the Act seeks to address systemic discrimination against women and as such should be given a liberal interpretation consistent with that purpose. Obviously, extending pay equity to more, rather than fewer, female employees does advance the objectives of equality for those women. However, that does not mean that an interpretation should be given to provisions of the legislation which results in unfair consequences for some employers not imposed on other employers running exactly the same business. The obligations to advance equal rights for women should be imposed equally. Putting a heavier burden on private sector employers who also happen to own a nursing home is an unfair application of the law and cannot be justified if an interpretation in keeping with the intention of the legislation is available.

**88** The Tribunal recognized what was necessary to interpret the section in order to avoid this result. It stated at para. 95 that to give effect to the Applicants' position would require it to "read language into the Schedule so that a corporation is part of the public sector if it operates a nursing home pursuant to a licence 'but only to the extent of its nursing home operations'." In my opinion, that is, in fact, the only interpretation which would give effect to the intention of the provision and avoid an absurd result. A reasonable interpretation of the legislation requires that such a qualifier be read into it, and the Tribunal's failure to do so cannot be sustained.

**89** Counsel for the Union submitted that the Tribunal had decided, alternatively, that the operations of the retirement home and nursing home were so intertwined that it was not possible to segregate them for purposes of a pay equity plan. The Tribunal made no such finding. The Tribunal did comment on some overlapping of personnel and functions. However, that was merely by way of background. It is apparent from the Tribunal's Reasons that its finding of public sector status was based entirely on its literal interpretation of the provision. The Tribunal would have reached the same conclusion if the two facilities were miles apart, provided they were still in the same geographic area so as to fall within the same "establishment".

G. CONCLUSIONS

**90** In the result, the Tribunal's decision cannot stand and is therefore quashed. It does not necessarily follow from this that this particular employer is not "public sector" or a "seeking employer" in respect of its nursing home operation. Having applied an improper definition of "public sector employer", the Tribunal concluded that the retirement home fell within that category solely because Caressant Care also owned a nursing home. It was not necessary in that context to look carefully at whether any of the employees or classes of employees at the retirement home were so intertwined with the functions of the nursing home that it was not possible to say they were truly in a different

workplace. This matter is therefore remitted back for a new hearing before a differently constituted Tribunal, which is directed to interpret the term "public sector employer" in accordance with these Reasons. For the sake of clarity, the proper interpretation of that term is consistent with the amended version in O. Reg 37/02. That is not to say that the amendment has retrospective effect. Rather, the amended version is simply a clearer statement of what the provision actually meant all along.

**91** Costs, if sought, will be considered on the basis of written submissions. Counsel for the applicant is requested to coordinate the exchange of submissions amongst counsel and to then deliver three bound sets of the submissions to the Divisional Court office no later than 30 days after the release of these Reasons.

A.M. MOLLOY J.
G.D. LANE J. -- I agree.
P.T. MATLOW J. -- I agree.

cp/e/qlgxc

# Tab 26

*Case Name:*

# Walker Youth Homes Inc. v. Ottawa-Carleton District School Board

**Between**
**Walker Youth Homes Inc., applicant, and**
**The Ottawa-Carleton District School Board, respondent**

[2004] O.J. No. 2307

[2004] O.T.C. 473

131 A.C.W.S. (3d) 439

Court File No. 04-DV-994

Ontario Superior Court of Justice

**Caputo J.**

Heard: April 26, 2004.
Judgment: June 1, 2004.

(67 paras.)

**Counsel:**

David Sherriff-Scott, for the applicant.

Paul A. Webber, Q.C., for the respondent.

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COSTS

**1** CAPUTO J.:-- MM is a 15 year old ward of the crown in the care of the Children's Aid Society of Toronto. The CAS placed MM in the applicant's residence in Ottawa. The applicant attempted to enrol MM with the respondent in the Special Education Program for "exceptional" students. The respondent refused to enrol MM.

**2** This is an urgent application for judicial review to a single judge pursuant to subsection 6(2) of the Judicial Review Procedure Act, R.S.O. 1990 c.J.1 (hereinafter "JRPA") to set aside the March 12, 2004 written decision of the Ottawa-Carleton District School Board (hereinafter "OCDSB") to refuse to register as a pupil within its Board, a 15 year old boy, MM. The application also seeks an order in the nature of mandamus to compel the registration of MM at the OCDSB.

**3** The parties agree that MM has a disability or what the Education Act describes as an exceptionality.

FACTS:

**4** MM is a ward of the crown and is in the "care of the Children's Aid Society of Toronto" (hereinafter "CAS"). In late 2003, the CAS decided that MM should live in the City of Ottawa and to be placed at Walker Youth Homes Inc., the applicant. MM has been residing at Walker Youth Homes since January 21, 2004. He will reside there continuously for the next two years and possibly until his 21st birthday.

**5** The Walker Youth Homes residence where MM lives is within the jurisdiction of the OCDSB. That residence has as its designated tax support, the OCDSB.

**6** On January 21, 2004 and following, the applicant contacted the OCDSB and continuously attempted by way of written correspondence and e-mails to bring about MM's registration. On March 12, 2004 the OCDSB wrote to the applicant refusing to register MM.

**7** Given that MM has a potential disability or "exceptionality" within the meaning of the Education Act, the OCDSB advised that MM would have to wait to some unknown date when the OCDSB considered that it had the placement which MM needed.

**8** MM is a 15 year old boy born June 14, 1998. He was made a ward of the crown and placed "in the care of the Children's Aid Society" of Toronto on May 14, 2003.

> Order of Spence, J., May 14, 2003, Exhibit "A" to the affidavit of Jeffrey Walker, Application Record, Tab 2A.

**9** Late in the Fall of 2003, the CAS determined that it would no longer be appropriate for MM to reside in the City of Toronto and that he should be moved to live for a significant period to Ottawa. CAS workers determined that the most suitable placement for MM was at Walker Youth Homes. One of the reasons which led the CAS to determine that MM should reside outside of the Toronto region was that his current environment was dangerous and subject to gang influence. This had brought MM into contact with the law in the past and such circumstances were considered dangerous and counter-productive for his well-being.

**10** MM's biological father has not been involved in his life for many years and lives in another country. MM's mother does not want to be involved in his life. Therefore, MM's connection with Toronto was slight and the CAS considered it to be in his best interests to have him at Walker Youth Homes. Accordingly, he took up residence at one of the Walker Youth Homes residences at [text deleted by LexisNexis Canada] in Ottawa on January 21, 2004.

**11** In so far as MM voluntarily resided anywhere, he resided at the home of his mother in Toronto. His mother continues to maintain a home in Toronto. Contrary to some evidence presented by the applicant, the independent reports tend to establish that the mother maintains an interest in MM's care and has been co-operative and collaborative.

**12** A court order had placed MM in the "care and custody of the Children's Aid Society of Toronto" (CAST). If the CAST as his "guardian", within the meaning of the Education Act, and the residence of his guardian was a relevant factor in assessing entitlement to admission, the guardian resided in Toronto. MM is not now, and has never been, in the care or custody of the Ottawa Children's Aid Society.

**13** Walker Youth Homes is a residential placement set of homes which deal with difficult adolescent boys. It provides intensive services for their support, care and remediation. It has consulting psychiatrists and psychologists, and extensively trained staff. The children who live at Walker Youth Homes residences are either wards of the CAS or otherwise on probation or in need of residential placements for their care.

**14** Walker Youth Homes also receives transfer children from other provinces who are subject to supervisory orders, or on probation, or in the care of or who are wards of extra-provincial societies equivalent to the Ontario CAS's.

**15** Children who reside at Walker Youth Homes typically live there for one to seven years. When a person lives at Walker Youth Homes, he resides there full time, 24 hours a day, seven days a week. Such children eat, sleep and reside in every sense of the word at Walker Youth Homes from which all other activities are co-ordinated, supervised and controlled. Such children receive full clinical intervention, social skills management, behaviour management and other group therapy and intervention. Their residential placements are highly structured, controlled and supervised not only with respect to general issues, but on day-to-day issues affecting their lives.

**16** The CAS placed MM in the Walker Youth Homes facility on [text deleted by LexisNexis Canada]. MM began residence at the [text deleted by LexisNexis Canada] home on January 21, 2004 and he has resided there continuously since that date. He sleeps, eats and resides in every sense of the word at that location. He will reside there until not earlier than January 21, 2006 with a possible extension of that time to his 18th birthday and thereafter possibly until his 21st birthday.

**17** On January 21, 2004 Jeffrey Walker, the Chief Executive Officer at Walker Youth Homes began an extensive e-mail and written correspondence with the OCDSB asking that MM be registered as a pupil immediately. Mr. Walker gave all available information in his possession to the OCDSB. Mr. Walker wrote if not daily, then on a weekly basis, requesting the status of OCDSB deliberations with respect to MM. No meaningful response was received from the OCDSB for nearly two months.

**18** More facts will be discussed when dealing with the issues.

ISSUES:

**19** There are two issues in this judicial review:

1) Is MM a child residing in the school district of the respondent and as such, entitled to be enrolled as a pupil with the respondent;
2) If so, can the respondent exclude MM from attending a school under its jurisdiction.

LAW:

Jurisdiction:

**20** The parties agree I have jurisdiction to hear this applicant on an urgent basis pursuant to S. 6(2) of the Judicial Review Procedure Act.

Issue #1: Resident issue:

**21** The issue is what is the correct definition of the word "reside" in the legislation?

**22** Section 47(2) of the Education Act: "Admission of ward, etc., of Children's Aid Society or training school to a secondary school - A child who is a ward of a Children's Aid Society, is in the care of a Children's Aid Society or is a ward of a training school, and who is otherwise qualified to be admitted to a secondary school, shall be admitted without the payment of a fee to a secondary school operated by the board of the secondary school district or separate school zone, as the case may be, in which the child resides."

**23** The rights of a child to attend a particular school is governed by Part II of the Education Act.

**24** Section 32(1) "Resident pupil right to attend school - A person has the right, without payment of a fee, to attend a school in a school section, separate school zone or secondary school district, as the case may be, in which the person is qualified to be a resident pupil."

**25** The word "resides" is not defined in the Education Act.

**26** Cases for over a hundred years have given the word 'resident' its plain meaning, i.e., where one actually resides - where an individual eats, drinks and sleeps.

Ex Parte Miller (1897), 34 N.B.R. 318 (C.A.)

Ex Parte Lambert (1931), 1 M.P.R. 12 (C.A.)

Toronto East General & Orthopaedic Hospital v. Ontario (County), [1947] 2 D.L.R. 766 (C.A.)

**27** In L.(T.I.) v. F.(J.L.) (2001), 197 D.L.R. (4th) 721 (Man. C.A.), it was said of adoption proceedings in a Manitoba statue:

> "There is no definition in the Act for the word 'reside', and there is nothing throughout the Act to indicate that anything other than the normal meaning should be attributed to that word."
>
> "...Had the Legislature intended that anything other than the ordinary residence of the applicants or the child determine jurisdiction, it would have so stated."

**28** See also, Procureur General de Quebec Commissaires d'Ecoles la municipalities de Mirabel, [1944] C.S. 299 @ p. 300 where the Quebec Superior Court issued an order for mandamus to force the registration of a child in a school system. The court dealt with the question of a child's residence when placed pursuant to the Child Protection and Tuberculosis Act, R.S.Q. 1941 c. 191, s. 5. In that case, the court held that:

> "Where a Child Family Placement Service, established under the Act, places children with families living within a school district, the commissioners, by Section 5 of the Act, are bound to admit those children to their school in the same

way as children actually resident within the district. If they refuse to do so, after having been required, mandamus will issue to compel them."

**29** The respondent submits that the words "in which the child resides" does not include mandatory placement in a home. The respondent in its factum listed three cases which all relate to circumstances where amendments were made to planning acts to allow to rezone constructions of group homes for juvenile offenders pending disposition of criminal proceedings or in fulfilment of their sentences after convictions.

**30** In these cases definitions of group homes were involved. The principles of the case involve consideration of whether persons were living in any similarity to a normal family residence and whether a mandatory placement as part of a criminal sentence is encompassed by the word "resides".

**31** The parties are not ad idem as to the correct definition of guardian as there are two in the Education Act. Section 1(1) defines guardian as a person who has lawful custody of a child, other than the parent. Section 18 in Part II of the Education Act for the purposes of specified section defines guardian as including, in addition to the definition in S. 1(1), a person who has received into his or her home, a child of compulsory school age.....who is in his care. The specified sections relate to enrolling children in school.

**32** Section 30 provides that a guardian who neglects or refuses to cause a child to attend school is guilty of an offence.

**33** I find that the definition of guardian is not determinative of the issue of determining the residence of MM.

CONCLUSIONS:

**34** The respondent submits that the legislation is complex and there are risks in addressing this issue if it is obiter.

**35** In determining the need to address this issue and properly interpret the meaning of the words "in which the child resides", in my opinion I have to consider the Special Education Regime enacted by the Education Act and Regulations.

**36** The Court of Appeal in the case of Bonnah addressed the Statutory and Regulatory Scheme under the Education Act. At page 460, Doherty, J. for the court said as follows:

> "The Act and regulations provide a comprehensive scheme for the identification and placement of exceptional pupils. Broadly stated, the provisions for a committee which identifies exceptional pupils and determines, hopefully with the co-operation of school authorities and parents, the appropriate placement for those students who are identified as exceptional pupils. Placement decisions are subject to two levels of appeal at the instance of the parents.
>
> The phrase "exceptional pupil" first appeared in the Education Act in 1980: The Education Amendment Act, 1980, S.O. 1980, c.61. An "exceptional pupil" is defined as:

> ...[A] pupil whose behavioural, communicational, intellectual, physical or multiple exceptionalities are such that he is considered to need placement in a special education program...

The key provision in the Act is s. 8(3):

> 8(3) The Minister shall ensure that all exceptional children in Ontario have available to them, in accordance with this Act and the regulations, appropriate special education programs and special education services without payment of fees by parents or guardians resident in Ontario, and shall provide for the parents or guardians to appeal the appropriateness of the special education placement, and for these purposes the Minister shall,
>
> (a) require school boards to implement procedures for early and ongoing identification of the learning abilities and needs of pupils, and shall prescribe standards in accordance with which such procedures be implemented; and
> (b) in respect of special education programs and services, define exceptionalities of pupils, and prescribe classes, groups or categories of exceptional pupils, and require boards to employ such definitions or use such prescriptions as established under this clause.
>
> Ontario Regulation 181/98, as amended by O. Reg. 137/01, entitled "Identification and Placement of Exceptional Pupils" puts flesh on the statutory bones of s. 8(3) of the Act. Section 10 provides for the creation of the IPRC. Section 14 sets out the manner in which a pupil may be referred to IPRC for a determination of whether that pupil should be identified as an exceptional pupil. If the pupil is so identified, the IPRC will make a placement decision. Sections 15 and 16 describe the nature of proceedings before the IPRC and the material that it may consider."

**37** The process starts for an exceptional student with enrolment in a secondary school.

**38** The respondent concedes that if MM is not enrolled as a student with the respondent, he will be denied access to the Special Education Program, at least in Ottawa.

**39** In fact, MM would be denied access to the Special Education Program anywhere.

**40** The Children's Aid Society of Toronto, being the caregiver to MM, under court order, decided the appropriate "residence" should be with the applicant in Ottawa. It is inconceivable to me that the Children's Aid Society Toronto or the applicant could enrol MM in a secondary school in Toronto while he is placed with the applicant in Ottawa.

**41** When considering the meaning and effect of S. 267.5(7) and (9) there are two applicable principles of statutory interpretation. The first is the plain meaning rule. The second is that statutory provisions are to be read in their grammatical and ordinary sense harmoniously with the objective of

the legislation (for further discussion see Walmer Development v. Wolch, [2003] O.J. No. 3435 (Div. Ct.) at para.27)

**42** The court must give effect to the words used when the meaning of the words used is plain and no ambiguity arises from the context. The words offer the best indicator of Parliament's intent (Will-Kare Paving Construction Ltd. V. Canada, [2000] 1 S.C.R. 915, 188 D.L.R. (4th) 242 (S.C.C.) per Binnie at para. 54 and R. v. McIntosh, [1995] 1 S.C.R. 686 per Lamer at page 697).

**43** However, on the other hand, competing statutes are to be interpreted in a way that avoids any absurd or inconsistent result. It should not be readily assumed that the legislature intends an unreasonable result or to perpetrate an injustice or absurdity. (see: Re Estrabrooks Pontiac Buick Ltd. (1982) 44 N.B.R. (2d) 201 (C.A.) at para 21).

**44** If a statute is susceptible of two interpretations, the interpretation that avoids absurdity is to be preferred. (Datacalc Research Corporation v. Her Majesty the Queen, [2002] T.C.J. No. 99 (Tax Ct. of Canada) at para 54).

**45** According to F. Bennion, Statutory Interpretation, 4th ed. (London: Butterworths, 2002, the concept of "absurdity" actually encompasses several components. The presumption against an "absurd" interpretation means the avoidance of an 1) unworkable or impractical result 2) an inconvenient result 3) an anomalous or illogical result 4) a futile or pointless result 5) an artificial result or 6) a disproportionate counter-mischief.

**46** Regarding inconvenience, the author at page 839 quotes Lord Shaw in Shannon Realities v. Ville de St. Michael [1924] AC 185 at 192, who said:

> "Where the words of a statute are clear, they must, of course be followed, but in their Lordships' opinion where alternative constructions are equally open, that alternative is to be chosen which will be consistent with the smooth working of the system which the statute purports to be regulating and that alternative to be rejected which will introduce uncertainty, friction or confusion into the working of the system."

**47** I find that MM resides in Ottawa within the jurisdiction of the respondent.

**48** I find that pursuant to S. 47(2), MM is entitled to be registered as a pupil with the respondent.

Issue #2:

**49** Is the respondent entitled to exclude MM from attending school on the basis that it would be detrimental to the safety or well-being of a person on the premises?

**50** The respondent relies on the following facts:

(a) From August, 2003, MM had been incarcerated in a detention center (near North Detention Center) until sentence, for an assault committed on a fellow resident in another group home.

(b) In the Fall of 2003, MM was sentenced under the Youth Criminal Justice Act 2002 to a term of four months secure custody which he served until January 21, 2004, at a closed custody facility (Syl Apps) in the Greater Toronto area.

(c) In January, 2004, MM was placed in "residential care" with the applicant, by either CAST or the sentencing court, to serve a term of probation of eighteen months which formed an additional part of the sentence previously referred to. There is no evidence that MM resides voluntarily at the applicant's site.

(d) MM's history includes six convictions for assault. He had a general background, both in Jamaica and Canada, of violence. He had been a gang member in the past and had a self-proclaimed interest in continuing to be a gang member.

(e) Contrary to the assertion of the applicant that MM was "bright", in fact his overall intellectual functioning was in the range of "Mild Developmental Disability".

(f) Contrary to the assertion of the applicant that MM is at risk of "losing his year", MM arrived in Canada with considerable lags in academic skill and he functions at several grade levels below an age-appropriate level. Any progress he makes will be slow at best.

(g) Contrary to the assertion of the applicant that MM desires to be in school, MM "professes little interest in school". While he understands that schooling can be the ticket to a good job as an adult, he "also appears to believe that there are other, more immediate, and remunerative methods of generating income than an "above the table" job."

(h) In addition to the intellectual problems, MM suffers from behavioural problems as well. He presented as Dual Diagnosis of both cognitive delays and serious emotional difficulties.

    (i) He sees violence and intimidation as the only legitimate and justified method of resolving conflicts, he has a penchant for violence and anti-social peers;
    (ii) He has a "self-stated interest in alcohol, tobacco, and marijuana";
    (iii) He is physically large for his age and uses his size to intimidate and manipulate others when dealing with conflict resolution/negotiation;
    (iv) He has a misogynist attitude towards women that makes it difficult for him to engage in a mutually respectful relationship with a same aged female peer;
    (v) He has assaultive impulses

Application Record, Affidavit of Jeffrey Walker,Esp. Exhibits A, B, C, H and I

Respondent's Record, Affidavit of Dan Wiseman, Esp. para 20 and Exhibit C

6. The following expert opinion was available to the Board from external sources:

    (a) "Intensive support in managing his own emotions and behaviours and developing social and problem solving skills will be important to him.

(b) Consistent monitoring of [MM's] behaviour will be important.
(c) In the short term, [MM's] academic skills are in such need of honing, and his behaviour is in such need of structure, that an on-site Section 20 programme is the only method of education at the present time".
(d) The following recommendations:

(i) "A highly structured, staff operated residential setting outside the GTA;
(ii) An on-site Section 20 programme with the ability to facilitate, when warranted, [emphasis added], integration into a community-based secondary school;
(iii) Built in Transitional, semi-independence programme to further facilitate [MM's] ...integration into the community close to his 18th birthday."

Respondent's Record, Affidavit of Dan Wiseman, Esp. para 20 and Exhibit C

7. The respondent Board concluded that, in the interest of safety and in the interest of an optimal placement, MM required placement in an Adaptive Special Support Unit. These units have a maximum of eight students, include a teacher and an educational assistant, and are highly structured. In addition, at least on an interim basis, there would also be a need for the full-time, one-on-one support of an additional education assistant.
8. There were, and are, no places available in any Adaptive Special Support Unit operated by the Board. Indeed, there is an existing waiting list of qualified resident pupils.
9. Funding by the Applicant and/or CAST for an additional full-time educational assistant has not yet been confirmed.
10. The Board determined that MM could not be safely admitted to a school of the Board at this time absent those supports.

Respondent's Record, Affidavit of Dan Wiseman, Esp. para 20 and Exhibit C

**51** The applicant takes the position that the Board in exercising its discretion must take into consideration the special education aspects relating to MM and must take into account all of the needs of the exceptional student, including safety concerns.

LAW:

**52** The parties agree that the Standard of Review on this issue is one of patent unreasonableness.

**53** The court does not have the right to substitute its view of the merits of any lawful action taken by the Board.

Bonnah v. Ottawa-Carleton District School Board Ontario, 64 O.R. (3d) 454, Court of Appeal C38421, April 8, 2003 - Tab 8

Bezaire v. Windsor Roman Catholic Separate School Board (1992), 9 O.R. (3d) 737 (Gen. Div. (Divisional Court) - Tab 10

**54** The court can only substitute its own discretion if the exercise of it was clearly discriminatory, arbitrary or in bad faith.

Titcher (Litigation Guardian of) v. Toronto District School Board, [2002] O.J. No. 4047 (S.C.J.) - Tab 12

**55** Section 265(1) provides:

> "It is the duty of a principal of a school, in addition to the principal's duties as a teacher...
>
> (m) subject to an appeal to the board, to refuse to admit to the school or classroom a person whose presence in the school or classroom would in the principal's judgment be detrimental to the physical or mental well-being of the pupils; ..."

**56** Section 305(1) provides:

> "The Minister may make regulations governing access to school premises, specifying classes of persons who are permitted to be on school premises and specifying the days and times at which different classes of persons are prohibited from being on school premises. 2000, c. 12, s. 3."

**57** Ontario Regulation 474/00 provides:

> "3.(1) A person is not permitted to remain on school premises if his or her presence is detrimental to the safety or well-being of a person on the premises, in the judgment of the principal, a vice-principal or another person authorized by the board to make such a determination."

**58** The Bonnah case addressed these issues. Doherty, J. at page 464:

> "Read together, s. 265(1)(m) and s. 3(1) of the regulation authorize principals to refuse to allow persons into a school, and to require persons to leave a school, where the principal determines that the presence of that person in the school would be detrimental to the safety of others in the school. These provisions allow principals to act quickly where the conduct of a person puts the safety of those under the charge of the principal at risk. Obviously, a principal can properly exercise these powers only where the safety concerns are genuine, and the principal's response to those concerns is a reasonable one in all of the circumstances. If it were shown that a principal used these powers to circumvent an obligation to leave an exceptional pupil in his or her placement pending an appeal, the court could intervene by way of judicial review just as it could if a principal used these powers for any other improper purpose.

