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

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, C. c-36, AS AMENDED, AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SINO-FOREST CORPORATION

Court File No. CV-11-431153-00CP

ONTARIO
SUPERIOR COURT OF JUSTICE

B E T W E E N :

THE TRUSTEES OF THE LABOURERS' PENSION FUND OF CENTRAL AND EASTERN CANADA, THE TRUSTEES OF THE INTERNATIONAL UNION OF OPERATING ENGINEERS LOCAL 793 PENSION PLAN FOR OPERATING ENGINEERS IN ONTARIO, SJUNDE AP-FONDEN, DAVID GRANT and ROBERT WONG

Plaintiffs

- and-

SINO-FOREST CORPORATION, ERNST & YOUNG LLP, BDO LIMITED (formerly known as BDO MCCABE LO LIMITED), ALLEN T.Y. CHAN, W. JUDSON MARTIN, KAI KIT POON, DAVID J. HORSLEY, WILLIAM E. ARDELL, JAMES P. BOWLAND, JAMES M.E. HYDE, EDMUND MAK, SIMON MURRAY, PETER WANG, GARRY J. WEST, POYRY (BEIJING) CONSULTING COMPANY LIMITED, CREDIT SUISSE SECURITIES (CANADA), INC., TD SECURITIES INC., DUNDEE SECURITIES CORPORATION, RBC DOMINION SECURITIES INC., SCOTIA CAPITAL INC., CIBC WORLD MARKETS INC., MERRILL LYNCH CANADA INC., CANACCORD FINANCIAL LTD., MAISON PLACEMENTS CANADA INC., CREDIT SUISSE SECURITIES (USA) LLC and MERRILL LYNCH, PIERCE, FENNER & SMITH INCORPORATED (successor by merger to Bank of America Securities LLC)

Defendants

Proceedings under the *Class Proceedings Act, 1992*

BOOK OF AUTHORITIES OF THE APPLICANT, CHUBB INSURANCE COMPANY OF CANADA

(Motion Returnable April 20, 2015)

DATE: April 16, 2015

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INDEX

TAB 1

Case Name:

Laidlaw 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 the Canada Business Corporations Act, R.S.C. 1985, c. C-44, as amended
AND IN THE MATTER OF the Business Corporations Act (Ontario), R.S.O. 1990, c. B.16, as amended
Re: Laidlaw Inc. and Laidlaw Investments Ltd.

[2003] O.J. No. 1135

[2003] O.T.C. 228

46 C.C.L.I. (3d) 263

122 A.C.W.S. (3d) 244

Court File No. 01-CL-4178

Ontario Superior Court of Justice
Commercial List

Farley J.

Heard: December 6, 2002.
Judgment: March 11, 2003.

(19 paras.)

Insurance law -- The insurance contract -- Formation of the contract -- Place contract made -- Payment of insurance proceeds.

Application by the insurer for a declaration that certain insurance policies issued to the respondent Laidlaw Inc. were made in Ontario and were subject to Ontario law, a declaration that the insurer was entitled to pay defence costs, settlements and judgments on behalf of insured parties under the policies in the chronological order in which they were executed, a declaration that the payment by the insurer of those amounts constituted full and complete satisfaction of its obligations under the polices, and a declaration that all insured parties were bound by the previous declarations. The policies were issued and delivered to Laidlaw in Ontario. The respondent Safety-Kleen and its outside directors opposed the declarations that the policies were subject to Ontario law and that all insured parties were bound by the other declarations.

HELD: Application allowed. Pursuant to Ontario law, the policies were contracts deemed to have been made in Ontario, and were therefore to be construed according to Ontario law. No determination was

made as to whether Safety-Kleen or its outside directors were included as insured parties under the policies. The first come, first served principle was appropriate and in the interests of overall fairness.

Statutes, Regulations and Rules Cited:

Courts of Justice Act, R.S.O. 1990, c. C.43, s. 97. Insurance Act, R.S.O. 1990, c. I.8, ss. 122, 123. Interpretation Act, R.S.O. 1990, c. I.11, s. 29(1).

Counsel:

Mary Margaret Fox and Keith Batten, for American Home Assurance Company, moving party.
Brian Empey, for Laidlaw Inc.
R.G. Slaght, Q.C. and Eleni Maroudas, for Safety-Kleen Outside Directors.
Adam Chamberlain, for Safety-Kleen Corp.
Kevin Zych, for Bondholders' Subcommittee.
W.E. Pepall, for PWC (Canada).
David Byers, for Bank Subcommittee.