> The word "person" in s. 265(1)(m) and s. 3(1) of the regulation should be given its normal meaning. That meaning encompasses pupils as well as non-pupils. Nor, in my view, does the existence of special provisions relating to the placement of exceptional pupils warrant interpreting the word "persons" in s. 265(1)(m) and s. 3 of the regulation as not including exceptional pupils. Section 265(1)(m) and s. 3(1) are not concerned with the placement of student according to their educational needs, but rather with preserving the safety of schools. The question of where an exceptional pupil should be placed to meet that pupil's best interests is a different question from the question of whether at a particular point in time a student poses a risk to the safety of himself or others in the school where he has been placed. It is an undeniable fact of life that a student may be both an immediate safety risk to others and an exceptional pupil. An interpretation of s. 265(1)(m) and s. 3(1) that would place exceptional pupils beyond the reach of a principal's power to exclude persons for safety reasons from the school is not only inconsistent with the language used in the Act and the regulation, but would seriously imperil the safety of exceptional pupils and other children who interact with that exceptional pupil. Where there are genuine safety concerns, considerations of the best interests of the child must extend to all of the children whose safety is at risk.
>
> Under the present scheme, a principal, and ultimately the Board, may exclude an exceptional pupil from his or her school or class for legitimate safety reasons."

**59** Doherty, J. also addressed the need to consider the placement needs of exceptional children:

> "That is not to say that the pupil's status as an exceptional pupil with respect to whom a placement decision has been made will be irrelevant to the manner in which a principal exercises his or her authority under s. 265(1)(m) and s. 3(1) of the regulation. Placement of exceptional pupils requires considerable expertise and careful assessment. Where a placement decision is challenged by the parents, it is clearly the policy of the Act and the regulations to leave the status quo in place while that challenge is considered. Where a principal must exercise his powers under s. 265(1)(m) or s. 3(1), he or she must bear in mind the special significance of the placement decision as it relates to exceptional pupils and strive to minimize any interference with that placement. For example, if safety concerns can be properly addressed by removal from the classroom rather than the school, then the more limited removal must be preferred in the case of an exceptional pupil."

**60** If MM is enrolled and excluded from attending school, the applicant could then refer the matter to the Identification Placement Review Committee (IPRC) and the placement process under the Special Education Statutory Regime would commence.

CONCLUSION:

**61** In the circumstances of this case, I am unable to say that the Board's decision to exclude MM from attending secondary school at this time for safety reasons was patently unreasonable.

**62** There will be an order to go granting the application for:

a) Leave granted to have this application heard on an urgent basis by a single Judge pursuant to subsection 6(2) of the Judicial Review Procedure Act, R.S.O. 1990, c.J-1 (hereinafter referred as the "JRPA").

b) An order in the nature of certiorari quashing or setting aside the March 12, 2004 Decision of the Superintendent of Instruction of the Ottawa-Carleton District School Board (hereinafter referred to as the "OCDSB") refusing to register or to consider allowing the registration of MM in any school within the jurisdiction of the OCDSB.

c) An order in the nature mandamus compelling the OCDSB to register MM as a student at MM's home school or at an otherwise alternative, appropriate school.

d) An order in the nature of mandamus compelling the OCDSB to immediately convene an Identification Placement Review Committee (hereinafter referred to as "IPRC") hearing pursuant to Regulation 181/98 under the Education Act of Ontario . The purpose of the IPRC hearing will be to identify MM's exceptionality, if any, his educational strengths and needs and to identify a suitable "placement" for him within the meaning of Regulation 181/98 of the Education Act

e) An order sealing the record of this proceeding or any document therein which identifies or tends to identify MM pursuant to s. 137(2) of the Courts of Justice Act.

**63** The application for an order in the nature of mandamus compelling the respondent to immediately provide a placement for MM in a school pending disposition of any IPRC hearing is dismissed.

COSTS:

**64** This case involved a number of overlapping regulations. The respondent submitted that the statutory matrix was complex and difficult. The meaning of the word "reside" in this legislation has not yet been determined by the court. The factums were lengthy, detailed and necessary. The hearing consumed 11/2 days.

**65** The applicant was substantially successful.

**66** I see no reason to derogate from the general rule that costs follow the cause. However, I consider that the meaning of the word "reside" had not previously been decided. I also consider that the respondent was successful in maintaining its position that MM was not entitled to attend school immediately.

**67** I fix costs in the sum of $17,500.00 all inclusive, payable to the applicant forthwith.

CAPUTO J.

cp/ci/e/nc/qw/qljml/qlkjg

# Tab 27

*Indexed as:*

# Cadillac Explorations Ltd. v. Procan Exploration Co.

**IN THE MATTER OF the bankruptcy of Cadillac Explorations Limited**
**Between**
**Cadillac Explorations Limited, applicant (appellant), and Procan Exploration Company, Kilborn Engineering (B.C.) Ltd. and Alto Construction Services (1973) Ltd., respondents (respondents), and**
**Dunwoody & Company, Alto Construction Services (1973) Ltd., Kilborn Engineering (B.C.) Ltd. and Territorial Leasing Ltd., respondents (respondents)**

[1984] B.C.J. No. 1648

53 B.C.L.R. 353

52 C.B.R. (N.S.) 37

25 A.C.W.S. (2d) 358

Vancouver Registry No. CA001874

British Columbia Court of Appeal
Vancouver, British Columbia

**Nemetz C.J.B.C., Hutcheon and Esson JJ.A.**

Judgment: filed May 7, 1984.

(11 pp.)

*Creditors and debtors -- Bankruptcy -- Approval of proposal -- Secured creditors included within meaning of "creditor" contained in Bankruptcy Act -- Secured creditors entitled to be heard on application for approval of proposal -- Bankruptcy Act, R.S.C. 1970, c. B-3.*

A trustee in bankruptcy applied for approval of a proposal to creditors. The chambers judge ruled that the secured creditors were entitled to be heard on that application. A creditor appealed that ruling.

HELD: The appeal was dismissed. A secured creditor was within the definition of "creditor" contained in s. 2 of the Bankruptcy Act. There was no contrary intention appearing to show that secured creditors were to be excluded under s. 41 of the Act. Accordingly, the secured creditors were entitled to be heard on an application to the court pursuant to ss. 40 and 41 for approval of a proposal to creditors.

**Counsel:**

Mary F. Southin, Q.C. and Gregory Walsh, appearing for appellant Cadillac Explorations Limited (Cadillac).
Douglas I. Knowles, appearing for respondent Procan Exploration Company (Procan).
A.K. MacKinnon, appearing for respondents Alto Construction Services (1973) Ltd. and Kilborn Engineering (B.C.) Ltd. (Alto & Kilborn)
Kenneth S. Fawcus, appearing for Dunwoody & Company.

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The judgment of the Court was delivered by

1 **ESSON J.A.**:-- Cadillac has made a proposal to its creditors under Part III of the Bankruptcy Act R.S.C. 1970 Ch. B-3 and Amendments. The proposal having been approved by the requisite majority of creditors, the trustee has applied under s. 40 for approval by the court. Cadillac raised the preliminary objection that Procan, Alto and Kilborn are not entitled to be heard on that application. Cadillac now appeals the ruling of the chambers judge that those parties are entitled to be heard.

2 The major, if not sole, enterprise of Cadillac is the development of a mining property in the North West Territories. Alto and Kilborn are creditors by reason of having supplied goods and services for the purpose of that development. They are secured creditors because they hold mining liens on the mining and mill property of Cadillac under the legislation of the Territory.

3 The position of Procan is different. It is a joint venturer with Cadillac in the mining development. The agreement between them provides that development expenses will be contributed pro rata with Cadillac undertaking to pay 60% and Procan 40%. In its proof of claim, Procan claims that Cadillac is indebted to it for about $542,000.00. Of that total, $537,000.00 is said to be an amount which Procan has contributed to Cadillac for development purposes which has been expended by Cadillac without Cadillac having met its obligation to expend 150% of that amount. On that basis, Procan asserts that Cadillac is obliged to repay the sum of $537,000.00. As to that amount, Cadillac denies that it is indebted and therefore denies that Procan is a creditor. The balance of Procan's claim, in the amount of about $4,400.00, is not disputed by Cadillac although there is some uncertainty as to whether it is an unsecured or secured claim. Procan claims to be an unsecured creditor for that amount but was held by the chambers judge to be secured because of a provision of the agreement giving it a lien for recovery of expenditures of that class.

4 The position of Alto, Kilborn and Procan gave rise to litigation at an earlier stage. At the meeting of creditors to consider the proposal, Cadillac took the position that they were not entitled to vote because:

a) Alto and Kilborn were secured creditors who had not surrendered or valued their security and,

b) Procan was not entitled to vote (except on the basis of being a creditor for $4,400.00) because it was not a creditor in respect of the larger amount of $537,000.00.

**5** Alto, Kilborn and Procan were permitted to vote subject to the objection and application was then made to the court for a ruling as to their entitlement to vote. All three voted against the proposal and, had their votes counted, the result would have been defeat for the proposal. McEachern C.J.S.C. ruled that, because Alto and Kilborn had not unequivocally surrendered their security, they were precluded from voting by the terms of s. 90 of the Act. That ruling was upheld on appeal to this court. The application in respect of Procan's right to vote was not pressed to a decision, presumably because the deletion of the votes of Alto and Kilborn was sufficient to make the vote one for approval.

**6** In his reasons for the ruling now appealed from, i.e., that Procan, Alto and Kilborn should be permitted to be heard on the application for approval, the chambers judge dealt with a number of issues, including the validity of Procan's claim in respect of the sum of $537,000.00 and the question whether the court has a discretion to grant audience on such an application to persons who are not given, by s. 41 of the Act, a right to appear. The primary position of Procan, Alto and Kilborn is that they have a right to be heard which is not subject to the exercise of any discretion. If they are correct in that, the other issues need not be considered.

7 The relevant sections of the Act are these:

> 40. -- Upon acceptance of the proposal by the creditors, the trustee shall apply to the court forthwith for its approval and shall send notice of the hearing of the application by registered mail, not less than fourteen days before the date of the hearing, to the debtor, to every creditor who has proved his claim and to the Superintendent; and the trustee, not less than three days before the date of the hearing, shall file in the prescribed form a report to the court on the proposal and shall forward a copy to the Superintendent not less than ten days before the date of the hearing.
>
> 41. -- (1) The court shall, before approving the proposal, hear a report of the trustee in the prescribed form as to the terms thereof and as to the conduct of the debtor, and, in addition, shall hear the trustee, the debtor, any opposing, objecting or dissenting creditor and such further evidence as the court may require.
>
> (emphasis added)

The first question is whether a secured creditor is a "creditor" within s. 41. If it is, Procan, Alto and Kilborn are all entitled to be heard because Alto and Kilborn are conceded to be secured creditors for the whole of the amount of their claims and Procan is conceded to be a secured creditor in respect of the $4,400.00 claim.

**8** The definition section of the Act is s. 2. It says:

> In this Act, "creditor" -- means a person having a claim, preferred, secured or unsecured, provable as a claim under this Act.

**9** Miss Southin, for Cadillac, submits that, because the respondents are secured creditors who have not surrendered, valued or realized upon their security, they do not have a secured claim "provable as a claim under this Act" and therefore are not within the definition of creditor. In support of that submission, she refers to s. 98, which reads as follows:

> 98. (1) Where a secured creditor realizes his security, he may prove for the balance due to him after deducting the net amount realized.
>
> (2) Where a secured creditor surrenders his security to the trustee for the general benefit of the creditors, he may prove for his whole claim.

**10** S. 98 defines the rights of a secured creditor after realizing upon or surrendering its security. It defines the amount for which it can then "prove". It does not follow, in my view, that a secured creditor who has neither realized nor surrendered does not have a "provable claim". In respect of those and similar words, s. 2 provides:

> "claim provable in bankruptcy" or "provable claim" or "claim provable" includes any claim or liability provable in proceedings under this Act by a preferred, secured or unsecured creditor.

**11** In s. 95 of the Act, under the heading "Claims provable" there is another definition of that phrase:

> (1) All debts and liabilities, present or future, to which the bankrupt is subject at the date of the bankruptcy or to which he may become subject before his discharge by reason of any obligation incurred before the date of the bankruptcy shall be deemed to be claims provable in proceedings under this Act.

**12** Those definitions indicate that all debts to which the bankrupt is subject at the date of bankruptcy give rise, at that date, to a claim provable by the creditor. Those provisions of the Act are not included in Part HI but, by s. 46, all provisions of the Act, insofar as they are applicable, apply mutatis mutandis to proposals. The equivalent date to the date of bankruptcy would be the date of the proposal. From the outset, a secured creditor is a creditor. He may file a proof of claim wherein he must state whether he is a secured creditor (s. 97(5)). His right to vote is affected by s. 90 and, as I have already said, if he realizes upon or surrenders the security, his rights are defined by s. 98. But, from the beginning, the secured creditor is within the definition of creditor in s. 2.

**13** As an alternative, Miss Southin submits that the definition does not apply to the word "creditor" in s. 41. She refers to the Interpretation Act, R.S.C. 1970 cap. 1-23, s. 14(2):

> "Where an enactment contains an interpretation section or provision, it shall be read and construed
>
> (a) as being applicable only if the contrary intention does not appear, and
> (b) as being applicable to all other enactments relating to the same subject matter unless the contrary intention appears. 1967-68, c. 7, s. 14"
>
> (underlining added)

**14** The submission is that a contrary intention should be held to appear in s. 41 for these reasons:

(1) A proposal is, in effect, an offer to the unsecured creditors which, if accepted by a majority of them, binds the dissentients. See Houlden and Morawetz Bankruptcy Law of Canada, page 93.
(2) By s. 36, proposals are made subject to the rights of secured creditors who can pursue their remedies no matter how such actions affect the unsecured creditors.
(3) Part III of the Act, in a number of places, appears to employ the word "creditors"on occasion to mean unsecured and preferred creditors only. In particular, reference is made to s. 36 dealing with voting on the proposal and s. 42(2) which provides that approval is binding on creditors.

**15** I will assume that a contrary intention can be established not only by express words but also by the context and other considerations requiring a different interpretation. In Pacific Simpson Lumber Ltd. et al. v. Kaisha et al. (1981), 129 D.L.R. (3d) 236 this Court applied such an approach in considering the words "unless a contrary intention appears" in s. 3(1) of the same Act in construing the word "year" in the regulations under the Indian Act. The Court gave a number of reasons for holding that "year" in those regulations did not have the meaning set out in the Interpretation Act. That conclusion was based upon the history of the legislation, the absurdity and impracticability which would result if the definition in the Interpretation Act was to be applied, and the fact that the word appeared in a phrase (year of issue) in which it would be reasonable to think that a different meaning was intended than if it had been used alone. Those reasons, taken together, were held to require the finding that a contrary intention appeared.

**16** The difference between "only if the contrary intention does not appear" in s. 14(2)(a) and "unless the contrary intention appears" in s. 14(2)(b) and s. 3(1) of the same Act is puzzling but I can see no reason to think that any difference in meaning was intended. The question must still be whether the context and other considerations require the conclusion that a contrary intention appears. I cannot find that, in this case, they do.

**17** The fact that a proposal is an offer to unsecured creditors designed to bring about a contract with them, and the fact that proposals are specifically made subject to the rights of secured creditors, are considerations which lend some support to an argument that, as a matter of policy, secured creditors should not be heard on an application under s. 41. But they are not considerations which compel the conclusion that parliament has legislated to exclude a right of audience to secured creditors. There are policy considerations which point in the opposite direction. One is the fact that secured creditors may not know, at an early stage of a proposal, what value to put upon their security; and often do not know whether, in the end, they will rely upon their security entirely or in part or at all. This lack of finality in the position of the secured creditor is emphasized by the provisions of ss. 102 and 103 providing for amendments of valuations and proof in certain circumstances. One cannot say that the interests of secured creditors, as distinct from their security, cannot be affected by the approval of a proposal.

**18** The argument that the word "creditors" in other sections excludes secured creditors is equally inconclusive. If it does, that is a consideration consistent with finding that "creditors" in s. 41 was not intended to include secured creditors, but it is not a consideration which compels the

conclusion that secured creditors are excluded. Nor am I persuaded that it is right to say that secured creditors are not included in the word "creditors" as used in ss. 36 and 42(2). Their voting rights are restricted, not by the words used in s. 36, but by the words of s. 90 which expressly restricts the rights of secured creditors. So with s. 42(2) which provides that a proposal is binding "on all the creditors with claims provable under this Act". By reason of other provisions of the Act, it is clear that that cannot be stretched to mean that the proposal can have the effect of destroying a charge. A proposal will, however be binding upon secured creditors who do not rely entirely upon their security and, as I have already held, secured creditors are "creditors with claims provable" until they take some step, such as realization in full, which has the effect of destroying that status.

**19** I therefore conclude that Procan, Alto and Kilborn are creditors within s. 41. It is not disputed that they are "opposing, objecting or dissenting" creditors and it therefore follows that they must be heard on the hearing of the application.

**20** That finding is sufficient to dispose of the appeal. I will, however, refer to one of the other questions decided by the chambers judge because of its possible bearing on the future conduct of the bankruptcy and because Procan has brought, in respect to that question, a separate appeal which was heard with this one. That is the question as to the validity of Procan's claim to be a creditor for $537,000.00. Before the chambers judge, Procan argued that it is a creditor in that amount and Cadillac argued that it was not indebted to Procan in respect of that head of claim. The chambers judge rejected both submissions and held that Procan is a creditor because Cadillac has breached its contract to make a pro rata contribution to expenditures giving rise, not to an obligation on the part of Cadillac to repay the $537,000.00, but to a unliquidated claim for damages by Procan. It is against that finding that Procan has appealed.

**21** Because Procan, as a creditor under s. 41, has a right to be heard based upon the smaller debt, it was unnecessary for the chambers judge to make any finding with respect to the status of its claim for $537,000.00. The trustee in bankruptcy has objected that any such finding was premature and made without jurisdiction in that the jurisdiction to determine the validity of claims lies, in the first instance, with the trustee under s. 106 of the Act. In asserting that position, the trustee may well be right but the issue as to jurisdiction need not be decided here. As the finding as to the status of the claim was unnecessary, it is of no binding effect between the parties.

**22** In view of the conclusion that the finding was unnecessary, Procan's appeal should succeed to the extent of granting the first order which it seeks, i.e., one declaring that the application by Cadillac seeking determination of the validity of Procan's claim was premature.

**23** The chambers judge also based his conclusion upon a discretionary power, which he found to reside in the court on an application of this kind, to hear parties who are not within the categories set out in s. 41. Again, in view of the conclusion that these parties are within those categories, it is unnecessary to deal with that aspect of the ruling appealed from.

**24** On the basis that the three parties are creditors within s. 41, the appeal is dismissed. Procan's cross-appeal is allowed to the extent indicated.

ESSON J.A.
NEMETZ C.J.B.C.:-- I agree.
HUTCHEON J.A.:-- I agree.

qp/s/mes

# Tab 28

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1987 CarswellBC 291, 18 B.C.L.R. (2d) 138, [1988] 1 W.W.R. 372, 45 D.L.R. (4th) 290

Bank of Montreal v. Gratton

BANK OF MONTREAL v. GRATTON

British Columbia Court of Appeal

Taggart, Esson and McLachlin JJ.A.

Heard: September 22, 1987
Judgment: October 7, 1987
Docket: Vancouver No. CA007213



Counsel: *F.W. Hansford*, for appellant.

*R.J. Ellis*, for respondent.

Subject: Corporate and Commercial

Chattel Mortgages and Bills of Sale --- Rights and liabilities of parties — Remedies on default — Seize or sue requirement.

Personal property security — Chattel mortgages and bills of sale — Operation of legislation — Lender holding two mortgages of same chattels securing different debts — Lender exercising remedy of sale under first mortgage — Seize or sue provisions of Chattel Mortgage Act not operating to extinguish debt secured by second mortgage.

Statutes — Interpretation — Interpretation Acts — Interpretation Act applying to every enactment "unless a contrary intention appears" — Contrary intention not needing to be found in express words — Contrary intention may be inferred from scheme of enactment, legislative history or other circumstances.

Where a mortgagee holds more than one mortgage on the same chattels, securing different debts, and exercises the remedy of sale under the first mortgage, the seize or sue provisions contained in s. 23 of the Chattel Mortgage Act do not operate to extinguish the debt under the subsequent mortgage or mortgages. The effect is to extinguish only the debt secured by the mortgage under which the seizure took place. This interpretation of the Chattel Mortgage Act is supported by the language of s. 23 itself, which uses the singular words "mortgage" and "grantor". The Interpretation Act, which provides in s. 28(3) that in an enactment words in the singular include the plural, and words in the plural include the singular, does not require a different result, since, by s. 2(1), the Act is to apply "unless a contrary intention appears". A contrary intention need not be found in express words, but may be inferred from the scheme of the enactment, its legislative history and other circumstances which surround the use of the word in question. Although the

Interpretation Act does not use the words "the context otherwise requires", the conclusion that a contrary intention appears may be based on the fact that the context otherwise requires. In the case of the Chattel Mortgage Act, the use of the singular throughout the statute can be taken as an indication of legislative intent that the scheme apply to the creation of a single chattel mortgage and the rights and obligations conferred by a single chattel mortgage.

**Cases considered:**

*C.I.B.C. v. Okanagan Truck & Equip. Wash Ltd.* (1982), 39 B.C.L.R. 322 (Co. Ct.) — *considered*

*Pac. Simpson Lumber Ltd. v. Kaisha*, [1982] 3 W.W.R. 194, 129 D.L.R. (3d) 236 (B.C.C.A.) — *considered*

*Starr Schein Ent. Inc. v. Gestas Corp.* (1987), 13 B.C.L.R. (2d) 85, [1987] 4 W.W.R. 664, [1987] I.L.R. 1-2189, affirming 70 B.C.L.R. 362, [1986] 3 W.W.R. 366, 18 C.C.L.I. 148, [1986] I.L.R. 1-2053 (C.A.) — *considered*

*Trans Can. Credit Corp. v. Wai* (1984), 55 B.C.L.R. 134 (Co. Ct.) — *considered*

**Statutes considered:**

Chattel Mortgage Act, R.S.B.C. 1979, c. 48

ss. 2-12

s. 13 [am. 1981, c. 21, s. 14]

s. 14 [am. 1981, c. 21, s. 15]

s. 16

s. 17

s. 18

s. 22

s. 23

Interpretation Act, R.S.B.C. 1979, c. 206

s. 2

s. 28(3)

Appeal from judgment of McEachern C.J.S.C., [1987] B.C.W.L.D. 444, [1987] C.L.D. 226, granting judgment on promissory note secured by chattel mortgage.

**The judgment of the court was delivered by *Esson J.A.*:**

1 Chattel mortgagees were once free to exercise a contractual right to sell the chattels secured by the mortgage and

sue for any deficiency after sale. Since 1973, the "seize or sue" provisions of the Chattel Mortgage Act have required the mortgagee to elect its remedy with the result that, if the remedy of seizure is exercised, the debt is extinguished. This appeal raises the question whether, if the mortgagee holds more than one mortgage on the same chattels, and exercises the remedy of sale under the first mortgage, the effect is to extinguish the debt under the subsequent mortgage or mortgages. McEachern C.J.S.C. held that the effect is to extinguish only the debt secured by the mortgage under which the seizure took place [[1987] B.C.W.L.D. 444, [1987] C.L.D. 226].

2 The facts which give rise to that question are these. In 1979 the bank lent to Mr. Gratton $19,700 on the security of a chattel mortgage charging a motor home. In 1980 a different branch of the bank lent $20,000 to him on a promissory note. In 1982 as consideration for an extension of time to pay that loan, Mr. Gratton gave a second chattel mortgage on the same motor home. The second mortgage was expressed to be subject to the first. All registration requirements were complied with by the bank. In 1983 the bank seized the motor home by a warrant based only upon the first mortgage. It sold the home for less than the amount owing under that mortgage. It then brought this action to recover the amount owing on the promissory note given in 1980, i.e., the loan secured by the second mortgage. Mr. Gratton now appeals the judgment against him for the amount of that loan.

3 The question is whether that indebtedness is extinguished by these provisions of the Chattel Mortgage Act, R.S.B.C. 1979, c. 48:

> 23.(1) Subject to sections 24(4) and 26, a grantee may enforce his right to the money due and owing under a chattel mortgage either by
>
> (*a*) taking possession of the chattels, on a surrender or under the mortgage; or
>
> (*b*) suing the grantor for the money due and owing,
>
> but not both.
>
> (2) Where the grantee takes possession of the chattels, the grantor's obligations and the obligations of the guarantor or indemnitor under the mortgage and in any instrument giving collateral security are extinguished.

4 The action was tried on an agreed statement of facts. The Chief Justice held that the seizure and sale of the security under the first mortgage did not extinguish the debt secured by the second mortgage because:

> (a) Section 23(1) deals only with the consequences of taking possession of chattels "under the mortgage" or suing the grantor (of the mortgage). Section 23(1) does not purport to deal with instruments other than the one under which possession was taken.
>
> (b) Upon seizure of the chattel under the 1979 mortgage, all that was extinguished was the grantor's obligations "under the mortgage and in any instrument giving collateral security" (s. 23(2)). The 1980 promissory note and the 1982 mortgage were not collateral to the 1979 mortgage and the defendant's obligations under them were not extinguished.

5 The Chief Justice, in finding for the bank, followed the decision of Lamperson Co. Ct. J. in *C.I.B.C. v. Okanagan Truck & Equip. Wash Ltd.* (1982), 39 B.C.L.R. 322, and that of Robinson Co. Ct. J. in *Trans Can. Credit Corp. Ltd. v. Wai* (1984), 55 B.C.L.R. 134. The essence of the grounds for decision in those cases is, I think, to be found in this language of Lamperson Co. Ct. J. at p. 324 of the earlier case:

> A grantor may give a first and second chattel mortgage over the same items to two separate grantees. If one

grantee were to seize the goods mortgaged the other grantee could, nonetheless, elect to sue the grantor under the personal covenants contained in the chattel mortgage. There is no reason why this should not be so if the chattel mortgagee is the same. The chattel mortgages in this case pertain to two separate and distinct loans. There would be a problem if the bank had artificially split one loan into two in order to circumvent the intent of the Chattel Mortgage Act. However, this is not the case here. The bailiff's warrant clearly indicates that the goods were seized pursuant to the chattel mortgage pertaining to the $32,000 promissory note. Nothing in the wording of the applicable sections of the Chattel Mortgage Act indicates that the suggested distinction should be drawn. I am of the view that each individual transaction should be treated separately, although they are between the same parties. Accordingly, in these circumstances, the seizure of the goods pursuant to the one chattel mortgage is not a seizure to the other.

6 In the passage which I have quoted from the reasons of the Chief Justice, he emphasizes that the words "mortgage" and "grantor" are in the singular. That view, the appellant submits, is in error because it overlooks the effect of s. 28(3) of the Interpretation Act, R.S.B.C. 1979, c. 206. That section, which is not referred to in the reasons under appeal or the earlier cases, reads as follows:

(3) In an enactment words in the singular include the plural, and words in the plural include the singular.

7 That broad language must be read in conjunction with s. 2(1) and (3) of the Interpretation Act:

2.(1) Every provision of this Act extends and applies to every enactment, whether enacted before or after the commencement of this Act, unless a contrary intention appears in this Act or in the enactment.

(3) Nothing in this Act excludes the application to an enactment of a rule of construction applicable to it and not inconsistent with this Act.

8 No contrary intention appears in the Interpretation Act. The real question is whether a contrary intention appears in the Chattel Mortgage Act.

9 We have been referred to no case which has considered the language of s. 28(3). In relation to other sections of the Interpretation Act, however, this court has considered the meaning of "unless a contrary intention appears in the enactment" in two recent decisions. They are: *Pac. Simpson Lumber Ltd. v. Kaisha*, [1982] 3 W.W.R. 194, 129 D.L.R. (3d) 236 (B.C.C.A.); *Starr Schein Ent. Inc. v. Gestas Corp.*, 13 B.C.L.R. (2d) 85, [1987] 4 W.W.R. 664, [1987] I.L.R. 1-2189.

10 In *Pac. Simpson*, Lambert J.A. for the court reviewed the history of the legislation and gave extensive reasons for concluding that the word "year" was used in the enactment with a contrary intention to that appearing in the definition in the Interpretation Act. In *Starr Schein*, the word under consideration was "property". The trial judge, Legg J., held that the definition in the Interpretation Act should not apply because "the context otherwise requires" [70 B.C.L.R. 362, [1986] 3 W.W.R. 366, 18 C.C.L.I. 148, [1986] I.L.R. 1-2053]. His reasons were agreed with by Seaton J.A. for the majority. Lambert J.A. dissented.

11 The issues in those cases were sufficiently different from those in the case at bar to render the decisions of no direct application. But they do throw light on the proper scope and application of the words "unless a contrary intention appears". Without attempting a comprehensive definition of that language, I take those decisions as supporting the following generalizations. The contrary intention need not be found in express words, but may be inferred from the scheme of the enactment, its legislative history and other circumstances which surround the use of the word in question. Although the Interpretation Act does not use the words "the context otherwise requires", the conclusion that a contrary intention appears may be based on the fact that the context otherwise requires.

12 I return to the question whether the singular words "mortgage" and "grantor" in s. 23(1) of the Chattel Mortgage Act include the plural of those words, or does a contrary intention appear? I think the emphasis here should be upon "mortgage" because I can see no logical basis for treating the two words differently.

13 The words "mortgage" or "chattel mortgage" are used many times in the Act and, with one exception, always in the singular. That exception is in s. 18:

> 18. Two or more registered mortgages of some or all of the same chattels have, as between themselves and for those chattels, priority in the order of the dates of registration, subject to a contrary intention appearing from the chattel mortgages.

14 In most instances, the use of "mortgage" makes sense only if the reference is understood to be in the singular — the reference is obviously to a particular instrument as in this language from s. 16:

> 16. Where a subsequent chattel mortgage
>
> (*a*) is made after an earlier chattel mortgage ...

15 The statute, read as a whole, sets out a scheme dealing with:

16 (a) the making, registering, transferring and renewal of a chattel mortgage (ss. 2-15, 22);

17 (b) the legal effects flowing from a chattel mortgage, including priorities and the seize or sue provisions (ss. 16, 17, 18 and 23).

18 The use of the singular throughout the statute can be taken as an indication of legislative intent that the scheme apply to the crea tion of a single chattel mortgage and the rights and obligations conferred by a single chattel mortgage. Even s. 18, where the plural is used because the context clearly requires it, is conceptually concerned with the rights flowing from each chattel mortgage in the singular.

19 The fact that a contrary intention clearly appears in many sections other than s. 23 is not conclusive in establishing that a contrary intention appears in relation to the use of the word in that section. But it is a matter of some significance. In the absence of any clear indication that the word is used in s. 23 in a different sense from in the other sections, it is reasonable to assume that it is used in the same sense. I see nothing in the context of s. 23 to indicate that the intention with respect to singular and plural is different from in other sections. On the other hand, there are indications within s. 23 that the intention is to use "mortgage" in the singular. For instance, s. 23(2) refers to "the mortgage and in any instrument giving collateral security".

20 Mr. Hansford, in his very full submissions for the appellant, placed great emphasis on the circumstances that, wherever the Chattel Mortgage Act refers to the chattel or chattels included in a mortgage, it uses only the plural "chattels". That is the word used in the definition of "chattel mortgage", in the definition of "chattels" and throughout the Act including the first two subsections of s. 23 which are the ones in question. Mr. Hansford submits that, if a contrary intention is found with respect to the word "mortgage", the corresponding contrary intention must be found with respect to "chattels" so that the plural would not include the singular. That, in turn, would result in the Act not applying to mortgages which charge only one chattel.

21 The flaw in that submission, in my view, is that it rests on the premise that, if a contrary intention is found with respect to one word in a section, the same intention must be found with respect to all others. That does not follow. Each word must be considered separately although, as with "mortgage" and "grantor", two or more words may sometimes

be so linked by context that it would create an absurdity to find a different intention with respect to them. I see no such necessary relationship between the intention applicable to "mortgage" and that applicable to "chattels".

22 Indeed, the word "chattels" provides a good example of a word in respect of which no contrary intention appears. No sensible reason can be advanced for the view that, in this instance, the plural should not include the singular. On the other hand, there are obvious and powerful reasons for holding that the plural must include the singular. If it does not, the Act would not apply to many, probably most, chattel mortgages. Where no reason can be advanced for the plural not including the singular, and where such an interpretation would result in an absurdity, one must conclude that no contrary intention appears. In respect of "mortgage" and "grantor", these considerations are not present, and the considerations which are present point to a contrary intention.

23 I conclude, for those reasons, that a contrary intention does appear in the Chattel Mortgage Act and that "mortgage" in ss. 23(1) and 23(2) is used in the singular. Essentially the same considerations require the conclusion that "grantor" in those sections is used in the singular.

24 We were referred to a number of authorities supporting submissions based, not upon the language of the statute, but on what the parties suggest is the proper course to be followed to give effect to the policy of the legislation. The appellant emphasizes that the policy of the Act is to protect a debtor from being sued for a deficiency after sale of the chattel and that, unless the seizure under one mortgage extinguishes the debt under all other mortgages held by the same grantee, the way will be opened for borrowers to evade the policy of the Act. On the other side of the question, the bank stresses that, if the appellant's view was to be accepted, that could result in anomalies unfair to lenders. These arguments on the policy of the Act establish nothing more favourable to the position of the appellant than that it is not inconsistent with that policy. That cannot justify a refusal to give effect to the plain meaning of s. 23 which, in my view, emerges once it is concluded that "mortgage" in that section does not include the plural.

25 I would dismiss the appeal.

*Appeal dismissed.*

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# Tab 29

*Indexed as:*

**R. v. Scory**

**IN THE MATTER OF an appeal by way of a Stated Case to the Court of Queen's Bench under the provisions of Section 734 of the Criminal Code of Canada**
**Between**
**Her Majesty the Queen, on the information of Corporal R.H. Robinson, a member of The Royal Canadian Mounted Police, appellant, and**
**William Scory, of Prelate, in the Province of Saskatchewan, garage proprietor, respondent (accused)**

[1965] S.J. No. 11

51 W.W.R. 447

Saskatchewan Court of Queen's Bench
Judicial Centre of Swift Current

**Davis J.**

January 28, 1965.

(5 paras.)

On appeal from Vause J.

**Counsel:**

D.K. Krueger, for the applicant.
J.M. Schmidt, for the respondent.

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1 **DAVIS J.**:-- This is an appeal by the Crown by way of stated case from the decision of C.W. Vause, a Provincial Magistrate, in which he found the accused, respondent, William Scory, not guilty of the charge:

"That on or about the 14th day of June, A.D. 1964, at Prelate district, Saskatchewan, that William Scory, Garage Proprietor, being a person, did unlawfully cause to be marked with a mark, stock of which he is not the owner, without authority of the owner, contrary to Section 23(b) of The Brands and Brand Inspection Act."

**2** On the facts stated the learned Magistrate found that the accused had branded a heifer, the property of one Rodney Cox, with an unrecorded brand which the accused used to brand his own stock; that the heifer already bore a brand, likewise unrecorded, which Cox had placed thereon. It did not appear on the facts stated whether the Cox brand was visible or known to the accused or whether the branding was done by him by mistake. The applicability or otherwise of mens rea was not argued before me, and I make no finding on it. The appeal was argued solely on the interpretation placed upon the word "owner" as it appears in Section 23(b) of the said Act. This subsection reads:

"23. A person who:

(a) ...
(b) brands or causes, directs or permits to be branded with his own or with any brand, vent or mark any stock of which he is not the owner without the authority of the owner;
(c) ...

is guilty of an offence and, in addition to any other penalty to which he may be subject by law, is liable on summary conviction to a fine not exceeding $200."

**3** The learned Magistrate held that the word "owner", where it appears in the said subsection, means "owner of the brand" rather than "owner of the stock", and that as the brand in question was unrecorded there was no offence. He appears to have arrived at this conclusion because of the definition of the word "owner" in Section 2, subsection (9) of the said Act, which reads:

"2. In this Act:

9. 'owner' means the owner jointly or in severalty of a brand or vent recorded as allotted and includes the duly recorded transferee thereof and the authorized agent of such owner or transferee."

**4** To hold that the definition is exhaustive and must prevail would do violence to the recognized rules of grammar and would render the subsection meaningless. The law is that if a defined expression it used in the context which the definition will not fit, the context must be allowed to prevail over the "artificial conceptions" of the definition clause and the word must be given its ordinary meaning. Maxwell on Interpretation of Statutes, Eleventh Edition, page 321; Strathern v. Paggen, 1926 Sessions Cases (Judiciary Reports) 9. With deference, I must hold that the word "owner where it appears in the said subsection means "owner of the stock" and not "owner of the brand" as was held by the learned Magistrate.

**5** The appeal will therefore be allowed and the case remitted to the learned Magistrate for completion and decision. The appellant is entitled to costs against the respondent, if asked for.

DAVIS J.

qp/t/qlslc/qladp

# Tab 30

*Indexed as:*

# R. v. Ambrose

**Between**
**Her Majesty the Queen, complainant, and**
**Ross Clyde Ambrose, respondent**

[1999] O.J. No. 3607

43 W.C.B. (2d) 441

Ontario Court of Justice
Toronto Region

**P. Harris J.**

Heard: September 1, 1999.
Judgment: September 21, 1999.

(22 paras.)

*Criminal law -- Peace officer -- Police -- Arrest and detention -- Arrest without warrant.*

Trial of the accused, Ambrose, on charges of assaulting two peace officers in the execution of their duties and failing to leave premises as directed, contrary to the Trespass to Property Act. The Toronto Police Services Board appointed Toronto Transit Commission special constables to enforce the Trespass to Property Act. Two constables issued tickets to Ambrose and his girlfriend for misuse of a metropass and failure to deposit the correct fare. A heated discussion ensued, and the constables asked Ambrose to leave the property or he would be arrested for trespass. Ambrose refused to leave, and one of the constables arrested him and touched his arm. Ambrose pulled away, and the constables wrestled him to the floor before handcuffing him and turning him over to the police. All three men suffered minor injuries. Ambrose claimed that the constables attacked him and that he used only such force as was necessary to defend himself.

HELD: Ambrose was convicted. The constables were police officers within the meaning of the Trespass to Property Act and were entitled to use reasonable force in arresting Ambrose. It would have been absurd that individuals trespassing on the Toronto Transit Commission's property could impede the movement of hundreds of rush hour patrons for some illegitimate purpose, while special constables employed to ensure the comfort, convenience and safety of passengers could do no more than utter words of arrest before seeking the assistance of a police officer.

**Statutes, Regulations and Rules Cited:**

Criminal Code, s. 2.

Interpretation Act, R.S.O. 1990, c. I-11, s. 7(2), 28.

Police Service Act, R.S.O. 1990, c. P-15, s. 2, 53(3).

Trespass to Property Act, R.S.O. 1990, c. T-21, ss. 2(1)(b), 9.

**Counsel:**

M. Denomme, for the Crown.
J. Di Luca, for the defence.

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**P. HARRIS J.:--**

The Charges

**1** Ross Clyde Ambrose was charged that on or about October 7th , 1998, he did assault a peace officer Matthew Edward, engaged in the execution of his duty, and that he did assault a peace officer Robert Brown, engaged in the execution of his duty and further that he did assault Matthew Edward and Robert Brown with intent to resist the lawful arrest of himself. He was also charged with failing to leave premises when directed on the same date, contrary to Section 2(1)(b) of the Trespass to Property Act.

The Issue

**2** The pivotal question in this case concerns the precise formal status of special constables Brown and Edward and whether they, having been appointed by the Toronto Police Services Board to enforce, inter alia, the Trespass to Property Act R.S.O. 1990, c. T-21 as amended, had the power to use force in affecting the arrest of Mr. Ambrose under the Trespass to Property Act. If they had no powers to use force during the arrest and detention of Mr. Ambrose, they were not acting in the lawful execution of their duties and consequently, Mr. Ambrose arguably was justified in using reasonable force in self defence to repel what was, in law, an assault by the two special constables on his person as a result of their efforts to handcuff and detain him following his arrest. The issue is whether the special constables had assumed the status of police officers and were authorized to use reasonable force within the meaning of Section 9 of the Trespass to Property Act as interpreted by caselaw.

The Facts

**3** I find the following events occurred on October 7th, 1998. Special constables Brown and Edward were in attendance at the Scarborough Town Centre Light Rapid Transit station performing investigative functions for their employer, the Toronto Transit Commission. Both in uniform, they began checking patrons of the TTC to ensure that they were using transit passes properly and paying the correct fare. A female was questioned to determine whether she was entitled to use the Metropass she had used to gain entry to the transit system. After some discussion, she said the

Metropass belonged to Mr. Ambrose who was at that time outside the paid area of the station entrance and he was summoned for further investigation.

**4** Though he testified to the contrary, I find that he said he did not want it anymore and had given it to the female who was apparently his girlfriend. Special constable Edward then issued two POA offence tickets - one to the female for failing to deposit the correct fare and one to Mr. Ambrose for misuse of a Metropass. Mr. Ambrose asked that the Metro pass be returned to him as it was still valid for the month of October. Mr. Edward stated that the pass would have to be retained by him as evidence in respect to the POA charges. After some considerable discussion between Mr. Ambrose and the two special constables that became heated at times, Mr. Ambrose was told to leave TTC property or he would be arrested "for trespass". He refused to leave the immediate area and after further warnings, Mr. Brown told Mr. Ambrose he was under arrest for trespassing and touched his arm. Mr. Ambrose pulled away from his grasp. Both special constables tried to take control of Mr. Ambrose and by pushing and pulling away from them he managed to break free. The constables then grabbed an arm each and took him to the floor whereupon a short struggle ensued before he was handcuffed and turned over to the police.

**5** All three involved sustained some minor injuries. Mr. Ambrose testified that when he refused to leave the TTC property because the Metropass was not returned, he was attacked by the two constables and used only such force as was necessary to defend himself and struggle free.

Analysis

**6** In resolving credibility issues to arrive at the foregoing findings of fact, I have employed the analysis contained in R. v. D.W. (1991) 63 C.C.C (3d) 397 (S.C.C.).

**7** This case therefore requires a determination as to whether the TTC special constables were acting in the lawful execution of their duty in using force to handcuff and detain Mr. Ambrose. As a result of the credibility findings, I have made, I am satisfied that if the constables were entitled to use such force, in affecting an arrest and detention, the prosecution has proven beyond a reasonable doubt that Mr. Ambrose is guilty of the offence with which he has been charged. On the other hand, I am prepared to find Mr. Ambrose not guilty of the Criminal Code Offences if the constables were not entitled to use such force, on the basis that his actions in repelling and resisting their use of force amounted to justifiable self defence.

The Law

**8** The overarching issue involves statutory interpretation. First there must be a resolution of the apparent conflict between statutory instruments that govern policing in Ontario and the powers assigned to TTC special constables pursuant to an agreement appended to an Ontario Regulation "Exhibit A".

Status of TTC Security Officers

**9** Even though no documentary evidence was produced by the prosecution proving the designation of Mssrs. Edward and Brown as special constables, I am satisfied on the authority of R. v. Bland 20 C.C.C (2d) 332 Ont CA at page 341 that it has always been the law in Ontario that judicial notice shall be taken of the published Regulations of Ontario:

> Section 5 of the Regulations Act is a particular or "special" statute, the application of which is confined first of all to "regulations" as defined by the Act, and

secondly, to such Regulations that have been published. The words "judicial notice shall be taken of its contents and of its publication" mean just what they say and if any Court has its attention drawn to a published version of a relevant Regulation judicial notice must be taken of it. Accordingly, judicial notice must be taken of speed limits as provided in Regulations which have been duly filed and published.

See also, Section 7(2) of the Interpretation Act R.S.O. 1990, c. T.21

7.(1) Every Act shall be judicially noticed by judges, justices of the peace and others without being specially pleaded.

(2) Every proclamation shall be judicially noticed by Judges, justices of the peace and others without being specially pleaded. R.S.O. 1980, c. 219, s. 7.

**10** Consequently, it is sufficient proof of the status and powers of the special constables that the Regulation and appended agreement (Exhibit A) designating them as special constables be brought to the Court's attention along with the fact that the transit officers have both testified, without challenge, that they possessed the designation special constables on the date in question. See also R. v. Fielding [1967] 3 C.C.C 258 (BCCA) where it was held that there is a presumption that all those acting as public officers have been duly appointed until the contrary is shown. Thus on a charge of resisting arrest by an RCMP Constable, it was unnecessary to prove that the constable had been duly appointed a peace officer.

**11** It is notable that the Toronto Police Services Board pursuant to clause 30 of the aforesaid agreement (Exhibit "A") has conferred on the TTC special constables the powers of a police officer to enforce, inter alia, the Criminal Code and the Trespass to Property Act R.S.O. 1990, c. T-21 as amended.

Authority to use Force under the Trespass to Property Act

**12** The Trespass to Property Act, R.S.O. 1990, Section 9, provides that a police officer, occupier or occupier's agent may affect an arrest but the statute is silent as to who is or is not permitted to use force in so doing:

Section 9

Arrest without warrant on premises

9 - (1) A police officer, or the occupier of premises, or a person authorized by the occupier may arrest without warrant any person he or she believes on reasonable and probable grounds to be on the premises in contravention of section 2.

Delivery to police officer

(2) Where the person who makes an arrest under subsection (1) is not a police officer, he or she shall promptly call for the assistance of a police officer and give the person arrested into the custody of the police officer.

Deemed arrest

(3) A police officer to whom the custody of a person is given under subsection (2) shall be deemed to have arrested the person for the purposes of the provisions of the Provincial Offences Act applying to his or her release or continued detention and bail. R.S.O. 1990, c. T.21, s. 9.

**13** There is no question that special constables are peace officers according to the definition of "peace officer" contained in Section 2 of the Criminal Code.

**14** The real question is whether they were acting in the capacity of police officers on the date in question, imbued with the authority use force upon arrest that that status confers.

**15** The decision of Hill J. in R. v. Asante, [1996] O.J. No. 1821, - Mensah, Ontario Court of Justice (General Division) May 8 , 1996 represents an authority for the proposition that a person who is not a police officer has no power or authority to forcibly arrest under the Trespass to Property Act. He states at page 25 - 26:

> On the issue of use of force to arrest for trespass, Section 9 of the Trespass to Property Act does not confer authority to forcibly arrest (on an occupier's agent) nor does Section 146 of the Provincial Offences Act which specifically addresses the use of force to arrest for a provincial offence:
>
> use of force
>
> (1) Every police officer is, if he or she acts on reasonable and probable grounds, justified in using as much force as is necessary to do what the officer is required or authorized by law to do.
>
> use of force by citizen
>
> (2) Every person upon whom a police officer calls for assistance is justified in using as much force as he or she believes on reasonable and probable grounds is necessary to render such assistance.
>
> Where legislation specifically addresses the scope of a person's authority, recognition of the operation of a parallel and broader common law authority or privilege is generally to be avoided: Silveira v. the Queen (1995), 97 C.C.C. (3d) 450 (S.C.C.) At 464-5, 466-7 Per Cory J; Regina v. Noble (1985), 16 C.C.C. (3d) 146 (Ont. C.A.) at 172 per Martin J.A. When it has seen fit to do so, the provincial legislature has had little difficulty in expressly conferring an authority to employ reasonable force: see for example, Child and Family Services Act, R.S.O. 1990, c. C11, s. 44(2) (police officer or child protection worker); Children's Law Reform Act, R.S.O. 1990, c. C12, s. 36(5) (police officer); Environmental Protection Act, R.S.O. 1990, c. e. 19, s. 163 (a provincial officer); and, Game and Fish Act, R.S.O. 1990, c. G1, s. 8(3) (conservation officer).
>
> Section 25(1) of the Code may be seen as recognizing certain common law powers inherent in the exercise of powers of arrest. As indicated, s. 25(1) of the Code

> has no application to the instant case as a federal enactment and in the face of specific statutory provisions of the Ontario legislature addressing the issue at hand ....
>
> I do not accept that there is no public policy or societal interest in denying the use of force to a citizen performing an arrest simply because the statute, in any event, permits the intrusive action of a deprivation of liberty through conferral of a power of arrest. Inherent in the employ of physical force, to arrest and to promote restraint of a suspected offender, is the risk of an escalation of violence and the prospect of injury. There is no public interest in having persons, other than peace officers who are trained in the limits and safe avenues of use of force, engaging in the use of physical force against the person. It has been acknowledged elsewhere that standards are lower for non-peace officer security personnel: Task Force on Policing in Ontario (Report to the Solicitor General of Ontario), 1974 at p. 36.

**16** On the basis of the analysis in R. v. Asante - Mensah I am persuaded that unless the special constables had attained the status of police officers on the date in question, they had no power to use force in arresting Mr.Ambrose.

Were the Special Constables - Police Officers?

**17** The conflict arises under the Police Service Act R.S.O. 1990, c. P-15 in the definition contained in Section 2. "Police officer" is defined as follows:

> "Police officer" means a chief of police or any other police officer, but does not include a special constable, a First Nations Constable, a municipal law enforcement officer or an auxiliary in member of a police force: ("agent de police"). (emphasis added)

**18** Consequently, according to the definition a special constable cannot be a police officer. Indeed in the agreement contained in the Regulations of Ontario 1008 dated 1997.06.18 (Exhibit "A") wherein the Toronto Police Service Board empowers special constable to perform security functions in relation to the property and operations of the TT Commission, clause 10 specifically prohibits transit security officers (special constables) from identifying themselves as police officers or as employees or members of the (Toronto Police) Service.

**19** Yet, as noted before, the same agreement purports to confer upon special constables (transit security officers) the powers of a police officer.

Conclusion

**20** I have concluded that special constables are in fact police officers within the meaning of the Trespass to Property Act and entitled to use reasonable force in an arrest under that Act for the following reasons:

(1) Section 53 (3) of the Police Service Act states:

53 (3) The appointment of a special constable may confer on him or her the powers of a police officer, to the extent and for the specific purpose set out in the appointment.

This section appears to conflict with the section 2 definition especially considering that R. v. Renz (1972) 10 C.C.C (2d) 250 (Ont CA) is good authority for the view that powers confer legal status. In this case the accused was charged with impersonating a conservation officer and thereby impersonating a peace officer contrary to the Criminal Code. The issue on appeal was whether a conservation officer was a peace officer. The court concluded that conservation officer, having been vested with the powers set out in the Game and Fish Act R.S.O 1970, c. 186, of a peace officer, had powers necessary to bring him within the definition of peace officer in Section 2 of the Criminal Code. (See also R. v. Beaman [1963] 2 C.C.C 91 (S.C.C.).

(2) It has long been a rule of statutory interpretation that definitions in a statute do not trump statutory provisions where there exists an apparent conflict. For example in R. v. Scory (1965) 51 W.W.R. 447 (Sask Q.B.) it was held that the rules of interpretation require that the context must be allowed to prevail over the "artificial conceptions" of the definition clause. Consequently, in spite of the Police Services Act definition to the effect that a special constable cannot be a police officer, given that the Police Services Act [Section 53(3)] and Ontario Regulation 1008 (Exhibit "A"), permits and promulgates the conferring of the powers and functions of a police officer on a special constable, the above definition must be held to be inapplicable. In other words, the general statute must yield to the specific legislative intent contained in Sections 53(3) and Ont. Regulation 1008.

(3) The purpose of statutory interpretation remains the discovery of legislative intent, whether the enactment be a statute or a regulation: "The Interpretation of legislation in Canada" (2nd), Pierre - André Côté, les Éditions Yvon Blais Inc, Cowansville, P.Q. 1991 at page 23. The interpretation Act R.S.O. 1990, c. I-11 Section 28 provides as follows:

Implied Provisions

28. In every Act, unless the contrary intention appears,

(a) where anything is directed to be done by or before a provincial judge or a justice of the peace or other public functionary or officer, it shall be done by or before one whose jurisdiction or powers extend to the place where it is to be done;

(b) where power is given to a person, officer or functionary to do or to enforce the doing of an act or thing, all such powers shall be understood to be also given as are necessary to enable the person, officer or functionary to do or enforce the doing of the act or thing;

Utilizing this interpretive guide and bearing in mind the policy statement contained in Exhibit A" (page 1) wherein it is stated that special constables are to be empowered to perform security functions in relation to the property and operations of the T.T.C., it should be statutorily presumed that special constables are thereby granted the necessary public policing status to perform a public policing function in respect to the public property of the Toronto Transit Commission.

(4) Finally there is a presumption of statutory interpretation that favours a reading that does not produce unreasonable or unwanted results: "The interpretation of legislation in Canada", supra at pages 373 to 424. Clearly, it would not be sensible to train special constables, dress them in uniforms, and employ them to perform a public security function on TTC property and confer no more powers than a private citizen in respect to the Trespass to Property Act. It would be absurd that individuals trespassing on TTC property could impede the movement of hundreds of rush hour patrons for some illegitimate purpose, while special constables employed to ensure the comfort convenience and safety of passengers using public transportation, could do no more than utter words of arrest and then go and hunt for a police officer.

In conferring the powers of police officers on special constables by regulation, the Ontario government has made it clear that the safety and security of passengers on public transportation takes precedence over the protection of individual interests. Consistent with this clear legislative purpose, special constables who have been vested with the powers and functions of police officers on TTC property must be deemed to have assumed the status of police officers within the meaning of the Trespass to Property Act in order to carry out the security functions required under the Agreement ("Exhibit A").

Decision

**21** Having decided that the special constables were acting in the capacity of police officers and in undertaking a forcible arrest were in fact acting in the lawful execution of duty, I am satisfied that the prosecution has proven the charges before the court beyond a reasonable doubt.

**22** I feel obligated to comment that although the special constables acted within their powers of arrest, a more diplomatic solution might have been the wiser strategy in these unique circumstances. Indeed, if they had given Mr. Ambrose the P.O.A. tickets and left the area for a while, it would have been unlikely that he would have remained at that location for any length of time. This aspect of the case will be taken into account on sentencing.

qp/s/mnj

# Tab 31

# DEBTORS AND CREDITORS SHARING THE BURDEN:

## A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act

Report of the Standing Senate
Committee on Banking, Trade and Commerce

# Table of Contents

## S. Subordination of Equity Claims

Insolvency legislation in the United States has created the concept of "subordination of equity claims." Equity claims are those claims that are not based on the supply of goods, services or credit to a corporation, but rather are based on some wrongful or allegedly wrongful act committed by the issuer of an instrument reflecting equity in the capital of a corporation. Conceptually, this type of claim relates more to the loss of a claimant who holds shares or other equity instruments issued by a corporation, rather than the claims of traditional suppliers. In American legislation, such claims are subordinated to the claims of traditional suppliers.

*Canadian insolvency law does not subordinate shareholder or equity damage claims.*

Canadian insolvency law does not subordinate shareholder or equity damage claims. It is thought that this treatment has led some Canadian companies to reorganize in the United States rather than in Canada.

Mr. Kent, for example, told the Committee that "[i]f [a shareholders' rights claims by people who say that they have been lied to through the public markets] is filed in Canada, there is no facility in place to deal with it. They have no choice but to file in the U.S. where there is a vehicle to deal with these claims in a sensible, fair and reasonable way. In Canada, we have no mechanism. Thus, you end up with situations where it becomes difficult to reorganize a Canadian enterprise under Canadian law because our laws do not generally deal with shareholder claims."

He also indicated, however, that shareholder claims may be addressed within specific corporate statutes. Mr. Kent mentioned, in particular, the *Canada Business Corporations Act* and some provincial/territorial statutes, and shared his view that "[i]t becomes a lottery, depending on where the corporation is organized, whether there is a vehicle for dealing with some of these claims or there may not be. It is a hodgepodge system."

The Joint Task Force on Business Insolvency Law Reform shared with the Committee a proposal that all claims arising under or relating to an instrument that is in the form of equity are to be treated as equity claims. Consequently, "all [equity] claims against a debtor in an insolvency proceeding ... including claims for payment of dividends, redemption or retraction or repurchase or shares, and damages (including securities fraud claims) are to be treated as equity claims subordinate to all other secured and unsecured claims against the debtor ... ." It also proposed that these claims could be extinguished, at the discretion of the Court, in connection with the approval of a reorganization plan.

In view of recent corporate scandals in North America, the Committee believes that the issue of equity claims must be addressed in insolvency legislation. In our view, the law must recognize the facts in insolvency proceedings: since holders of equity have necessarily accepted – through their acceptance of equity rather than debt – that their claims will have a lower priority than claims for debt, they must step aside in a bankruptcy proceeding. Consequently, their claims should be afforded lower ranking than secured and unsecured creditors, and the law – in the interests of fairness and predictability – should reflect both this lower priority for holders of equity and the notion that they will not participate in a restructuring or recover anything until all other creditors have been paid in full. From this perspective, the Committee recommends that:

*In view of recent corporate scandals in North America, the Committee believes that the issue of equity claims must be addressed in insolvency legislation.*

**The Bankruptcy and Insolvency Act be amended to provide that the claim of a seller or purchaser of equity securities, seeking damages or rescission in connection with the transaction, be subordinated to the claims of ordinary creditors. Moreover, these claims should not participate in the proceeds of a restructuring or bankruptcy until other creditors of the debtor have been paid in full.**

# Tab 32

*Indexed as:*

# Canada 3000 Inc. (Re)

**NAV Canada, Greater Toronto Airports Authority, Winnipeg Airports Authority Inc., Halifax International Airport Authority, Edmonton Regional Airports Authority, Calgary Airport Authority, Aéroports de Montréal, Ottawa Macdonald-Cartier International Airport Authority, Vancouver International Airport Authority and St. John's International Airport Authority, Appellants/Respondents on cross-appeals**

**v.**

**International Lease Finance Corporation, Hyr Här I Sverige Kommanditbolag, IAI X, Inc., Triton Aviation International LLC, Sierra Leasing Limited, ACG Acquisition XXV LLC, ILFC International Lease Finance Canada Ltd., U.S. Airways Inc., G.E. Capital Aviation Services Inc., as Agent and Manager for Polaris Holding Company and AFT Trust-Sub I, Pegasus Aviation Inc., PALS I, Inc., Ansett Worldwide Aviation, U.S.A., MSA V, RRPF Engine Leasing Limited, Canadian Imperial Bank of Commerce, Flight Logistics Inc., C.I.T. Leasing Corporation, NBB-Royal Lease Partnership One and GATX/CL Air Leasing Cooperative Association, Respondents/Appellants on cross-appeals**

**And between**

**NAV Canada, Appellant**

**v.**

**Wilmington Trust Company and Wilmington Trust Corporation, Respondents**

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**And between**

**NAV Canada, Appellant**

**v.**

**G.I.E. Avions de transport régional, ATR Marketing Inc., Heather Leasing Corporation, Renaissance Leasing Corporation, Inter-Canadian (1991) Inc. and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents**

**And between**

**NAV Canada, Appellant**

**v. Inter-Canadian (1991) Inc., Wilmington Trust Company, Wilmington Trust Corporation, Aéroports de Montréal, Greater Toronto Airports Authority, Ottawa Macdonald-Cartier International Airport Authority and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents,**

**and**

**Aéroports de Montréal, Appellant**

**v.**

**Wilmington Trust Company, Wilmington Trust Corporation, NAV Canada, Greater Toronto Airports Authority, Ottawa Macdonald-Cartier International Airport Authority and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents,**

**and**

**Greater Toronto Airports Authority, Appellant**

**v.**

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**Ottawa Macdonald-Cartier International Airport Authority, Wilmington Trust Company, Wilmington Trust Corporation, Aéroports de Montréal, NAV Canada, Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc. and Inter-Canadian (1991) Inc., Respondents, and Ottawa Macdonald-Cartier International Airport Authority, Appellant**

**v.**

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**And between**

**NAV Canada, Appellant**

**v.**

**Inter-Canadian (1991) Inc., Renaissance Leasing Corporation, Heather Leasing Corporation, G.I.E. Avions de transport régional, ATR Marketing Inc., Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Aéroports de Montréal, Greater Toronto Airports Authority and Ottawa Macdonald-Cartier International Airport Authority, Respondents, and**

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de transport régional, ATR Marketing Inc., Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., NAV Canada, Greater Toronto Airports Authority and Ottawa Macdonald-Cartier International Airport Authority, Respondents, and Greater Toronto Airports Authority, Appellant

v.

Ottawa Macdonald-Cartier International Airport Authority, Renaissance Leasing Corporation, Heather Leasing Corporation, G.I.E. Avions de transport régional, ATR Marketing Inc., Aéroports de Montréal, NAV Canada, Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc. and Inter-Canadian (1991) Inc., Respondents, and Ottawa Macdonald-Cartier International Airport Authority, Appellant

v.

Renaissance Leasing Corporation, Heather Leasing Corporation, G.I.E. Avions de transport régional, ATR Marketing Inc. and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents

And between

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v.

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And between

Aéroports de Montréal, Appellant

v.

Newcourt Credit Group (Alberta) Inc., Canada Life Assurance Company, CCG Trust Corporation, Greater London International Airport Authority, Greater Toronto Airports Authority, Saint John Airport Inc., St. John's International Airport Authority, Charlottetown Airport

Authority Inc., Renaissance Leasing Corporation, Heather Leasing Corporation and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents, and
St. John's International Airport Authority and Charlottetown Airport Authority Inc., Appellants
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Canada Life Assurance Company, CCG Trust Corporation, Renaissance Leasing Corporation, Heather Leasing Corporation, Canadian Regional Airlines Ltd., Canadian Regional (1998) Ltd. and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents, and
Greater Toronto Airports Authority, Appellant
v.
Greater London International Airport Authority, Saint John Airport Inc., St. John's International Airport Authority, Charlottetown Airport Authority Inc., Newcourt Credit Group (Alberta) Inc., Canada Life Assurance Company, CCG Trust Corporation, Aéroports de Montréal, Renaissance Leasing Corporation, Heather Leasing Corporation, Canadian Regional Airlines Ltd., Canadian Regional (1998) Ltd. and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents
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And between
Ottawa Macdonald-Cartier International Airport Authority, Appellant
v.

**Wilmington Trust Company and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents**

**And between**

**St. John's International Airport Authority, Appellant**

**v.**

**Newcourt Credit Group (Alberta) Inc., Canada Life Assurance Company, CCG Trust Corporation, Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc. and Renaissance Leasing Corporation, Respondents**

**And between**

**Charlottetown Airport Authority Inc., Appellant**

**v.**

**CCG Trust Corporation and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Respondents**

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[2006] 1 S.C.R. 865

[2006] S.C.J. No. 24

2006 SCC 24

File Nos.: 30214, 30729, 30730, 30731, 30732, 30738,

30740, 30742, 30743, 30745, 30749, 30750, 30751.

Supreme Court of Canada

Heard: January 16, 17, 2006;
Judgment: June 9, 2006.

**Present: McLachlin C.J. and Bastarache, Binnie, LeBel, Deschamps, Fish and Charron JJ.**

(98 paras.)

**Appeal From:**

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

ON APPEAL FROM THE COURT OF APPEAL FOR QUEBEC

**Catchwords:**

*Transportation law -- Airports -- Seizure and detention of aircraft -- Airlines operating fleets of aircraft under leasing agreements with legal titleholders -- Airlines, registered owners of aircraft, incurring charges for civil air navigation and airport services -- Service providers applying to superior court judge for authorization, pursuant to s. 9 of Airport Transfer (Miscellaneous Matters) Act and s. 56 of Civil Air Navigation Services Commercialization Act, to seize and detain aircraft operated by airlines for unpaid charges incurred prior to airlines' bankruptcies -- Whether titleholders' right to repossess leased aircraft should take priority over service providers' seize and detain orders - - Whether titleholders liable to service providers for unpaid charges -- Whether seize and detain orders can be exercised against security posted by titleholders in substitution for aircraft -- Whether lessors of engines attached to detained aircraft entitled to repossess engines -- Airport Transfer (Miscellaneous Matters) Act, S.C. 1992, c. 5, s. 9 -- Civil Air Navigation Services Commercialization Act, S.C. 1996, c. 20, ss. 55, 56.*

*Legislation -- Interpretation -- Contextual interpretation -- Owner of aircraft -- Whether word "owner" in s. 55 of Civil Air Navigation Services Commercialization Act includes legal titleholders of aircraft -- Civil Air [page873] Navigation Services Commercialization Act, S.C. 1996, c. 20, s. 55.*

**Summary:**

An airline in the modern era may consist of little more than a name, with its aircraft leased, its suppliers on week to week contracts and even its reservation and yield management systems outsourced to one of the global service providers such as Sabre or Galileo. Start-ups are relatively easy, balance sheets are often thin, and failure can be quick and (to outsiders) unexpected. Yet privatized Canadian airports and NAV Canada (the privatized civil air navigation service) are obliged by statute to provide service even to financially troubled airline operators. When an operator collapses leaving unpaid bills for airport charges and air navigation services, the question becomes: who takes the financial loss, the people who ultimately own the leased aircraft or the people who were obliged to (and did) provide the airport and navigation services?

Before going bankrupt, the airline companies Canada 3000 and Inter-Canadian operated their fleets of aircraft under leasing agreements with the respondent legal titleholders and were the registered owners of the aircraft under the *Aeronautics Act*. These airlines incurred approximately $33.75 million in charges for civil air navigation and airport services provided by NAV Canada and the airport authorities pursuant to the *Airport Transfer (Miscellaneous Matters) Act* ("*Airports Act*") and the *Civil Air Navigation Services Commercialization Act* ("*CANSCA*").

*The Collapse of Canada 3000*

In November 2001, Canada 3000 applied for protection under the *Companies' Creditors Arrangement Act* ("*CCAA*"). NAV Canada and the airport authorities applied to a judge of the Ontario Superior Court of Justice, under s. 56 of *CANSCA* and s. 9 of the *Airports Act*, for authorization to seize and detain certain aircraft operated by the airline. The judge released the aircraft on the posting of security by the legal titleholders and later dismissed the seizure and detention motions, holding that the provisions in question of *CANSCA* and the *Airports Act* did not give the authorities priority over the rights of the legal titleholders to repossess the aircraft. He also held that the titleholders were not jointly and severally liable for the charges owed to NAV Canada under s. 55 of

*CANSCA*, since they were not [page874] "owners" within the meaning of the Act. The majority of the Court of Appeal upheld the motions judge's decision.

*The Collapse of Inter-Canadian*

In December 1999, the airport authorities and NAV Canada obtained, pursuant to s. 56 of *CANSCA* and s. 9 of the *Airports Act*, an order of the Quebec Superior Court to seize and detain a number of aircraft operated by Inter-Canadian. The airline was subsequently deemed to have made an assignment in bankruptcy. Faced with the legal titleholders' claims that they were entitled to repossess the aircraft, the trustee in bankruptcy applied to the Superior Court for directions. The judge allowed a motion to release the aircraft in exchange for security. He later held that the legal titleholders were jointly and severally liable for the amounts owing. The majority of the Court of Appeal overturned the motions judge's ruling, concluding that the lessors' right to repossession took priority and that the legal titleholders were entitled to the return of their aircraft free and clear of the unpaid charges.

*Held*: The appeals and cross-appeals should be allowed in part.

This case is from first to last an exercise in statutory interpretation, and the issues of interpretation are closely tied to context. Prior to *CANSCA* and the *Airports Act*, civil air navigation and airport services were provided by the federal government. Under the current legislative scheme, the privatized NAV Canada and airport authorities operate as self-funded corporations that provide services on the basis of a cost-based tariff fixed by government regulation. They cannot withhold airport or navigation services even from an obviously failing airline. At the time the measures in question here were enacted, airline insolvencies and bankruptcies had become a fact of life throughout the airline industry. The legislative scheme shows that Parliament fully appreciated that in dealing with aircraft flown in and out of jurisdictions under complex leasing arrangements, the only effective collection scheme would be to render the aircraft themselves available for seizure, and thereafter to let those interested in them resolve their dispute about where the money should come from to pay the debts due to the service providers. [paras.36-39]

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*No Joint and Several Liability for Charges for Air Navigation Services*

The appeals are dismissed with respect to NAV Canada's claim that the legal titleholders are jointly and severally liable for outstanding civil air navigation charges incurred by the registered owners and operators of the failed airlines, since the legal titleholders are not "owners" within the meaning of s. 55 of *CANSCA*. It is clear from the statutory scheme and the legislative record that Parliament intended to create a "user-pay" system for civil air navigation services, and that the only "users" of those services within the contemplation of the Act are the airlines. While in some contexts the meaning of "owner" could include legal titleholders, a purposive interpretation of s. 55 excludes them. The definition of "owner" in s. 55(2) lists only persons in possession or legal custody and control of the aircraft. Section 55(1) should be similarly construed. Interpreting the list in s. 55(2) as exhaustive of ownership for the purposes of s. 55(1) is consistent with the rest of the statutory scheme governing aeronautics, the legislative history, and conforms with common sense. If NAV Canada's interpretation of s. 55 were correct, it would mean that a seizure and detention order issued in respect of Canada 3000's unpaid user charges could in theory attach not only to a legal titleholder's aircraft leased to Canada 3000, but also to any other aircraft to which that lessor holds title, in-

cluding aircraft leased to other airlines. Moreover, to interpret "owner" as argued by NAV Canada would give preference to the ambiguous English text of s. 55 over the relatively clear French provision. A restrictive interpretation of "owner" is consistent with the policy and practice throughout the federal aeronautics scheme where the term "owner" is used to refer to the person in legal custody and control of the aircraft, not the legal titleholder. In enacting *CANSCA*, Parliament intended not to replace or override the existing regulatory framework but rather to fit cohesively within it. [paras.41-61]

*The Seizure and Detention Remedy*

Although the legal titleholders are not directly liable for the charges due to the service providers, NAV Canada and the airport authorities were entitled to orders seizing and detaining the aircraft pursuant to s. 56 of *CANSCA* and s. 9 of the *Airports Act*, and are [page876] entitled now to have their claims (as assessed by the motions judges) satisfied out of the security posted in substitution for the aircraft. Whereas s. 55 of *CANSCA* identifies a group of persons who are made legally liable for the amounts owing, the detention remedy set out in s. 9 of the *Airports Act* and s. 56 of *CANSCA* has a different focus. This court-granted remedy entitles the authorities to possess the aircraft until the debt is paid or security furnished. It does not confer any interest in the beneficial ownership of the aircraft, and it cannot be circumvented by a leasing arrangement made between an airline and an aircraft lessor. Since ss. 9(1) and 56(1) do not distinguish between the unpaid charges accumulated by specific aircraft operated by a defaulting owner or operator, the amount in respect of which the seizure of each aircraft is made is the entire amount owed by that registered owner or operator. There is no limitation of debts on an aircraft by aircraft basis. [paras.9-10] [paras.62-75] [paras.85-86]

Much of the potential unfairness complained of by the legal titleholders in the operation of the detention remedy can adequately be addressed by the motions judge. The right to seize and detain is not automatic. It requires a prior court authorization which may be subject to such terms as the court considers necessary. The court also has a discretion to limit the duration of the remedy by requiring the applicable authority to release a detained aircraft from detention prior to payment of the amount with respect to which the seizure was made. In any event, an authority that obtains an order is required to release a detained aircraft upon payment of the outstanding charges, or upon the provision of acceptable security therefor. Parliament has thus left the door open for the motions judge to work out an arrangement that is fair and reasonable to all concerned provided that the object and purpose of the remedy (to ensure the unpaid user fees are paid) is fulfilled. [para.73] [para.92]

The legal titleholders are sophisticated corporate players and are well versed in the industry in which they have chosen to invest. Since they can select which airlines they are prepared to deal with and negotiate appropriate security arrangements as part of their lease transactions, they are in a better position to protect themselves against this type of loss than are the airport authorities and NAV Canada. [paras.71-72]

The intervention of bankruptcy proceedings in both Quebec and Ontario created procedural complications. In the case of Inter-Canadian, the detention remedies [page877] were applied for well before the assignment in bankruptcy. In the case of Canada 3000, the detention remedies were applied for while the *CCAA* stay was in effect and Canada 3000 remained the registered owner of the aircraft in question. In neither case did the aircraft become part of the bankrupt estate (because ultimate ownership was in the legal titleholder). The aircraft were legitimate targets of the detention remedies as they were still sitting on a Canadian airport tarmac and were still "owned or operated"

(within the meaning of the relevant statutes) by the airlines at the relevant date. Given the authority to charge interest, the interest continues to run to the first of the date of payment, the posting of security or the bankruptcy. [para.77] [para.96]

In the proceedings involving Inter-Canadian it was not necessary for the Quebec Superior Court judge to resort to provincial law or, more specifically, to the *Civil Code of Québec*. The *Aeronautics Act*, the *Airports Act*, and *CANSCA* are federal statutes that create a unified aeronautics regime. Parliament endeavoured to create a comprehensive remedy that would be applicable across the country and would not vary from one province to another. This uniformity is especially vital since aircraft are highly mobile and move easily across jurisdictions. [paras.78-79]

Two of the respondents leased to Canada 3000 the engines attached to two of the aircraft which, when seized, were airworthy. For the present purposes, the engines are part of the aircraft in respect of which charges were incurred and that are the subject of the detention. The *Aeronautics Act* does not envisage the dismantling of the aircraft (and thus of its value as security) on the tarmac. [paras. 87-89]

**Cases Cited**

**Applied:** *Bell ExpressVu Limited Partnership v. Rex*, [2002] 2 S.C.R. 559, 2002 SCC 42; **distinguished:** *Royal Bank of Canada v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411; **referred to:** *Pan American World Airways Inc. v. The Queen*, [1981] 2 S.C.R. 565; *Heydon's Case* (1584), 3 Co. Rep. 7a, 76 E.R. 637; *Grand Trunk Railway Co. of Canada v. Hepworth Silica Pressed Brick Co.* (1915), 51 S.C.R. 81; *Bristol-Myers Squibb Co. v. Canada (Attorney General)*, [2005] 1 S.C.R. 533, 2005 SCC 26; *Dilworth v. Commissioner of Stamps*, [1899] A.C. 99; *R. v. Loblaw Groceteria Co. (Manitoba) Ltd.*, [1961] S.C.R. 138; [page878] *Slaight Communications Inc. v. Davidson*, [1989] 1 S.C.R. 1038; *Schreiber v. Canada (Attorney General)*, [2002] 3 S.C.R. 269, 2002 SCC 62; *R. v. Dubois*, [1935] S.C.R. 378; *R. v. Ulybel Enterprises Ltd.*, [2001] 2 S.C.R. 867, 2001 SCC 56; *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 S.C.R. 27; *R. v. Morgentaler*, [1993] 3 S.C.R. 463; *Aetna Financial Services Ltd. v. Feigelman*, [1985] 1 S.C.R. 2; *The Emilie Millon*, [1905] 2 K.B. 817; *Channel Airways Ltd. v. Manchester Corp.*, [1974] 1 Lloyd's Rep. 456; *Peoples Department Stores Inc. (Trustee of) v. Wise*, [2004] 3 S.C.R. 461, 2004 SCC 68; *Firestone Tire & Rubber Co. of Canada v. Industrial Acceptance Corp.*, [1971] S.C.R. 357; *Bank of America Canada v. Mutual Trust Co.*, [2002] 2 S.C.R. 601, 2002 SCC 43.

**Statutes and Regulations Cited**

*Aeronautics Act*, R.S.C. 1985, c. A-2, ss. 3(1) "aeronautical product", "registered owner", 4.4(5), 4.5.

*Airport Transfer (Miscellaneous Matters) Act*, S.C. 1992, c. 5, ss. 9, 10.

*Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, ss. 121, 122.

*Canadian Aviation Regulations*, SOR/96-433, ss. 101.01(1) "operator", "owner", 202.15 to 202.17.

*Civil Air Navigation Services Commercialization Act*, S.C. 1996, c. 20, ss. 2(1) "user", (2), 7, 8, 9, Part III, 32 to 35, 36(3)(*a*)(i), 37(4), 44, 55, 56, 57(1).

*Civil Code of Québec*, S.Q. 1991, c. 64, arts. 1592, 1593.

*Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, s. 11.31.

*Interpretation Act*, R.S.C. 1985, c. I-21, ss. 8.1, 8.2, 12.

**Treaties and Other International Instruments**

*Air Transport Agreement Between the Government of Canada and the Government of the United States of America* (1995), Annex I, s. 1.

*Convention on International Civil Aviation*, Can. T.S. 1944 No. 36, art. 19.

**Authors Cited**

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**History and Disposition:**

APPEALS and CROSS-APPEALS from a judgment of the Ontario Court of Appeal (Abella and Cronk JJ.A. and Juriansz J. (*ad hoc*)) (2004), 69 O.R. (3d) 1, 235 D.L.R. (4th) 618, 183 O.A.C. 201, 3 C.B.R. (5th) 207, [2004] O.J. No. 141 (QL), affirming in part a decision of Ground J. (2002), 33 C.B.R. (4th) 184, 5 P.P.S.A.C. (3d) 272, [2002] O.J. No. 1775 (QL). Appeals and cross-appeals allowed in part.

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APPEALS from judgments of the Quebec Court of Appeal (Nuss, Pelletier and Morissette JJ.A.), [2004] R.J.Q. 2966, 247 D.L.R. (4th) 503, [2004] Q.J. No. 11921 (QL), [2004] Q.J. No. 11922 (QL), [2004] Q.J. No. 11923 (QL), [2004] Q.J. No. 11924 (QL), [2004] Q.J. No. 11925 (QL), [2004] Q.J. No. 11926 (QL), [2004] Q.J. No. 11927 (QL), [2004] Q.J. No. 11928 (QL), [2004] Q.J.

No. 11930 (QL), [2004] Q.J. No. 11932 (QL), [2004] Q.J. No. 11933 (QL), [2004] Q.J. No. 11961 (QL), reversing, in whole or in part, decisions of Tremblay J., [2000] R.J.Q. 2935, [2000] Q.J. No. 7330 (QL), [2000] Q.J. No. 4959 (QL), [2000] Q.J. No. 4996 (QL), [2000] Q.J. No. 5004 (QL), [2000] Q.J. No. 5005 (QL), [2000] Q.J. No. 5007 (QL), [2000] Q.J. No. 5009 (QL). Appeals allowed in part.

**Counsel:**

Clifton P. Prophet and Eric Wredenhagen, for NAV Canada (30214).

Lyndon A. J. Barnes and Jean-Marc Leclerc, for Greater Toronto Airports Authority (30214).

John T. Porter and Alan B. Merskey, for Winnipeg Airports Authority Inc., Halifax International Airport Authority, Edmonton Regional Airports Authority, Calgary Airport Authority, Aéroports de Montréal, Ottawa Macdonald-Cartier International Airport Authority, Vancouver International Airport Authority and St. John's International Airport [page881] Authority (30214).

Richard A. Conway, David P. Chernos, Linda M. Plumpton and Jana N. Stettner, for International Lease Finance Corporation, Hyr Här I Sverige Kommanditbolag, IAI X, Inc., Triton Aviation International LLC, Sierra Leasing Limited, ACG Acquisition XXV LLC, ILFC International Lease Finance Canada Ltd. and U.S. Airways Inc. (30214).

Christopher W. Besant and Joseph J. Bellissimo, for G.E. Capital Aviation Services Inc., as Agent and Manager for Polaris Holding Company and AFT Trust-Sub I, Pegasus Aviation Inc., and PALS I, Inc. (30214).

Barbara L. Grossman and Christopher D. Woodbury, for Ansett Worldwide Aviation, U.S.A., and MSA V (30214).

Kenneth D. Kraft, for RRPF Engine Leasing Limited and Flight Logistics Inc. (30214).

Pamela L. J. Huff and Jill Lawrie, for C.I.T. Leasing Corporation and NBB-Royal Lease Partnership One (30214).

Written submissions only by Craig J. Hill and Roger Jaipargas, for GATX/CL Air Leasing Cooperative Association (30214).

Michel G. Ménard, for NAV Canada (30729, 30730, 30731, 30732).

Richard L. Desgagnés and Véronique E. Marquis, for Ottawa Macdonald-Cartier International Airport Authority, St-John's International Airport Authority and Charlottetown Airport Authority Inc. (30731, 30732, 30742, 30749, 30750, 30751).

Gerald N. Apostolatos, for Aéroports de Montréal (30731, 30732, 30738, 30740, 30742).

Sandra Abitan, David Tardif-Latourelle and Allon Pollack, for Greater Toronto Airports Authority (30731, 30732, 30742, 30743, 30745).

Bertrand Giroux, Markus Koehnen, Jeff Gollob, Jason Murphy, Jean-Yves Fortin and Geneviève Bergeron, for Wilmington Trust Company, Wilmington Trust Corporation, Renaissance Leasing Corporation, Heather Leasing Corporation, G.I.E. Avions de transport régional and ATR Marketing Inc. (30729, 30730, 30731, 30732, 30738, 30740, 30742, 30743, 30745, 30749, 30750).

Pierre Bourque and Eugene Czolij, for Newcourt Credit Group (Alberta) Inc., Canada Life Assurance Company and CCG Trust Corporation (30740, 30742, 30745, 30750, 30751).

No one appeared for Canadian Imperial Bank of Commerce, Inter-Canadian (1991) Inc., Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc., Greater London International Airport Authority, Saint John Airport Inc., Canadian Regional Airlines Ltd. and Canadian Regional (1998) Ltd.

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The judgment of the Court was delivered by

**1** **BINNIE J.**:-- When an airline collapses leaving unpaid bills for airport charges and air navigation services, the question becomes who takes the financial loss (or, as it is sometimes said, "the haircut"), the people who ultimately own the aircraft or the people who were obliged to (and did) provide the airport and navigation services?

**2** The question lands before the Court because of the collapse of "Inter-Canadian (1991) Inc. Airline" in 1999 and, in 2001, of Canada 3000 Airlines Ltd. and Royal Aviation Inc. (collectively "Canada [page882] 3000"). The answer depends on the statutory interpretation to be given to provisions of the *Airport Transfer (Miscellaneous Matters) Act*, S.C. 1992, c. 5 ("*Airports Act*"), and the *Civil Air Navigation Services Commercialization Act*, S.C. 1996, c. 20 ("*CANSCA*"). The important context for this interpretation is the unusual nature of the modern airline business.

**3** After decades of financial turbulence, an airline in the modern era may consist of little more than a name, with its aircraft leased, its suppliers on week to week contracts and even its reservation and yield management systems outsourced to one of the global service providers such as Sabre or Galileo. Start-ups are relatively easy, balance sheets are often thin, and failure can be quick and (to outsiders) unexpected, as the history of Canada 3000 illustrates. When a financial collapse occurs (and these have been frequent in Canada and elsewhere in the past decade), there is little meat on the corporate bones for unsecured creditors. Doing business with such airline operators carries significant financial risks, yet the appellant Canadian airports operating under government supervision are obliged by statute to allow financially troubled airlines to make use of their services (and sometimes the airport will not know if an airline is in financial trouble or not). Airport costs are largely recovered through landing fees. If these and other fees go unpaid, the airport is out of pocket for the cost of the service it was obliged by law to provide.

**4** "NAV Canada", the privatized successor to the former government-run civil air navigation system, is also obliged to offer its services to any aircraft flying through Canadian airspace on a cost-recovery basis. Its business is even riskier than that of the airports because quite often these aircraft do not even land in Canada, as in the case of transatlantic traffic flying the great circle route to and from the eastern seaboard of the United States: [page883] *Pan American World Airways Inc. v. The Queen*, [1981] 2 S.C.R. 565.

**5** When Parliament adopted its policy of privatizing major airports and navigation services in the early 1990s putting such services on a commercial footing, potential investors were expected to insist on some assurance that they would in fact be financially viable serving the chronically unstable aviation business. Thus, Parliament decided to extend to the private operators of airport and

navigation services a statutory power to apply to a superior court judge for an order to seize and detain aircraft until outstanding charges are paid, similar to the power Parliament had earlier conferred on the Crown in pre-privatization days under the *Aeronautics Act*, R.S.C. 1985, c. A-2, s. 4.5.

**6** It is worth emphasizing that no power to seize and detain as such is conferred. A superior court judge is interposed between the aircraft sought to be seized and the airports or NAV Canada. As discussed below, the role of the judge is crucial to an understanding of the statutory detention remedy.

**7** The respondents are primarily entities with the ultimate ownership of the aircraft in respect of which the charges in issue were incurred ("the legal titleholders"). Their position is that under the terms of their various leases with the defaulting airlines, they did not operate the aircraft, nor did they make use of the services for which charges were levied, nor did they derive benefit therefrom. They say that they are investors, and that when the lessees failed they were entitled to repossess their aircraft free of the charges which the defaulting airlines - not the legal titleholders - incurred. They consider it unjust that they were required in these cases to post security as a condition of removing "their" aircraft from the airports in question. The appellant airport authorities and NAV Canada, on the other hand, argue that the failure of Canada 3000 and Inter-Canadian reflects the sort of air carrier instability that Parliament rightly anticipated and in light of [page884] which it created the statutory remedies in question. Parliament must be taken to appreciate, they say, that an airline may be only a corporate shell but an aircraft under detention is a good, solid and enduring hostage for payment.

**8** I agree with the courts below that the respondent legal titleholders are not subject to personal or corporate liability to pay the unpaid charges under s. 55 of *CANSCA*. But that is not to say that the aircraft are similarly unburdened.

**9** In my view, the appellants are entitled to obtain judicially authorized seize and detain orders (hereinafter sometimes collectively referred to as the detention remedy) to be exercised against the security posted in substitution for the aircraft. The matters should be remitted to the motions judges to work out the details of the orders. Considered in the context in which the detention remedy was intended by Parliament to operate, the detention remedy cannot be circumvented as suggested by the respondents by the expedient of leasing arrangements made between the airlines and the aircraft lessors. The detention remedy is purely statutory and Parliament's intention to create an effective collection mechanism against *the aircraft* itself owned or operated by the person liable to pay the amount or charge must be given full effect.

**10** On the other hand, the appellants' remedy, if an order is granted, is limited to possession. Simple possession under the statutes does not confer any interest in the beneficial ownership of the aircraft. I do not think the appellants' further claim to the airborne equivalent of a maritime lien is well founded, nor do they have any "implied" power to sell the aircraft once detained. They get what the statute says they get - a right to apply for a judicial order to seize and detain the aircraft until payment - no more, and no less.

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**11** For the reasons that follow, I would allow the appeals and the cross-appeals in part, and return the seizure and detention applications to the respective motions judges to be dealt with in accordance with this judgment.

## I. Facts

**12** In 1992, the *Airports Act* privatized airports formerly owned and operated by the federal government. In 1996, *CANSCA* implemented the same objective in relation to Canada's civil air navigation services. Thus NAV Canada was incorporated as a non-profit corporation for the purpose of developing, operating and maintaining the civil air navigation system; see *House of Commons Debates*, vol. 133, 2nd Sess., 35th Parl., March 25, 1996, at p. 1153. *CANSCA* implemented the transfer of what was Transport Canada's civil air navigation services to NAV Canada and established the commercial and economic regulatory arrangements for the continued operation of those services; see *House of Commons Debates*, vol. 134, 2nd Sess., 35th Parl., May 15, 1996, at p. 2821.

### A. *Canada 3000*

**13** On November 8, 2001, Canada 3000 applied for protection under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). The effect of an initial court order made on the same day stayed all proceedings by creditors pending the filing of a plan of arrangement. Although the stay contemplated the continuation of operations, some five hours later the airlines' management issued a press release declaring that the airlines had ceased operations. The next day, November 9, a further order was issued grounding the fleet and providing for the return of aircraft operated by the airlines to Canada.

**14** On November 9, 2001, NAV Canada applied to the Ontario Superior Court of Justice under s. 56(1) of *CANSCA* for an authorization to seize and detain certain aircraft operated by Canada 3000. [page886] The Greater Toronto Airport Authority ("GTAA") applied for relief against Canada 3000 but did not at that time seek leave of the court to seize and detain any aircraft.

**15** On November 10, 2001, the directors and officers of Canada 3000 resigned. The next day the Canada 3000 companies were put into bankruptcy. At that time, the Canada 3000 companies owed approximately $7.4 million to NAV Canada, $13 million to the GTAA, and $8.35 million to the other Canadian airport authorities. On November 12, the GTAA moved to seize and detain aircraft under s. 9 of the *Airports Act* and on November 23, the other airport authorities applied for similar relief.

**16** The detention remedy sought by the authorities was in relation to 38 aircraft operated by the Canada 3000 companies and collectively worth approximately US $1.1 billion. Despite the existence of the legal titleholders, all of the aircraft were registered in the name of Canada 3000 as owner under the *Aeronautics Act*. Canada 3000 held leases with the various respondents in respect of 36 aircraft. The lessors retained legal title to the aircraft. At the time of the *CCAA* application, rental payments under the leases were significantly in arrears.

**17** The termination provisions varied somewhat from lease to lease. Under some, the leases came to an end and the lessors became entitled to repossession upon the granting of the *CCAA* order, under others by the cessation of operations, and under the rest by the assignment in bankruptcy. The *CCAA* stay operated, in effect, as an interim bar to repossession (see s. 11.31 *CCAA*). At the time the detention remedy was sought, the aircraft sought to be seized were grounded at the Canadian airports listed in the style of cause of the various proceedings.

**18** On December 3, 2001, after the aircraft had been grounded for close to a month, the motions judge [page887] approved the terms of their release on the posting of security for 110 percent of the amounts alleged to be owed. The motions judge then heard the seizure and detention motions through December and into January 2002, and dismissed them on May 7, 2002. The airport authorities and NAV Canada appealed and on January 20, 2004, the Ontario Court of Appeal dismissed their appeal.

B. *Inter-Canadian*

**19** Inter-Canadian operated its fleet of aircraft under leasing agreements with the legal titleholders but it too was the registered owner under the *Aeronautics Act*. On November 27, 1999, Inter-Canadian ceased operations and laid off 90 percent of its employees. At that point, it had accumulated unpaid charges totalling approximately $5 million owing to NAV Canada and to the airport authorities.

**20** Through early December 1999 the airport authorities and NAV Canada moved to seize and detain a number of the aircraft. This was authorized by four orders made by the Quebec Superior Court between December 8 and 17. Before the seizure motions were launched, however, one of the respondents, Renaissance Leasing Corporation, had purported to terminate its lease with Inter-Canadian. The aircraft nevertheless remained on the tarmac at Dorval airport.

**21** On January 5, 2000, Inter-Canadian filed a notice of intention to make a proposal to its creditors pursuant to the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3. The airline's creditors rejected its proposal in March and the company was deemed retroactively to have made an assignment in bankruptcy as of January 5. Faced with the legal titleholders' claims that they were entitled to repossession of the aircraft, the trustee in bankruptcy applied to the Superior Court for directions.

**22** On July 7, 2000, the Superior Court allowed a motion to release the aircraft in exchange for security set at 150 percent of the claims of the [page888] airport authorities and NAV Canada. On November 9, 2000, Tremblay J., having heard the application on its merits, confirmed the validity of the detention and also held the legal titleholders liable for the amounts owing. His ruling was overturned by a majority decision of the Quebec Court of Appeal, which held that the lessors' right to repossession took priority and that the legal titleholders were entitled to the return of their aircraft free and clear of the unpaid charges.

## II. Judicial History

A. *Canada 3000*

### (1) Ontario Superior Court of Justice (Ground J.)

**23** The motions judge concluded that the legal titleholders were not jointly and severally liable for the charges owed to NAV Canada under s. 55 of *CANSCA*. They were not "owners" within the meaning of the Act because none of the aircraft were registered in their name. Nor were any of the titleholders in possession of the aircraft when the charges were incurred. In his view, "the word 'owner' in [*CANSCA*] should not be interpreted to include persons who do not have custody or control of the aircraft, do not operate the aircraft, and do not make use of the air navigation services in respect of which the navigation charges are levied": (2002), 33 C.B.R. (4th) 184, at para. 52.

**24** Further, the motions judge concluded that the seizure and detention remedies found in *CANSCA* and the *Airports Act* did not create a lien or security interest that ranked in priority to the ownership or perfected security rights of third parties. He preferred the analogy of a *Mareva* injunction:

> I am not persuaded, however, that the legislation granting such detention rights should be interpreted as creating rights against third parties having ownership or perfected security interests in the aircraft such that they, in effect, become liable for the debts of third parties and must extinguish those debts before they can [page889] enforce their contractual rights to repossess the aircraft or enter into possession of the aircraft to realize on their security. [para. 43]

**25** Accordingly, he dismissed the claims of NAV Canada and the airport authorities.

(2) Ontario Court of Appeal

(a) *Cronk J.A., for the Majority*

**26** Cronk J.A. agreed with the motions judge that the titleholders were not jointly and severally liable under s. 55 of *CANSCA*. A restrictive definition of "owner" excluding legal titleholders was consistent with the user-pay model established by *CANSCA*, the broader regulatory system and the relevant legislative history, all of which demonstrated Parliament's intent to limit liability to "persons having legal custody and control and persons otherwise in possession of aircraft": (2004), 69 O.R. (3d) 1, at para. 118.

**27** Cronk J.A. also agreed that the seizure and detention provisions in *CANSCA* and the *Airports Act* do not give the authorities priority over the rights of the titleholders to repossess the aircraft:

> I conclude that the remedies under the Detention Provisions, if granted, do not create rights in the Aircraft that rank in priority to the interests in the Aircraft of the Lessors, the legal titleholders to the Aircraft, in the face of a claim for repossession and recovery of the Aircraft by the Lessors... . The Detention Provisions are intended to apply to aircraft of persons having legal custody and control or who are otherwise in possession of the aircraft. [para. 190]

**28** In the view of the majority, even if the aircraft had been properly detained, the engines attached to the aircraft and leased to Canada 3000 by two of the respondents could be removed by their respective owners. The appeal of the various authorities was dismissed.

[page890]

(b) *Juriansz J. (ad hoc), Dissenting in Part*

**29** Juriansz J. (*ad hoc*, now J.A.) would have allowed the appeal in respect of the detention remedies. In his view, these remedies focus on the aircraft and not the persons liable to pay. As long

as the aircraft is owned or operated by a person liable to pay then it may be the subject of an application to seize and detain it. The fact that other persons may have property interests in the aircraft is of no consequence:

> The remedy is "in addition to any other remedy available for the collection" of the outstanding charges. The remedy is not confined to collection of outstanding charges from persons liable for the charges. The remedy is not directed to persons at all, but rather to "aircraft", and permits the Authorities, under court supervision, to seize, to detain and to refuse to release the aircraft until somebody has satisfied the outstanding charges. [para. 255]

Juriansz J. also held that the detention provisions apply to the leased engines since they were affixed to the aircraft that were subject to the detention remedy.

B. *Inter-Canadian*

(1) Quebec Superior Court (Tremblay J.)

**30** The motions judge held the titleholders to be jointly and severally liable for the unpaid charges due to NAV Canada under s. 55 of *CANSCA*. *CANSCA* and the *Airports Act* provide for a right to retain the aircraft operated by a party that has not paid its charges. The motions judge relied on arts. 1592 and 1593 of the *Civil Code of Québec*, S.Q. 1991, c. 64, and determined that the authorities' right of retention of the aircraft took priority over the lessors' interests: [2000] R.J.Q. 2935.

**31** Accordingly, by order dated November 9, 2000, the motions judge confirmed the validity of the [page891] seizures, and declared the respondents liable to pay the overdue charges.

(2) Quebec Court of Appeal

(a) *Pelletier and Morissette JJ.A., for the Majority*

**32** Pelletier and Morissette JJ.A. reversed the motions judge's decision and absolved the legal titleholders from liability for unpaid service charges to NAV Canada under s. 55 of *CANSCA*. In their view, limiting the definition of "owner" to the enumerated categories in s. 55(2) was the only interpretation consistent with both the English and French versions of the statute and the statutory context. They noted that NAV Canada's interaction is primarily with the user of the aircraft, not the legal titleholders. They concluded, at (2004), 247 D.L.R. (4th) 503, para. 106, that

> [translation] these aircraft are in no way liable for the debts of Inter-Canadian for the simple reason that they do not belong to this debtor.

**33** Moreover, in their view, neither the airport authorities nor NAV Canada had any right to an order to seize and detain the aircraft in priority to the rights of the legal titleholders. They rejected the motions judge's resort to the *Civil Code*.

(b) *Nuss J.A., Dissenting*

**34** Nuss J.A. concluded that the intention and purpose of the statutory provisions would be defeated if the legal titleholders could obtain release of the aircraft without payment of the charges.

However, he limited the liability of a legal titleholder to an obligation to pay the charges incurred in the operation of aircraft of which it is the titleholder:

> ... the titleholder, to obtain release of its seized aircraft must only pay all the charges, in the use of the airport, incurred (and unpaid) by the operator in the operation of any aircraft owned by the same titleholder. [Emphasis added; para. 145.]

[page892]

III. Statutory Provisions

**35** The statutory provisions are reproduced in the relevant paragraphs of the reasons.

IV. Analysis

**36** This case is from first to last an exercise in statutory interpretation, and the issues of interpretation are, as always, closely tied to context. The notion that a statute is to be interpreted in light of the problem it was intended to address is as old at least as the 16th century; see *Heydon's Case* (1584), 3 Co. Rep. 7a, 76 E.R. 637. In a more modern and elaborate formulation, it is said 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" (E. A. Driedger, *Construction of Statutes* (2nd ed. 1983), at p. 87).

**37** As this Court noted in 1915, part of the context is "the condition of things existent at the time of the enactment": *Grand Trunk Railway Co. of Canada v. Hepworth Silica Pressed Brick Co.* (1915), 51 S.C.R. 81, at p. 88. At the time the measures in question here were enacted, airline insolvencies and bankruptcies had become a fact of life throughout the airline industry. Many of the planes flown in and out of and across Canada were leased to, and flown by, airlines in, or close to, bankruptcy protection. Under the interpretation offered by the respondents and the majority decisions of the Courts of Appeal, the detention remedy would be opposable to everybody but the titleholder, whose aircraft is often the only asset to survive the financial wreckage. Parliament would be taken to have intended a remedy that is least effective when it is most needed. It is more likely that Parliament fully appreciated that in dealing with aircraft flown in and out of jurisdictions under complex leasing arrangements, the only effective collection scheme is to render the aircraft themselves available for seizure, and thereafter to let those interested in them, including legal titleholders, registered owners, sublessors and operators, [page893] resolve their dispute about where the money is to come from to pay the debts due to the service providers. I should add that I agree with Juriansz J. that the legal titleholders are not without benefit from the services provided, although the benefit is indirect. Without the day to day flight operations the legal titleholders would have no business. They lease the aircraft intending them to be used in the very activities for which the services are provided. By and large, the legal titleholders are sophisticated corporations. They are knowledgeable about the ways of the industry in which they have chosen to participate.

**38** Part of the important context is the commercial reality of the marketplace where a statute is intended to function. Here the privatized appellants provide services on the basis of a cost-based

tariff fixed by regulation. Prior to *CANSCA* and the *Airports Act*, civil air navigation and airport services were provided by the federal government. Central to the statutory scheme is the fact that these service providers are self-funded and intended to be financially viable and independent; see *CANSCA*, ss. 7 and 8; *House of Commons Debates*, March 25, 1996, at pp. 1152-54. The privatized service providers do not possess the financial resources of the Crown. The statutory remedies are clearly intended to promote financial viability within a risky business environment and to make privatization attractive and practicable to potential investors.

**39** Another important commercial fact is that not only are NAV Canada and the airport authorities required to provide services according to a cost-based tariff, but they cannot withhold services from even an obviously failing airline. Pursuant to the lease agreement between Transport Canada and [page894] the Airport Authorities, the airports cannot limit the access of aircraft to their facilities except in cases of bad weather or emergency conditions; see *Ottawa Macdonald-Cartier International Airport Ground Lease*, s. 8.10.02. Similarly, NAV Canada is obligated under s. 9 of *CANSCA* to provide all users with its civil air navigation services. This reflects the obligation undertaken by Canada under international agreements; see, e.g., *Air Transport Agreement Between the Government of Canada and the Government of the United States of America*, February 24, 1995 ("*USA-Canada Open-Skies Agreement*"), Annex I, s. 1.

**40** With these preliminary comments on context (and in particular the vitally important commercial context in which these statutes were designed to operate), I turn to the two major questions raised by the appeals. Firstly are the *legal titleholders* liable for the debt incurred by the registered owners and operators of the failed airlines to the service providers? Secondly, even if they are not so liable, are *the aircraft* to which they hold title subject on the facts of this case to judicially issued seizure and detention orders to answer for the unpaid user charges incurred by Canada 3000 and Inter-Canadian?

A. *Are the Legal Titleholders Jointly and Severally Liable to NAV Canada Under Section 55 of CANSCA for Outstanding Civil Air Navigation Charges?*

**41** In my view, on a purposeful interpretation of s. 55, the answer is no. I agree with Ground J. and with the unanimous view of both Courts of Appeal that the legal titleholders are not personally liable for the unpaid charges. Section 55 provides:

> **55.** (1) [Joint and several liability] The owner and operator of an aircraft are jointly and severally liable [page895] for the payment of any charge for air navigation services imposed by the Corporation in respect of the aircraft.
>
> (2) [Meaning of "owner"] In subsection (1), "owner", in respect of an aircraft, includes
>
> (*a*) the person in whose name the aircraft is registered;
>
> (*b*) a person in possession of an aircraft as purchaser under a conditional sale or hire-purchase agreement that reserves to the vendor the title to the aircraft until payment of the purchase price or the performance of certain conditions;

> (*c*) a person in possession of the aircraft as chattel mortgagor under a chattel mortgage; and
>
> (*d*) a person in possession of the aircraft under a bona fide lease or agreement of hire.

**42** The appellants contend that the word "owner" in s. 55(1) should be given its ordinary meaning to include the legal titleholders. Who, more than they, should be considered an "owner"? The legal titleholders respond that it would be absurd to make them jointly and severally liable for civil air navigation charges related to air operations in which they did not participate, any more than the owner of a rented car should be liable for charges incurred by a renter in using a toll bridge. They point out that the practical effect of NAV Canada's argument would be mischievous. In this case, for example, Canada 3000 leased a number of aircraft from International Lease Finance Corporation ("ILFC") based in California, one of the largest aircraft leasing companies in the world. If NAV Canada's interpretation of s. 55 is correct, it would mean that a seizure and detention order issued in respect of Canada 3000's unpaid user charges could in theory attach not only to the ILFC aircraft leased to Canada 3000, but also to any other aircraft to which ILFC holds title, including aircraft leased to other airlines (e.g. Lufthansa, British Airways or United Airlines). Thus the wreckage created by Canada 3000's collapse could spread disruption widely and [page896] perhaps unjustifiably trigger a further crisis in other airlines.

**43** It seems clear from the statutes and the legislative record that Parliament intended to create a "user-pay" scheme for civil air navigation services, and that the only "users" of the civil air navigation services within the contemplation of the Act are the airlines, not the legal titleholders.

(1) The Meaning of "Owner"

**44** If s. 55(1) were read in isolation, the ordinary and grammatical meaning of "owner" would include the legal titleholder. However, this Court held, in *Bell ExpressVu Limited Partnership v. Rex*, [2002] 2 S.C.R. 559, 2002 SCC 42, that

> one must consider the "entire context" of a provision before one can determine if it is reasonably capable of multiple interpretations... .
>
> ... It is necessary, in every case, for the court charged with interpreting a provision to undertake the contextual and purposive approach set out by Driedger, and *thereafter* to determine if "the words are ambiguous ...". [Underlining added; paras. 29-30.]

**45** Accordingly, to paraphrase the Court's decision in *Bristol-Myers Squibb Co. v. Canada (Attorney General)*, [2005] 1 S.C.R. 533, 2005 SCC 26, it is necessary to suspend judgment on the precise scope of the word "owner" in s. 55(1) and first to examine the "contextual" elements of the Driedger approach.

(2) Statutory Context of Section 55

**46** Understandably, the appellants lay great emphasis on the fact that s. 55(2) is introduced by the words

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> In subsection (1), "owner", in respect of an aircraft, includes ... .

followed by a list of four subsections. In the French text, on the other hand, the introductory words are

> *Pour l'application du paragraphe (1), "propriétaire", relativement à un aéronef, s'entend* ... .

There was, as might be expected, much argument over the words "includes" and "*s'entend*" in s. 55(2). NAV Canada argues that "includes" expands the definition of owner beyond the enumerated groups and that its ordinary meaning encompasses titleholders. The legal titleholders respond that the sense of "*s'entend*" in the French text is usually conveyed by the English word "means", which generally precedes a definition to be construed as exhaustive, and which would therefore exclude them from personal liability.

**47** The English word "includes" may also, depending on the context, precede a list that exhausts the definition; see, e.g., *Dilworth v. Commissioner of Stamps*, [1899] A.C. 99 (P.C.), at pp. 105-6; *R. v. Loblaw Groceteria Co. (Manitoba) Ltd.*, [1961] S.C.R. 138.

**48** In this case, in my view there are three significant reasons for adopting a restrictive interpretation of the word "includes" in s. 55(2), and thereby excluding the legal titleholders from liability under s. 55(1).

**49** Firstly, it *is* significant that the French version signals a closed list; see Uniform Law Conference of Canada, *Drafting Conventions for the Uniform Law Conference of Canada* (online), s. 21(4) . The shared meaning is not conclusive when such an interpretation would be contrary to the purpose and intent of the statute, but it is preferred; see *Slaight Communications Inc. v. Davidson*, [1989] 1 S.C.R. 1038, at pp. 1070-72; *Schreiber v. Canada (Attorney General)*, [2002] 3 S.C.R. 269, 2002 SCC 62, at para. 56; and R. Sullivan, *Sullivan and Driedger on the Construction of Statutes* (4th ed. 2002), at pp. 79-90. Further, where one of the linguistic versions is broader than the other, the common meaning favours the more restricted or limited meaning; [page898] see *Schreiber*; *R. v. Dubois*, [1935] S.C.R. 378. As the English version is ambiguous, indicating that the list could be exhaustive or expansive depending on the context, the fact that the relatively clear French version signals that "owner" is restricted to the persons listed in s. 55(2) is a factor weighing against NAV Canada's expansive interpretation.

**50** Secondly, I conclude (as did the Courts of Appeal) that interpreting the list enumerated in s. 55(2) as exhaustive of ownership for the purposes of s. 55(1) is consistent with the regulatory scheme as a whole and its legislative history, outlined below. In restricting "owner" to those in possession and legal custody and control of the aircraft, s. 55(2) is brought into conformity with the meaning that the word "owner" carries throughout the interlocking statutes that regulate aeronautics. For example, under the *Canadian Aviation Regulations*, SOR/96-433 ("*CARs*"), only a person who has legal custody and control may be a registered owner. Sections 55(2)(*b*) to (*d*) all explicitly state that the "owner" must be in possession of the aircraft. Also of significance is s. 55(2)(*d*), which in-

cludes as owner someone "in possession of the aircraft under a bona fide lease". No reference is made therein to the lessor. Parliament put its mind to aircraft leasing agreements and decided that the person in possession of the aircraft is the owner for the purposes of user charges.

**51** Thirdly, exclusion of legal titleholders is consistent with Parliament's manifest intent to limit the scope of liability to "users" of NAV Canada's civil air navigation services. Section 32 of *CANSCA* authorizes NAV Canada to impose charges only on a "user", which s. 2(1) of the Act defines as "an aircraft operator." Part III of *CANSCA* lays out detailed mechanisms through which NAV Canada may impose fees. All of its provisions contemplate that it is the user who will be charged. Section 36(3)(*a*)(i) states that notice of changes to existing [page899] charges and notice of new charges must be sent to representative user organizations. Section 37(4) states that NAV Canada must advise representative user organizations once a new charge has been approved. Section 44 limits the right to appeal charges to "any user, group of users or representative organization of users".

**52** In contrast, titleholders are not provided with notice of rates or accounts of the charges that their aircraft accumulate. In this case, the respondents in the Canada 3000 case were only notified of the $7.4 million owing to NAV Canada the day before the airline filed for protection under the *CCAA*. Thus Cronk J.A. observed that

> the charges scheme of the *CANSCA* does not protect aircraft lessors and secured creditors from the possible imposition by NAV Canada of improper or arbitrary navigation charges precisely because it is not envisaged that such persons will have any liability for such charges. [para. 101]

**53** In summary, in my view, the statutory context supports the exclusion of the legal titleholders from the definition of owner under s. 55 of *CANSCA*.

(3) The Broader Legislative Framework

**54** As stated, aeronautics in Canada is governed by a complex web of statutes, regulations and international conventions. *CANSCA* and the *Airports Act* are part of this broader legislative framework. In *R. v. Ulybel Enterprises Ltd.*, [2001] 2 S.C.R. 867, 2001 SCC 56, the Court emphasized, at para. 52, "the principle of interpretation that presumes a harmony, coherence, and consistency between statutes dealing with the same subject matter". See also *Bell ExpressVu*, at para. 27.

**55** The policy and practice throughout the federal regulatory scheme is to use the term "owner" to refer to the person in legal custody and control of [page900] the aircraft, not the legal titleholder. The *CARs*, for example, define owner as "the person who has legal custody and control of the aircraft" (s. 101.01(1)). The *Aeronautics Act* refers only to "registered owners" and, under s. 4.4(5), only the operator or *registered* owner may face liability for charges imposed under that Act. Section 3(1) defines a registered owner as the person to whom a certificate of registration has been issued and the *CARs* make clear that an aircraft may only be registered by an owner who, again, must have legal custody and control of the aircraft; see ss. 202.15 to 202.17. Section 2(2) of *CANSCA* itself states that "[u]nless a contrary intention appears, words and expressions used in this Act have the same meaning as in subsection 3(1) of the *Aeronautics Act*." I appreciate that arguments are available to counter these points but in my view the legal titleholders have the better side of the debate.

**56** Internationally, the *Convention on International Civil Aviation*, December 7, 1944, Can. T.S. 1944 No. 36 (the "Chicago Convention"), does not require legal title to correspond with registered ownership. Article 19 states that registration shall be in accordance with the laws of the contracting State. It is common ground that, by virtue of ss. 202.15, 202.16 and 202.17 of the *CARs*, an aircraft may only be registered in the Canadian Civil Aircraft Register by the "owner" of the aircraft as that term is defined under s. 101.01(1) of the *CARs*, and that that person is the entity having legal custody and control of the aircraft. Thus an airline operating aircraft in Canada under a long-term lease is named on the Certificate of Registration as "owner" of the aircraft, notwithstanding that title is actually held by the lessor; see D. H. Bunker, *Canadian Aviation Finance Legislation* (1989), at p. 764. We have been given no reason why the privatization legislation should be held to depart so strikingly from Canadian regulatory practice.

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(4) Legislative History

**57** Though of limited weight, Hansard evidence can assist in determining the background and purpose of legislation; *Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 S.C.R. 27, at para. 35; *R. v. Morgentaler*, [1993] 3 S.C.R. 463, at p. 484. In this case, it confirms Parliament's apparent intent to exclude legal titleholders from personal liability for air navigation charges. The legislative history and the statute itself make it clear that Parliament did not intend *CANSCA* to replace or override the existing regulatory framework but rather to fit cohesively within it. In introducing *CANSCA*, the Minister of Transport stated that the *Aeronautics Act*, which establishes the essential regulatory framework to maintain safety in the aviation industry, "will always take precedence over the commercialization legislation" (*House of Commons Debates*, March 25, 1996, at p. 1154). In the Ontario Court of Appeal, Cronk J.A. highlighted a number of other instances where government spokespersons emphasized to Members of Parliament that *CANSCA* was to fit within the existing regulatory framework which generally favours the narrow meaning of "owner"; see, e.g., *House of Commons Debates*, May 15, 1996, at p. 2834; May 29, 1996, at p. 3144; June 4, 1996, at pp. 3394 and 3410; and *Debates of the Senate*, vol. 135, 2nd Sess., 35th Parl., June 10, 1996, at pp. 588-89.

**58** In 1985, during passage of the *Aeronautics Act*, a concern was raised in Parliament that liability under s. 4.4(5) (that Act's liability provision) could extend to legal titleholders. In response, the Government inserted the term "registered owner". The Parliamentary Secretary to the Minister of Transport specifically stated that the change was made to ensure that liability did not extend to those who had a security or other financial interest in the aircraft; *House of Commons Debates*, vol. IV, 1st Sess., 33rd Parl., June 20, 1985, at pp. 6065-66.

**59** In 1996, the Government considered Bill C-20 (which became *CANSCA*) as it transferred the [page902] operation of the civil navigation system from Transport Canada to NAV Canada. The Clause by Clause Analysis brief presented to the Senate Committee explained that s. 55 is based on the wording of the equivalent section of the *Aeronautics Act* which, as stated, restricts "owner" to *registered* owner; see "Clause by Clause Analysis for the *Civil Air Navigation Services Commercialization Act*", as presented to the Senate Committee on Transport and Communications, at pp. 51-52. However, the textual discrepancy noted above was not addressed.

(5) Conclusion on the Section 55 Issue

**60** A purposive interpretation of s. 55 that takes into account the foregoing considerations compels rejection of the position urged by NAV Canada. Moreover, and importantly, the narrow interpretation of "owner" in s. 55(1) conforms with common sense. It would be a severe disruption to the functioning of the airline industry if, as a result of Canada 3000's failure to pay its charges, NAV Canada could seize and detain an aircraft operated by, for example, Air Canada. There is no reason to think Parliament intended to let the damage caused by a failed airline expand beyond that airline's fleet of aircraft.

**61** Accordingly, applying Driedger's contextual approach to s. 55(1) of *CANSCA*, I agree with the Courts of Appeal that the titleholders of the aircraft are *not* jointly and severally liable for the charges due to NAV Canada. They are not "owners" within the meaning of that section.

B. *The Detention Remedy*

**62** If the legal titleholders are not directly liable for the charges due to the service providers, they argue that it would be unfair and contradictory to hold their aircraft hostage for the payment. Section 56 of *CANSCA* and s. 9 of the *Airports Act* should be [page903] interpreted consistently with s. 55(1) of *CANSCA*, the legal titleholders argue, and their right to repossess the aircraft on termination of the lease should take priority over the statutory remedy.

**63** On the other hand, Nuss J.A., dissenting in the Quebec Court of Appeal, put the contrary position:

> If the titleholder could obtain release of the seized aircraft without the payment of the outstanding charges or providing security, the intention and purpose of the Detention Provisions enacted by Parliament would be defeated. This is so because the debt is constituted of charges incurred by the operator of the aircraft (who is often, as in this case, the registered owner) and not by the titleholder. Thus, if the contention of [the titleholders] were to prevail, the titleholder, who is neither the operator nor the "owner" within the meaning of the statutes, could always obtain release of the aircraft and the charges would not be paid. The recourse provided by Parliament would, inevitably, be of no avail. [para. 126]

I believe that Nuss J.A. is correct on this point.

**64** The relevant provisions, which authorize applications to a superior court judge of the province in which any aircraft owned or operated by the person liable to pay the charge or amount is situated, are expressed in the two statutes in similar terms.

**65** Section 56 of *CANSCA* provides:

> **56.** (1) [Seizure and detention of aircraft] In addition to any other remedy available for the collection of an unpaid and overdue charge imposed by the Corporation for air navigation services, and whether or not a judgment for the collection of the charge has been obtained, the Corporation may apply to the superior court of the province in which any aircraft owned or operated by the per-

son liable to pay the charge is situated for an order, issued on such terms as the court considers appropriate, authorizing the Corporation to seize and detain any such aircraft until the charge is paid or a bond or other security for the unpaid and overdue amount in a form satisfactory to the Corporation is deposited with the Corporation.

(2) [Application may be *ex parte*] An application for an order referred to in subsection (1) may be made [page904] *ex parte* if the Corporation has reason to believe that the person liable to pay the charge is about to leave Canada or take from Canada any aircraft owned or operated by the person.

(3) [Release] The Corporation shall release from detention an aircraft seized under this section if

*(a)* the amount in respect of which the seizure was made is paid;

(*b*) a bond or other security in a form satisfactory to the Corporation for the amount in respect of which the seizure was made is deposited with the Corporation; or

*(c)* an order of a court directs the Corporation to do so.

**66** Section 9 of the *Airports Act*, under which the airport authorities bring their seizure and detention applications, is to the same effect.

**9.** (1) [Seizure and detention for fees and charges] Where the amount of any landing fees, general terminal fees or other charges related to the use of an airport, and interest thereon, set by a designated airport authority in respect of an airport operated by the authority has not been paid, the authority may, in addition to any other remedy available for the collection of the amount and whether or not a judgment for the collection of the amount has been obtained, on application to the superior court of the province in which any aircraft owned or operated by the person liable to pay the amount is situated, obtain an order of the court, issued on such terms as the court considers necessary, authorizing the authority to seize and detain aircraft.

(2) [Idem ] Where the amount of any fees, charges and interest referred to in subsection (1) has not been paid and the designated airport authority has reason to believe that the person liable to pay the amount is about to leave Canada or take from Canada any aircraft owned or operated by the person, the authority may, in addition to any other remedy available for the collection of the amount and whether or not a judgment for the collection of the amount has been obtained, on *ex parte* application to the superior court of the province in which any aircraft owned or operated by the person is situated, obtain an order of the court,

issued on such terms as the court considers necessary, authorizing the authority to seize and detain aircraft.

(3) [Release on payment] Subject to subsection (4), except where otherwise directed by an order of a court, [page905] a designated airport authority is not required to release from detention an aircraft seized under subsection (1) or (2) unless the amount in respect of which the seizure was made is paid.

(4) [Release on security] A designated airport authority shall release from detention an aircraft seized under subsection (1) or (2) if a bond, suretyship or other security in a form satisfactory to the authority for the amount in respect of which the aircraft was seized is deposited with the authority.

(5) [Same meaning] Words and expressions used in this section and section 10 have the same meaning as in the *Aeronautics Act*.

**67** According to these provisions, the airport authorities or NAV Canada (upon obtaining a court order) may take possession of an aircraft and detain it. The aircraft must be either "owned" or "operated" by a person who is liable to pay. Either is a sufficient basis for an application.

**68** The key difference between the joint and several liability provisions in s. 55 of *CANSCA* and the detention remedy provided for in s. 56 of *CANSCA* and s. 9 of the *Airports Act* is that the seizure and detention remedy lies against the aircraft. Whereas s. 55 identifies a group of *persons* who are made legally liable for the amounts owing, the detention remedy has a different focus. It provides for a right to possess *aircraft* until the debt is paid or security provided.

**69** The legal titleholders argue that the claim of NAV Canada and the airport authorities to detain the aircraft must yield to their right under their respective leases to repossession. They liken the seizure and detention remedies to a *Mareva* injunction, in which the assets are frozen while various parties work out their respective entitlements; see *Aetna Financial Services Ltd. v. Feigelman*, [1985] 1 S.C.R. 2. However, in my view, there is no need to resort to analogies, especially loose analogies (e.g. *Mareva* injunctions are interlocutory, whereas the detention remedy is available whether or not a judgment for the collection of the charge or amount has been obtained. Moreover, *Mareva* injunctions are directed at persons (*Aetna Financial Services*, [page906] at pp. 25-26), whereas the seizure and detention remedy targets the aircraft itself).

**70** The *CARs*, adopted pursuant to the *Aeronautics Act*, provide that an "operator" in respect of an aircraft "means the person that has possession of the aircraft as owner, lessee or otherwise" (s. 101.01(1)). At the dates of the applications for seizure and detention orders, Canada 3000 and Inter-Canadian were still the *registered* owners of the aircraft. Accordingly, if the Court is to read the words of the detention remedy in the context of the realities of this industry previously discussed, it seems to me that those remedies must be available against the aircraft of Canada 3000 (except any aircraft already repossessed by the titleholder prior to the *CCAA* application on November 8, 2001) and Inter-Canadian. (Once a titleholder reclaims possession, it becomes an operator in possession within s. 55(1) of *CANSCA*. However, as its possession post-dates the charges, no personal liability is incurred on that account.)

**71** It is difficult to endorse the indignation of the legal titleholders with respect to detention of their aircraft until payment is made for debts due to the service providers. They are sophisticated corporate players well versed in the industry in which they have chosen to invest. The detention remedies do not affect their ultimate title. Investors who have done their due diligence will recognize that detention remedies have deep roots in the transport business. In *The Emilie Millon*, [1905] 2 K.B. 817 ("*Mersey Docks*"), for example, the English Court of Appeal examined a statute that stipulated that the Mersey Docks and Harbour Board could cause a ship to be detained until all harbour and tonnage payments had been made despite the fact that the ownership of the ship did not correspond to the debtor who had incurred the charges. The ruling in that case reflects the traditional scope of this type of remedy (at p. 821):

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> The Mersey Docks and Harbour Board have a right by statute to detain the vessel until the dock tonnage rates and harbour rates are paid. That is an express statutory right, and the board have nothing to do with any sale of the vessel to a purchaser. That is a matter which only concerns those who are interested in the vessel. It does not concern the board. The board are entitled to detain the vessel, whoever is the owner, until the rates are paid. The order appealed against deprives them of that right, and without their consent purports to give them an option to try and make some claim to a lien upon or right against the fund in priority to other claimants. The board have no such lien or right. If this vessel had been allowed to leave the dock, the board would have been left to make a futile claim against the fund in court. [Emphasis added.]

This type of provision is not uncommon in the airline business, see, e.g., decisions under a differently worded U.K. Act such as *Channel Airways Ltd. v. Manchester Corp.*, [1974] 1 Lloyd's Rep. 456 (Q.B.), at p. 461, in which it was held that the *Manchester Corporation Act* "mean[t] what it sa[id]", and that the city could detain aircraft in respect of which charges had been incurred until those charges had been paid. The legal titleholders face this problem on the other side of the Atlantic. It is a risk they manage there. No reason was given as to why they cannot manage it here.

**72** The legal titleholders are in a better position to protect themselves against this type of loss than are the airport authorities and NAV Canada. The legal titleholders can select which airlines they are prepared to deal with and negotiate appropriate security arrangements as part of their lease transactions with the airlines. In the case of the aircraft at issue in these appeals, many if not all of the leases provided for substantial security deposits. For example, the total amount posted by Canada 3000 to the ILFC as security deposits for airport fees and charges was approximately $15,305,500. It is unnecessary to catalogue all of the possible security arrangements, but these deposits demonstrate a legal titleholder's ability to negotiate protection at a time when the airline is solvent to cover the amounts in overdue charges that the airline may [page908] eventually be required to pay to the statutory service providers.

**73** I agree with Cronk J.A. (at para. 133) that the detention remedy under the statutes is subject to several constraints: (i) the remedy is not automatic and requires prior court authorization; (ii) the

remedy is discretionary and may be subject to such terms as the court considers necessary; (iii) under s. 9(3) of the *Airports Act* and s. 56(3)(*c*) of *CANSCA*, the court also has a discretion to limit the duration of the remedy by requiring the applicable authority to release a detained aircraft from detention prior to payment of the amount with respect to which the seizure was made; (iv) in any event, an authority that obtains an order under the detention provisions is required to release a detained aircraft upon payment of the outstanding amount or charges in respect of which the seizure was made or upon the provision of acceptable security therefor (ss. 9(3) and 9(4) of the *Airports Act* and ss. 56(1) and 56(3) of *CANSCA*); and (v) an order is not available under the detention provisions if the aircraft in respect of which the order is sought is exempt from seizure and detention under provincial law (s. 10(1) of the *Airports Act* and s. 57(1) of *CANSCA*) or, in the case of the *Airports Act*, under a regulation made by the Governor in Council (s. 10(2)).

**74** On the other hand, the conclusion of Juriansz J., dissenting in part, was correct that "the wording of the Detention Provisions makes apparent that aircraft may be seized and detained without regard to the property interests of persons who are neither the registered owners nor the operators of the aircraft under the legislation. As long as the aircraft is owned or operated by a person liable to pay the outstanding charges, it may be the subject of an application to seize and detain it. The fact that there may be other persons, who are not liable to pay the outstanding charges but have property interests in the aircraft, is of no consequence" (para. 239).

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**75** I turn, then, to a number of additional arguments raised on both sides which, in my view, with respect, unnecessarily complicate a straightforward task of statutory interpretation.

(1) Whether or Not a Lien Existed

**76** In the Ontario case, there was considerable debate about whether the detention remedy created a lien. However, as the English Court of Appeal commented in *Mersey Docks*, there was no need for the port authority "to ... make some claim to a lien" (p. 821). Nor is it necessary here. In this case, as in *Mersey Docks*, the remedy is purely a creature of statute. Whether or not a lien could be said to arise by operation of law is perhaps of theoretical interest but it has no practical bearing on the result in these appeals.

(2) Effect of the Bankruptcy Proceedings

**77** The intervention of bankruptcy proceedings in both Quebec and Ontario created procedural complications. For present purposes, it is sufficient to note that the detention remedies in Quebec were applied for well before the assignment in bankruptcy. In Ontario, the detention remedies were applied for while the *CCAA* stay was in effect and Canada 3000 remained the registered owner of the aircraft in question. In neither case did the aircraft become part of the bankrupt estate (because ultimate ownership was in the legal titleholder). The aircraft were nevertheless legitimate targets of the detention remedies as they were still sitting on a Canadian airport tarmac and were still "owned or operated" (within the meaning of the relevant statutes) by the airlines at the relevant date.

(3) Resort to the *Civil Code of Québec*

**78** In the Quebec Superior Court, Tremblay J. held that the seizure and detention provisions create a right similar to that found in arts. 1592 and 1593 of [page910] the *Civil Code of Québec*. However, with respect, there is no need to make reference to provincial law or, more specifically, to the *Civil Code*, and to do so here is inappropriate. Section 56 of *CANSCA* and s. 9 of the *Airports Act* specifically state that the remedy is to be "in addition to any other remedy", which includes remedies under provincial law.

**79** The *Aeronautics Act*, the *Airports Act* and *CANSCA* are federal statutes that create a unified aeronautics regime. Parliament endeavoured to create a comprehensive code applicable across the country and not to vary from one province to another. This uniformity is especially vital since aircraft are highly mobile and move easily across jurisdictions.

**80** NAV Canada also relied on ss. 8.1 and 8.2 of the *Interpretation Act*, R.S.C. 1985, c. I-21, to urge that s. 56 of *CANSCA* provides for a *civiliste* right of retention . However, neither section applies in this case. Section 8.1 states that

> if in interpreting an enactment it is necessary to refer to a province's rules, principles or concepts forming part of the law of property and civil rights, reference must be made to the rules, principles and concepts in force in the province at the time the enactment is being applied.

If it were *necessary* to resort to provincial law, then the provincial law to be used is that of the province in which the provision is being applied: *Peoples Department Stores Inc. (Trustee of) v. Wise*, [2004] 3 S.C.R. 461, 2004 SCC 68. Here, for reasons stated, resort to provincial law is not necessary.

**81** Section 8.2 of the *Interpretation Act* states that

> when an enactment contains both civil law and common law terminology, or terminology that has a different meaning in the civil law and the common [page911] law, the civil law terminology or meaning is to be adopted in the Province of Quebec and the common law terminology or meaning is to be adopted in the other provinces.

**82** The issue here is not one of conflicting terminology. The language used in relation to the detention remedy is perfectly apt to make Parliament's intention clear bilingually and bijuridically. In short, resort to the *Civil Code* was neither necessary nor appropriate.

(4) Existence of a Power of Sale

**83** The appellants argue that the existence of a seizure and detention implies (in their favour) a power of sale. No such power is contained in *CANSCA* or the *Airports Act*. Nor is it necessarily implied in the creation of a power to seize and detain. The only claim that the authorities have under federal aeronautics law is the claim to possession of the aircraft until their user charges are paid.

(5) Presumption Against Interference With Private Rights

**84** The Ontario motions judge applied a narrow approach to the Detention Remedy on the basis that it invades what would otherwise be the proprietary rights of the legal titleholders. Reference was made to *Royal Bank of Canada v. Sparrow Electric Corp.*, [1997] 1 S.C.R. 411, where it was

held that the legislation at issue in that case did not impose a charge in the nature of a lien because of the absence of clear and unambiguous language. However, only if a provision is ambiguous (in that after full consideration of the context, multiple interpretations of the words arise that are equally consistent with Parliamentary intent), is it permissible to resort to interpretive presumptions such as "strict construction". The applicable principle is not "strict construction" but s. 12 of the *Interpretation Act*, which provides that every enactment "is deemed remedial, and shall be given such fair, large and liberal construction and interpretation as best ensures the attainment of its objects"; see *Bell ExpressVu*, at para. 28:

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> Other principles of interpretation - such as the strict construction of penal statutes and the "*Charter* values" presumption - only receive application where there is ambiguity as to the meaning of a provision. (On strict construction, see: *Marcotte v. Deputy Attorney General for Canada*, [1976] 1 S.C.R. 108, at p. 115, *per* Dickson J. (as he then was); *R. v. Goulis* (1981), 33 O.R. (2d) 55 (C.A.), at pp. 59-60; *R. v. Hasselwander*, [1993] 2 S.C.R. 398, at p. 413; *R. v. Russell*, [2001] 2 S.C.R. 804, 2001 SCC 53, at para. 46... .)

In my view, there is no ambiguity in the statutory language creating the detention remedy and thus resort to "strict construction" is not called for.

(6) Limitation of Debts on an Aircraft by Aircraft Basis

**85** The titleholders argue that it would be extremely unfair that one titleholder's aircraft, however recently leased, may ultimately be held hostage for all of the unpaid user charges of the airline that flew it. They contend that if (which they deny) the titleholders must pay charges in order to recover an aircraft, they should only be required to pay the charges incurred by the individual aircraft sought to be released, as opposed to the charges outstanding in relation to the whole fleet of the defaulting airline.

**86** However, the statute says that an aircraft operated by the person liable to pay the amount can be seized and, absent further court order, need not be released until the entire amount owed by that *operator* has been paid. This point is made clearly by the release provisions in s. 9(3) of the *Airports Act* and s. 56(3) of *CANSCA*. The authorities must only release the aircraft if "the amount in respect of which the seizure was made is paid". Since s. 9(1) and s. 56(1) do not distinguish between the amounts accumulated by specific aircraft operated by a defaulting owner or operator, it seems clear that the amount in respect of which the seizure was made is the entire amount owed by that registered owner or operator.

[page913]

(7) Limitation of Seizure to Exclude Engines

**87** Two of the respondents, RRPF Engine Leasing Ltd. and Flight Logistics Inc. (the "engine lessors"), leased to Canada 3000 the engines attached to two of the aircraft which, when seized, were airworthy. The engine lessors argue that they should be entitled to repossess their engines because seizure of the aircraft is not seizure of the engines. They cite Laskin J. (as he then was) in *Firestone Tire & Rubber Co. of Canada v. Industrial Acceptance Corp.*, [1971] S.C.R. 357, for the proposition that the doctrine of accession does not apply to a removable and identifiable object such as the engines.

**88** In my view, the engines are part of the aircraft for present purposes. Engines and equipment such as onboard computers fall under the definition of "aeronautical product" in the *Aeronautics Act* (s. 3(1)). If the engines could be removed, third-party lessors could cannibalize any "aircraft propeller or aircraft appliance or part or the component parts of any of those things, including any computer system and software"; see *Aeronautics Act*, s. 3(1).

**89** *Firestone Tire* is not of assistance here. In that case, a truck was repossessed under a conditional sales contract. The vendor in possession of the seized truck sought to retain the tires mounted on the truck as against the claim of the unpaid conditional seller of the tires. Laskin J. was concerned about the windfall one creditor might receive when repossessing the property of another unpaid creditor for which he "has given no value" (p. 359). Here, no beneficial interest is implicated. The engines are attached to the aircraft in respect of which charges were incurred and that are the subject of the detention. The Act does not envisage the dismantling of the aircraft (and thus of its value as a security) on the tarmac.

[page914]

(8) Effect of Sub-Leases

**90** The respondents Ansett Worldwide Aviation, U.S.A. and MSA V leased three aircraft to Canada 3000, two of which, in turn, had been leased by those respondents from other persons under head leases. These sub-lessors stand in no better position than the legal titleholders, and the aircraft in which they have a leasehold interest were subject to seizure.

C. *The Important Role of the Motions Judge*

**91** The detention remedy does not create any rights unless, and until, a court order is made authorizing the seizure and detention of an aircraft. Instead, the provisions create potential remedies, available at the discretion of the court and subject to such conditions as the court considers necessary, as Cronk J.A. noted, at para. 134.

**92** Much of the potential unfairness which the titleholders envisage in the operation of the detention remedy can be addressed by the motions judge. Section 56(3)(*c*) of *CANSCA* states that NAV Canada must release the aircraft "if ... an order of a court directs the Corporation to do so". Similarly, s. 9(3) of the *Airports Act* states that an airport authority need not release the aircraft until the charges are paid, "except where otherwise directed by an order of a court". Parliament has left the door open for the motions judge to work out an arrangement that is fair and reasonable to all

concerned, provided that the object and purpose of the remedy (to ensure the unpaid user fees are paid) is fulfilled. It would be open to a judge on a detention remedy hearing to determine an allocation amongst the titleholders that reflected such factors as the number of seized aircraft, the amount of charges in relation to a particular aircraft or the short duration of an aircraft's life spent in the doomed fleet. The judge need not make each aircraft hostage for the full amount of the unpaid charges, provided the result is that the authority is paid in full. In this way, what may otherwise be portrayed as a draconian [page915] remedy can be reduced to a fair and proportionate judicial response to the airline collapse.

D. *Interest*

**93** The *Airports Act* explicitly authorizes the airport authorities to charge interest on the overdue amounts. Section 9(1) defines the amount on account of which the seizure was made as the "amount of any landing fees, general terminal fees or other charges related to the use of an airport, and interest thereon". While *CANSCA* makes no explicit mention of interest, ss. 32 to 35 lay out a broad authority for NAV Canada to set and charge its fees. A procedure has been established under s. 35(1)(*a*), whereby the Minister of Transport approves the charges imposed by NAV Canada. The Minister has approved a regulation imposing interest. Notice was provided to airline operators (although not the legal titleholders) and no judicial review of this regulation was sought.

**94** The time value of money is universally accepted in ordinary commercial practice; see *Bank of America Canada v. Mutual Trust Co.*, [2002] 2 S.C.R. 601, 2002 SCC 43. There is no reason for this principle to be excluded in the case of privatized aeronautics services, and it is not surprising that NAV Canada has been permitted to incorporate interest on unpaid charges into its charging scheme.

**95** The question then turns to how long the interest can run. The airport authorities and NAV Canada have possession of the aircraft until the charge or amount in respect of which the seizure was made is paid. It seems to me that this debt must be understood in real terms and must include the time value of money.

**96** Given the authority to charge interest, my view is that interest continues to run to the first of the [page916] date of payment, the posting of security or bankruptcy. If interest were to stop accruing before payment has been made, then the airport authorities and NAV Canada would not recover the full amount owed to them in real terms. Once the owner, operator or titleholder has provided security, the interest stops accruing. The legal titleholder is then incurring the cost of the security and losing the time value of money. It should not have to pay twice. While a *CCAA* filing does not stop the accrual of interest, the unpaid charges remain an unsecured claim provable against the bankrupt airline. The claim does not accrue interest after the bankruptcy: ss. 121 and 122 of the *Bankruptcy and Insolvency Act*.

**97** A particular issue is raised in the Quebec appeals regarding proper notice of the interest charges. This is an issue to be dealt with by the motions judge when these matters are returned for further consideration and disposition.

V. Disposition *

* The amendments to para.98, issued on August 16, 2006, are included in these reasons.

**98** For these reasons, I would allow the appeals and cross-appeals in part, as follows:

1. I would dismiss the appeals of NAV Canada seeking to hold the respondents liable in their personal/corporate capacity;
2. I would allow the appeals of NAV Canada and the airport authorities of the dismissal of their seizure and detention applications and remit those applications to the respective motions judges to be dealt with in accordance with these reasons;
3. I would set aside the orders requiring NAV Canada and the airport authorities to reimburse [page917] the respondents for the aircraft detention costs;
4. I would allow the appeals of NAV Canada and the GTAA of the ruling that the engine lessors are entitled to repossess the leased engines;
5. Interest on overdue charges continues to run to the first of the date of payment, the posting of security or bankruptcy.

In other respects, the appeals and cross-appeals will be dismissed. Aéroports de Montréal, St. John's International Airport Authority Inc. and Charlottetown Airport Authority Inc. are entitled to their costs in the Quebec appeals. All other parties shall bear their own costs.

*Appeals and cross-appeals allowed in part.*

**Solicitors:**

Solicitors for NAV Canada (30214): Gowling Lafleur Henderson, Toronto.

Solicitors for Greater Toronto Airports Authority (30214): Osler Hoskin & Harcourt, Toronto.

Solicitors for Winnipeg Airports Authority Inc., Halifax International Airport Authority, Edmonton Regional Airports Authority, Calgary Airport Authority, Aéroports de Montréal, Ottawa Macdonald-Cartier International Airport Authority, Vancouver International Airport Authority and St. John's International Airport Authority (30214): Ogilvy Renault, Toronto.

Solicitors for International Lease Finance Corporation, Hyr Här I Sverige Kommanditbolag, IAI X, Inc., Triton Aviation International LLC, Sierra Leasing Limited, ACG Acquisition XXV LLC, ILFC International Lease Finance Canada Ltd. and U.S. Airways Inc. (30214): Torys, Toronto.

Solicitors for G.E. Capital Aviation Services Inc., as Agent and Manager for Polaris Holding [page918] Company and AFT Trust-Sub I, Pegasus Aviation Inc., and PALS I, Inc. (30214): Cassels Brock & Blackwell, Toronto.

Solicitors for Ansett Worldwide Aviation, U.S.A., and MSA V (30214): Fraser Milner Casgrain, Toronto.

Solicitors for RRPF Engine Leasing Limited (30214): Heenan Blaikie, Toronto.

Solicitors for Flight Logistics Inc. (30214): Morrison Brown Sosnovitch, Toronto.

Solicitors for C.I.T. Leasing Corporation and NBB-Royal Lease Partnership One (30214): Blake Cassels & Graydon, Toronto.

Solicitors for GATX/CL Air Leasing Cooperative Association (30214): Borden Ladner Gervais, Toronto.

Solicitors for NAV Canada (30729, 30730, 30731, 30732): Lapointe Rosenstein, Montréal.

Solicitors for Ottawa Macdonald-Cartier International Airport Authority, St-John's International Airport Authority and Charlottetown Airport Authority Inc. (30731, 30732, 30742, 30749, 30750, 30751): Ogilvy Renault, Montréal.

Solicitors for Aéroports de Montréal (30731, 30732, 30738, 30740, 30742): Langlois Kronström Desjardins, Montréal.

Solicitors for Greater Toronto Airports Authority (30731, 30732, 30742, 30743, 30745): Osler Hoskin & Harcourt, Montréal.

Solicitors for Wilmington Trust Company, Wilmington Trust Corporation, Renaissance Leasing Corporation, Heather Leasing Corporation, G.I.E. Avions de transport régional and ATR Marketing Inc. (30729, 30730, 30731, 30732, 30738, 30740, 30742, 30743, 30745, 30749, 30750): Brouillette Charpentier Fortin, Montréal.

Solicitors for Newcourt Credit Group (Alberta) Inc., Canada Life Assurance Company and CCG Trust Corporation (30740, 30742, 30745, 30750, [page919] 30751): Desjardins Ducharme Stein Monast, Montréal.

Solicitors for Canadian Imperial Bank of Commerce (30214): Blake Cassels & Graydon, Toronto.

Solicitors for Inter-Canadian (1991) Inc. and Ernst & Young Inc., in its capacity as trustee for the bankruptcy of Inter-Canadian (1991) Inc. (30730, 30731, 30732, 30738, 30740, 30742, 30743, 30745, 30749, 30750, 30751): Kugler Kandestin, Montréal.

Solicitors for Greater London International Airport Authority and Saint John Airport Inc. (30742): Ogilvy Renault, Montréal.

Solicitors for Canadian Regional Airlines Ltd. and Canadian Regional (1998) Ltd. (30742): Fraser Milner Casgrain, Montréal.

cp/e/qlplh

# Tab 33

Second Session
Thirty-ninth Parliament, 2007

SENATE OF CANADA

*Proceedings of the Standing Senate Committee on*

# Banking, Trade and Commerce

*Chair:*
The Honourable W. DAVID ANGUS

Wednesday, November 28, 2007 (in camera)
Thursday, November 29, 2007

**Issue No. 2**

**Consideration of a draft agenda (future business)**
**and**
**First meeting on:**

Bill C-12, An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005

APPEARING:
The Honourable Jean-Pierre Blackburn, P.C., M.P.,
Minister of Labour
Colin Carrie, M.P.,
Parliamentary Secretary to the Minister of Industry

WITNESSES:
(*See back cover*)

Deuxième session de la
trente-neuvième législature, 2007

SÉNAT DU CANADA

*Délibérations du Comité sénatorial permanent des*

# Banques et du commerce

*Président :*
L'honorable W. DAVID ANGUS

Le mercredi 28 novembre 2007 (à huis clos)
Le jeudi 29 novembre 2007

**Fascicule n° 2**

**Étude d'un projet d'ordre du jour (travaux futurs)**
**et**
**Première réunion concernant :**

Le projet de loi C-12, Loi modifiant la Loi sur la faillite et l'insolvabilité, la Loi sur les arrangements avec les créanciers des compagnies, la Loi sur le Programme de protection des salariés et le chapitre 47 des Lois du Canada (2005)

COMPARAISSENT :
L'honorable Jean-Pierre Blackburn, C.P., député,
ministre du Travail
Colin Carrie, député,
secrétaire parlementaire du ministre de l'Industrie

TÉMOINS :
(*Voir à l'endos*)

THE STANDING SENATE COMMITTEE ON BANKING, TRADE AND COMMERCE

The Honourable W. David Angus, *Chair*

The Honourable Yoine Goldstein, *Deputy Chair*

and

The Honourable Senators:

| | |
|---|---|
| Biron | * LeBreton, P.C. |
| Eyton | (or Comeau) |
| Fitzpatrick | Meighen |
| Harb | Moore |
| * Hervieux-Payette, P.C. | Peterson |
| (or Tardif) | Ringuette |
| | Tkachuk |

*Ex officio members

(Quorum 4)

*Changes in membership of the committee:*

Pursuant to rule 85(4), membership of the committee was amended as follows:

The name of the Honourable Senator Moore was added (*November 20, 2007*).

The name of the Honourable Senator Poy substituted for that of the Honourable Senator Cowan (*November 21, 2007*).

The name of the Honourable Senator Chaput substituted for that of the Honourable Senator Massicotte (*November 26, 2007*).

Substitution pending for the Honourable Senator Poy (*November 26, 2007*).

The name of the Honourable Senator Massicotte substituted for that of the Honourable Senator Chaput (*November 26, 2007*).

The name of the Honourable Senator Peterson substituted for that of the Honourable Senator Massicotte (*November 29, 2007*).

LE COMITÉ SÉNATORIAL PERMANENT DES BANQUES ET DU COMMERCE

*Président :* L'honorable W. David Angus

*Vice-président :* L'honorable Yoine Goldstein

et

Les honorables sénateurs :

| | |
|---|---|
| Biron | * LeBreton, C.P. |
| Eyton | (ou Comeau) |
| Fitzpatrick | Meighen |
| Harb | Moore |
| * Hervieux-Payette, C.P. | Peterson |
| (ou Tardif) | Ringuette |
| | Tkachuk |

*Membres d'office

(Quorum 4)

*Modifications de la composition du comité :*

Conformément à l'article 85(4) du Règlement, la liste des membres du comité est modifiée, ainsi qu'il suit :

Le nom de l'honorable sénateur Moore est ajouté (*le 20 novembre 2007*).

Le nom de l'honorable sénateur Poy est substitué à celui de l'honorable sénateur Cowan (*le 21 novembre 2007*).

Le nom de l'honorable sénateur Chaput est substitué à celui de l'honorable sénateur Massicotte (*le 26 novembre 2007*).

Remplacement à venir pour l'honorable sénateur Poy (*le 26 novembre 2007*).

Le nom de l'honorable sénateur Massicotte est substitué à celui de l'honorable sénateur Chaput (*le 26 novembre 2007*).

Le nom de l'honorable sénateur Peterson est substitué à celui de l'honorable sénateur Massicotte (*le 29 novembre 2007*).

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**ORDER OF REFERENCE**

Extract from the *Journals of the Senate* of Thursday, November 15 2007:

Second reading Bill C-12, An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005.

The Honourable Senator Meighen moved, seconded by the Honourable Senator Eyton, that the bill be read the second time.

After debate,

The question being put on the motion, it was adopted.

The bill was then read the second time.

The Honourable Senator Meighen moved, seconded by the Honourable Senator Keon, that the bill be referred to the Standing Senate Committee on Banking, Trade and Commerce.

The question being put on the motion, it was adopted.

**ORDRE DE RENVOI**

Extrait des *Journaux du Sénat* du jeudi 15 novembre 2007 :

Deuxième lecture du projet de loi C-12, Loi modifiant la Loi sur la faillite et l'insolvabilité, la Loi sur les arrangements avec les créanciers des compagnies, la Loi sur le Programme de protection des salariés et le chapitre 47 des Lois du Canada (2005).

L'honorable sénateur Meighen propose, appuyé par l'honorable sénateur Eyton, que le projet de loi soit lu pour la deuxième fois.

Après débat,

La motion, mise aux voix, est adoptée.

Le projet de loi est alors lu pour la deuxième fois.

L'honorable sénateur Meighen propose, appuyé par l'honorable sénateur Keon, que le projet de loi soit renvoyé au Comité sénatorial permanent des banques et du commerce.

La motion, mise aux voix, est adoptée.

*Le greffier du Sénat,*

Paul C. Bélisle

*Clerk of the Senate*

If there are other flaws after one or two years of implementation, a report will be submitted to the minister responsible indicating that the bill was well intentioned but it contains a flaw.

Then the minister responsible will make the necessary change to a given provision. We cannot review everything because the process will never be finished, but we want to see if our objective is right and if the legislation to be amended meets that objective. If so, we need to move forward. Moreover, the bill was giving unanimous support in the House of Commons. I was not there at the time, before the current government was in office, but everyone said that employees' wages had to be protected.

That is why we are back here today with the unanimous support of Parliament.

[*English*]

**The Chair:** Mr. Carrie, do you want to make a preliminary comment?

**Mr. Carrie:** When looking at this, we do have to balance the competing interests. The wage earner protection part of it is very important in that balance. As Minister Blackburn said, we looked at all kinds of different ways of approaching this and in the spirit of balance; it does have to be moved forward together.

**Mr. Carrie:** Thank you very much. I want to begin by congratulating you on your chairmanship of this very important committee. As you said in your opening statement, you are a Conservative senator from Quebec. I believe it has been over 30 years since the last Conservative had the chair. Is that correct?

**The Chair:** Not quite, but it is certainly close to 20 years. Thank you for your thoughts.

**Mr. Carrie:** I would like to thank you for this opportunity to address the committee about Bill C-12, an act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, and the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005.

I would like to begin by thanking Minister Blackburn for joining me here today and for his comments in respect of the Wage Earner Protection Program Act. Mr. Chair, I intend to focus my comments on the insolvency law portions of this bill.

Canada's insolvency laws are an important part of our framework legislation and play a key role in our competitiveness and economic performance in this era of increased globalization. With modern effective framework legislation, the Canadian economy will be stronger and Canadian entrepreneurs will be better placed to compete domestically and globally.

Former Bill C-55, now known as chapter 47 of the Statutes of Canada, 2005, or chapter 47, introduced broad reforms intended to modernize Canada's insolvency regime. The objectives of chapter 47 were to facilitate the restructuring of viable but financially troubled companies, to improve the

Si, dans un ou deux ans, à l'application, il y a des choses qui sont incorrectes, un rapport sera fait au ministre responsable disant que, avec cette loi, on avait une bonne volonté, mais qu'il y a telle lacune.

À ce moment-là, le ministre responsable apportera le correctif nécessaire sur un point. On ne veut pas revoir l'ensemble parce qu'on ne s'en sortira pas, mais on veut voir si notre objectif est bon et si, effectivement, les lois qu'on doit modifier tiennent compte de notre orientation. Si oui, il faut maintenant aller de l'avant. De plus, cela a été unanime à la Chambre des communes. Je n'y étais pas à ce moment, avant le gouvernement actuel, mais tout le monde a dit : oui, il faut protéger le salaire des employés.

C'est dans ce contexte que nous revenons aujourd'hui devant vous avec la volonté unanime du Parlement.

[*Traduction*]

**Le président :** Monsieur Carrie, avez-vous une déclaration préliminaire à faire?

**M. Carrie :** Dans cette mesure législative, il faut trouver un juste milieu entre les intérêts concurrents. La partie sur la protection des salariés est un élément très important de cet équilibre. Comme le ministre Blackburn l'a dit, nous avons envisagé toutes sortes d'approches, pour trouver cet équilibre; le projet de loi doit être adopté dans son ensemble.

**M. Carrie :** Merci beaucoup. Tout d'abord, permettez-moi de vous féliciter de présider ce très important comité. Comme vous l'avez dit au début de la réunion, vous êtes un sénateur conservateur du Québec. Voilà bien plus de 30 ans, n'est-ce pas, qu'un sénateur conservateur n'a pas occupé ce fauteuil?

**Le président :** Pas tout à fait, mais certainement près de 20 ans. Je vous remercie.

**M. Carrie :** Merci de m'avoir invité à venir parler devant le comité du projet de loi C-12, Loi modifiant la Loi sur la faillite et l'insolvabilité, la Loi sur les arrangements avec les créanciers des compagnies, la Loi sur le programme de protection des salariés et le chapitre 47 des Lois du Canada (2005).

J'aimerais tout d'abord remercier le ministre Blackburn de sa présence avec moi aujourd'hui et de ses commentaires concernant la Loi sur le Programme de protection des salariés. Monsieur le président, j'ai l'intention d'axer mes observations sur les portions du projet de loi relatives à la législation en matière d'insolvabilité.

En cette ère de mondialisation accrue, les lois canadiennes en matière d'insolvabilité forment une partie importante de notre cadre législatif et jouent un rôle clé dans notre compétitivité et notre rendement économiques. Un cadre législatif moderne et efficace permettra à l'économie canadienne d'être plus solide et aux entrepreneurs canadiens d'être plus concurrentiels à l'échelle nationale et internationale.

L'ancien projet de loi C-55, maintenant connu sous le nom de chapitre 47 des Lois du Canada (2005) ou de chapitre 47, introduisait de vastes réformes visant à moderniser le système d'insolvabilité au Canada. Les objectifs du chapitre 47 étaient de faciliter les restructurations d'entreprises viables mais éprouvant

protection of wage earners, to make the insolvency system fairer and reduce abuse, and to improve the administration of the entire system.

In meeting these objectives, chapter 47 created an appropriate balance between the competing interests of debtors and creditors and, as well, between different creditors. This is extremely important because it is crucial that our insolvency regime be designed to function efficiently and provide incentives to discourage abuse.

As you are aware, however, chapter 47 received expedited passage through Parliament. As a result, it contains a number of important technical flaws that prevent the government from bringing the law into force. Bill C-12, which is before you today, will correct those technical flaws.

Bill C-12 is the product of extensive consultations with a panel of leading insolvency law experts, both practitioners and academics. The panel assisted department officials in identifying the flaws and in determining workable solutions. In addition, department officials received input from a wide variety of stakeholder groups, including, for example, the Canadian Bar Association, the Canadian Life and Health Insurance Association and family law advocates.

In my comments, I have referred to chapter 47's technical flaws. That is deliberate. As Minister Blackburn has said, Bill C-12 can be considered as a piece of housekeeping legislation. It is not intended to re-examine the policy elements of chapter 47.

We have heard that insolvency reform is needed as soon as possible. Bill C-12 will achieve that goal. As I have said, chapter 47 found an appropriate balance to the competing interests inherent in insolvency policy. Where chapter 47 can be improved is in the details. It is for that reason that Bill C-12 takes the technical route — to fix the details, not to start over.

With that objective in mind, I would like to discuss some of those details that Bill C-12 will fix. I will focus on five examples: interim financing, trustee's personal liability, national receivers, equity claims and transfers at undervalue.

With respect to interim financing, chapter 47 codified the process by which companies in financial trouble obtain financing in order to give them breathing room while they restructure. Bill C-12 addresses two flaws contained in chapter 47.

First, Bill C-12 will require that secured parties be informed of any application for interim financing that may affect their interests. It is a matter of fairness that they should be entitled to defend their interests.

des difficultés financières, d'améliorer la protection des salariés, de rendre le système d'insolvabilité plus équitable et de réduire les abus et d'améliorer l'administration du système.

Pour atteindre ces objectifs, le chapitre 47 a créé un équilibre approprié entre les intérêts concurrents des débiteurs et des créanciers ainsi qu'entre les différents créanciers. Cela est extrêmement important parce qu'il est crucial que notre régime d'insolvabilité soit conçu de façon à permettre un fonctionnement efficace et à décourager les abus.

Comme vous le savez, le chapitre 47 a été adopté de façon accélérée par le Parlement. Aussi contient-il un certain nombre de défauts techniques qui empêchent le gouvernement de le mettre en vigueur. Le projet de loi C-12, qui est devant vous aujourd'hui, corrigera ces défauts techniques.

Le projet de loi C-12 résulte de longues consultations auprès d'un groupe d'éminents spécialistes en droit de l'insolvabilité, formé tant de praticiens que d'universitaires. Le groupe a aidé les fonctionnaires du ministère à cerner les défauts techniques et à mettre au point des solutions pratiques. En outre, les fonctionnaires du ministère ont obtenu des renseignements d'un grand éventail de groupes d'intervenants, dont l'Association du Barreau canadien, l'Association canadienne des compagnies d'assurances de personnes et des avocats spécialisés en droit de la famille.

Dans mes observations, j'ai fait référence aux défauts techniques du chapitre 47 de façon délibérée. Comme l'a déclaré le ministre Blackburn, le projet de loi C-12 peut être considéré comme un projet de loi d'ordre administratif. Il ne vise pas à réexaminer les éléments de politique du chapitre 47.

Nous avons compris qu'il fallait apporter des réformes au système d'insolvabilité le plus tôt possible. Le projet de loi C-12 permettra de réaliser cet objectif. Comme je l'ai mentionné, le chapitre 47 a trouvé le juste équilibre entre les intérêts concurrents inhérents à la politique en matière d'insolvabilité. C'est au niveau des détails que le chapitre 47 peut être amélioré. Le projet de loi C-12 emprunte donc la voie technique, à savoir celle de régler les détails et non de recommencer le travail.

Tout en gardant cet objectif à l'esprit, j'aimerais examiner brièvement certains détails que corrigera le projet de loi C-12. Je vais vous en donner cinq exemples : le financement provisoire, la responsabilité personnelle du syndic, les séquestres nationaux, les réclamations relatives aux capitaux propres, ainsi que les opérations sous-évaluées.

En ce qui a trait au financement provisoire, le chapitre 47 a codifié le processus permettant aux sociétés éprouvant des difficultés financières d'obtenir le financement qu'il leur assurera une marge de manœuvre pendant leur restructuration. Le projet de loi C-12 comble deux défauts du chapitre 47.

Premièrement, le projet de loi C-12 exige que les créanciers garantis soient informés de toute demande de financement provisoire pouvant avoir un effet sur leurs intérêts. Ils doivent avoir le droit de défendre leurs intérêts; c'est une question d'équité.

Second, it will also make it clear that the special status accorded to interim financing loans will only apply to money lent to help the company during the period of distress. Again, as a matter of fairness, debts that existed before an insolvency filing will not be entitled to jump ahead of other creditors.

With respect to trustee's personal liability, chapter 47 also attempted to address the problem where a trustee or a receiver is made personally liable for the obligations of the debtor. Trustees and receivers are insolvency practitioners whose role is to go in after an insolvency filing, take over the assets of the bankrupt company and, in some cases, run the business until a purchaser can be found. This is a going-concern sale. It is recognized that going-concern sales are more beneficial than closing the business. Evidence shows that creditors receive better recovery and that more jobs are saved.

Recent case law, however, has made it possible for the insolvency practitioner to be found personally responsible to pay existing debts of the company in these circumstances. This is not good for the insolvency system, and it is not fair to the trustee or the receiver.

The reform in chapter 47, however, did not do enough to prevent these obligations from being passed on to the trustee or receiver. The result is that trustees and receivers may not wish to take on files where this risk is present. This may leave creditors with smaller recoveries and employees out in the cold.

Bill C-12 makes it clear that a trustee or a receiver should not be personally responsible for existing obligations. To ensure that workers are not left without recourse, however, Bill C-12 also makes it clear that their claims continue against the new purchaser.

With respect to national receivers, chapter 47 created the concept of a national receiver appointed under the Bankruptcy and Insolvency Act. The goal was to improve efficiency in the insolvency system by allowing one person to deal with all of the debtor's property, wherever the property is located in Canada.

The provision in chapter 47 was not sufficient, however, because it did not provide a specific list of powers that the national receiver could rely upon. This may lead to differing rules, depending on where the receiver is appointed.

Bill C-12 provides a list of powers to provide guidance to the appointing court. In addition, it offers flexibility for the court to grant such other powers as the court thinks are appropriate on a case-by-case basis.

With respect to equity claims, chapter 47 introduced a reform to limit the rights of equity holders to receive payments under a restructuring plan. In bankruptcy, of course, an equity holder has

Deuxièmement, il permettra également de préciser que le statut particulier qui est accordé aux prêts consentis aux fins de financement provisoire ne s'appliquera qu'aux sommes prêtées pour aider l'entreprise pendant la période où elle est en difficulté. Encore une fois, par souci d'équité, les dettes qui existaient avant la proposition d'insolvabilité n'auront pas préséance sur celles des autres créanciers.

En ce qui concerne la responsabilité personnelle du syndic, le chapitre 47 a également tenté de résoudre le problème lorsque le syndic ou le séquestre est tenu personnellement responsable des obligations d'un débiteur. Les syndics et les séquestres sont des praticiens de l'insolvabilité qui entrent en scène après le dépôt d'une procédure d'insolvabilité, prennent le contrôle des actifs de la société en faillite et qui, dans certains cas, dirigent l'entreprise jusqu'à ce que l'on trouve un acquéreur. Cela s'appelle une vente d'entreprise en exploitation. Il est reconnu qu'il est plus rentable de vendre une entreprise en exploitation que de procéder à sa fermeture. Les faits montrent que les créanciers obtiennent un meilleur rétablissement et que plus d'emplois sont sauvegardés.

Un jugement récent a toutefois permis de tenir un professionnel de l'insolvabilité personnellement responsable du paiement des dettes courantes de la compagnie dans certaines circonstances. Cette approche n'est guère appropriée pour le régime d'insolvabilité et est injuste à l'égard du syndic ou du séquestre.

L'amendement du chapitre 47 n'a toutefois pas suffi à éviter que ces obligations soient transmises au syndic ou au séquestre. Par conséquent, il peut arriver que les syndics et les séquestres refusent des affaires au motif qu'elles présentent un risque — ce qui se traduit pour les créanciers par une réduction des montants recouvrés et, pour les travailleurs, par des pertes d'emplois.

Le projet de loi C-12 établit clairement qu'un syndic ou un séquestre ne peut être tenu personnellement responsable d'obligations existantes. Pour éviter que les travailleurs se retrouvent sans recours, le projet de loi C-12 établit clairement que les réclamations de ceux-ci seront maintenues auprès du nouvel acheteur.

En ce qui concerne les séquestres nationaux, le chapitre 47 a introduit le concept de séquestre national nommé en vertu de la Loi sur la faillite et l'insolvabilité. Cet ajout avait pour objectif d'accroître l'efficacité du régime d'insolvabilité en permettant à une seule personne de traiter tous les biens du failli, où que ceux-ci soient situés au Canada.

Les dispositions du chapitre 47 n'étaient toutefois pas suffisantes parce qu'elles n'établissaient pas clairement les pouvoirs sur lesquels pouvait se fonder le séquestre national. Cette lacune pouvait être source de règles divergentes selon le lieu de nomination du séquestre.

Le projet de loi C-12 donne une liste de pouvoirs qui guidera le tribunal chargé de la nomination. En outre, il donne suffisamment de latitude au tribunal, permettant à ce dernier d'octroyer les pouvoirs qu'il jugera nécessaires, selon le cas.

En ce qui concerne les réclamations relatives à des capitaux propres, le chapitre 47 introduisait une modification visant à restreindre la possibilité, pour les actionnaires, de recevoir des

no right to be paid for their shares until all claims against the company are paid. In a restructuring, because it is a matter of negotiation, the rights of equity holders are not clear. It is possible for equity holders to get paid when other creditors are not. This is a problem as equity holders should not have greater rights in a restructuring than they would in a bankruptcy. Bill C-12 will correct this.

First, a definition of "equity claim" has been introduced. This clarifies that equity claims include items like dividend payments, return of capital, a right to have the company buy back your shares, a loss on the value of your shares and the right to be indemnified by the company for losses on the value of those shares. Second, an explicit amendment is included to prevent, during the restructuring, an equity claim receiving a payment unless all other claims are paid in full first. Third, the right of shareholders to vote on changes to the corporate structure is removed. Instead, that power has been given to the court. The Bill C-12 amendments will complete the reform started by chapter 47 by providing more clarity and explicit rules.

Chapter 47 also made amendments to the anti-abuse mechanism in the BIA related to efforts by unscrupulous debtors who try to shield their assets. Bill C-12 clarifies how the provisions will apply, and by doing so, makes them more efficient tools against potential abuse. At the same time, an amendment is made to the definition of "arm's length parties" to ensure that these provisions do not inadvertently capture legitimate family law agreements.

In conclusion, Mr. Chair, I have spent my time today explaining how Bill C-12 will improve on chapter 47. I have done so because Bill C-12 represents the best opportunity to bring chapter 47 into force quickly.

While there may be some stakeholders who want to reopen the debate on how chapter 47 balanced the many competing interests, doing so will only bring further delay when insolvency practitioners are telling us that insolvency reform is needed right now.

As members of this committee are aware, chapter 47 contains a five-year legislative review clause that will provide an opportunity to re-examine these and other policy debates.

Mr. Chair, on behalf of Minister Prentice, let me thank the committee for giving the opportunity to speak to this important piece of legislation today. I am pleased to respond to your questions.

paiements dans le cadre d'un plan de restructuration. Bien entendu, en cas de faillite, un actionnaire ne peut recevoir un paiement en échange de ses actions tant que toutes les réclamations visant la compagnie ne sont pas réglées. Dans le cas d'une restructuration, parce qu'il s'agit d'une affaire négociée, les droits des actionnaires ne sont pas clairs. Il est possible pour les actionnaires de recevoir un paiement, contrairement à d'autres créanciers. C'est un problème, car les actionnaires ne devraient pas avoir plus de droits lors d'une renégociation que lors d'une faillite. Le projet de loi C-12 va y remédier.

Premièrement, le projet définit la notion de réclamations relatives à des capitaux propres. Il précise que les réclamations relatives à des capitaux propres comprennent notamment les dividendes, les remboursements de capital, le droit de rachat d'actions au gré de l'actionnaire, les pertes attribuables à la diminution de la valeur des actions et le droit de recevoir une indemnité de la compagnie relativement à une diminution de la valeur des actions. Deuxièmement, le projet de loi apporte des amendements explicites pour veiller à ce que, dans le cadre d'une restructuration, le paiement d'une réclamation relative à des capitaux propres puisse avoir lieu seulement si le paiement intégral de toutes les autres réclamations a été effectué. Troisièmement, les actionnaires n'ont plus droit de vote sur la modification de la structure organisationnelle; ce droit est plutôt accordé au tribunal. Les modifications prévues par le projet de loi C-12 boucleront la vague de modifications lancée par le chapitre 47 en apportant plus de clarté, ainsi que des règles précises.

Pour empêcher les créanciers sans scrupule de tenter de camoufler leurs actifs, le chapitre 47 modifiait également les mécanismes établis dans la LFI en vue d'éviter les abus. Le projet de loi C-12 précise comment les dispositions s'appliqueront et, ce faisant, font de ces dispositions de meilleures armes contre d'éventuels abus. Parallèlement, la définition de l'expression « sans lien de dépendance » est clarifiée pour éviter que ces dispositions n'englobent malencontreusement les ententes légitimes en droit familial.

En conclusion, monsieur le président, j'ai expliqué aujourd'hui en quoi le projet de loi C-12 améliorera le chapitre 47. Ce projet de loi est la voie à suivre pour mettre rapidement en vigueur le chapitre 47.

Certains souhaitent rouvrir le débat sur la mesure dans laquelle le chapitre 47 constituait un juste équilibre entre de nombreux intérêts concurrents, mais cela ne ferait que repousser davantage une réforme que réclament les professionnels de l'insolvabilité.

Comme le savent les membres du comité, le chapitre 47 prévoit un examen de la loi cinq ans après son entrée en vigueur, ce qui donnera l'occasion de se pencher de nouveau sur ces dispositions, entre autres sujets de débat.

Monsieur le président, au nom du ministre Prentice, je remercie le comité de m'avoir donné l'occasion de parler aujourd'hui de cet important projet de loi. Je serai heureux de répondre à vos questions.

**IN THE MATTER OF THE *COMPANIES CREDITORS' ARRANGEMENT ACT*, R.S.C. 1985, c. C-36, AS AMENDED AND IN THE MATTER OF A PLAN OR COMPROMISE OR ARRANGEMENT OF SINO-FOREST CORPORATION**

Court of Appeal File Numbers: C56118 / C56115 / C56125
Superior Court File No. CV-12-9667-00CL

**COURT OF APPEAL FOR ONTARIO**

# BRIEF OF AUTHORITIES OF THE RESPONDENT, SINO-FOREST CORPORATION


**BENNETT JONES LLP**
One First Canadian Place
Suite 3400, P.O. Box 130
Toronto, Ontario
M5X 1A4

**Robert W. Staley** (LSUC #27115J)
**Kevin Zych** (LSUC #33129T)
**Derek J. Bell** (LSUC #43420J)
**Raj Sahni** (LSUC #42942U)
**Jonathan Bell** (LSUC #55457P)

Tel: 416-777-4857
Fax: 416-863-1716

Lawyers for Sino-Forest Corporation