---

1 **FARLEY J.**:-- American Home Assurance Company ("Homeco") moved for relief as per its Notice of Motion dated October 16, 2002 as follows:

1. a declaration that certain policies of Directors, Officers and Corporate Liability insurance issued by American Home to Laidlaw Inc. ("LINC") and Subsidiaries of LINC, as listed in Schedule "A" hereto (collectively "the Policies"), are deemed to have been made in the Province of Ontario, Canada and are subject to the laws of Ontario, Canada;
2. a declaration that American Home is entitled to pay defence costs, settlements and judgments on behalf of Insureds under the Polices ("Defence Costs", "settlement amounts" and "judgement amounts", respectively), in the chronological order in which such Defence Costs, settlements and judgments are incurred, agreed to or obtained, without increasing American Home's obligations to make payments under any of the Policies beyond the limits of liability specified in such Policies;
3. a declaration that payment by American Home of any Defence Costs, settlement amounts or judgment amounts paid in accordance with the declaration sought in paragraph 2, above, shall constitute, to the extent of such payment, full and complete satisfaction of American Home's obligations under the Policies, and shall serve to reduce the limits of the applicable Policy(ies) accordingly;
4. a declaration that all Insureds under the Policies listed in Schedule "A" hereto who are served with the Motion Record herein, all parties identified in Schedule "B" hereto who have commenced Claims against Insureds under the Policies, and any party identified in Schedule "C" hereto who may in the future institute a Claim or action against any Insured under the Policies, seeking relief which would have been, but for the exhaustion of the limits of the Policies, potentially recoverable under the Policies, shall be bound by the declarations sought in paragraphs 1-3 above, as such may be made by this Court; and
5. such further and other relief as counsel may advise and this Honourable Court permit.

2 As indicated at paragraphs 28-29 of the affidavit of Anthony Tatulli on behalf of Homeco:

> The Laidlaw Bondholders Settlement
>
> 28. Commencing in approximately mid-2001, attorneys representing the parties to Action No. 1 as identified in Schedule "B" to the Notice of Motion, commenced negotiations with respect to possible settlement of that Action. Those negotiations continued over several months, culminating in the settlement of that Action (the "Laidlaw Bondholders' Settlement") evidenced by a preliminary agreement dated January 7, 2002 and the Stipulation of Settlement dated July 25, 2002. A true copy of the Stipulation of Settlement, without Exhibits, is attached hereto as Exhibit "N". American Home has agreed to contribute to the Laidlaw Bondholders' Settlement on behalf of its Insureds, subject to various conditions to that settlement being satisfied, one of which is found in Section 11(j) of the Stipulation of Settlement. Section 11(j) requires, as a condition of the Laidlaw Bondholders' Settlement, "... the entry by an Ontario Court of competent jurisdiction, of a final, non-appealable order in a form acceptable to American Home approving the right of American Home under Ontario law to pay defense costs, settlements and judgments in the chronological order in which such defense costs, settlements and judgments are incurred, agreed to or obtained without increasing American Home's obligations to make payments under any directors' and officers' liability policies issued by American Home or any of its affiliates beyond the limits of liability specified in such policies".
>
> 29. American Home has served the following persons and entities with the motion materials:
>
> (a) LINC and Subsidiaries against which any actions or proceedings have been commenced;
>
> (b) all persons who are Natural Person Insureds of LINC commencing with LINC's fiscal year ending August 31, 1997 and continuing to the present, all Natural Person Insureds of Laidlaw Environmental Services, Inc. for the fiscal year ending August 31, 1997 and continuing to May 15, 1998, and all Natural Person Insureds of those LINC Subsidiaries named as defendants in any of the Actions; this includes all Natural Person Insureds named as defendants, defendants by Counterclaim, or Third-Parties in all of the Actions and proceedings identified in Schedule "B" to the Notice of Motion;
>
> (c) the plaintiffs or, in some cases, defendants who have Counterclaimed or instituted Third-Party Claims against Insureds, in the Actions listed in Schedule "B" to the Notice of Motion; and
>
> (d) the persons and entities identified in Schedule "C" to the Notice of Motion.
>
> Where a party is or was an Insured in more than one capacity, American Home has only served that person once. Where to American Home's knowledge a party is represented by counsel, that counsel has been served, instead of the party. In the case of certain former directors of Laidlaw Environmental Services, Inc., the only address American Home was able to find was that of Laidlaw Environmental Services, Inc. Those former directors/officers will be served: c/o General Counsel, Safety-Kleen, with a request that the material be forwarded to the former directors/officers or returned.

3 The declarations sought in the Notice of Motion were opposed by only two parties: Safety-Kleen Corp. ("SK") and the SK Outside Directors - but only in respect of the declarations sought in paragraphs

1 and 4 of the Notice of Motion as to the law applicable to the Policies and the parties to be bound by the declarations requested. It was also suggested that there was some concern about Homeco being relieved of its obligation to act in good faith and in accordance with the terms and conditions of the subject Policies. With respect to this concern I see nothing in the material before me which would relieve Homeco of such obligation; I think that this is a red herring. In my view nothing in this motion relieves Homeco of such obligation which remains intact and extant.

4 The Insurance Act, R.S.O. 1990, c. I.8 provides in ss. 122-123 as follows:

> s. 122 Except where otherwise provided and where not inconsistent with other provisions of this Act, this Part applies to every contract of insurance made in Ontario, other than contracts of,
>
> (a) accident and sickness insurance;
>
> (b) life insurance; and
> (c) marine insurance.
>
> s. 123 Where the subject-matter of a contract of insurance is property in Ontario or an insurable interest of a person resident in Ontario, the contract of insurance, if signed, countersigned, issued or delivered in Ontario or committed to the post office or to any carrier, messenger or agent to be delivered or handed over to the insured, or the insured's assign or agent in Ontario shall be deemed to evidence a contract made therein, and the contract shall be construed according to the law thereof, and all moneys payable under the contract shall be paid at the office of the chief officer or agent in Ontario of the insurer in lawful money of Canada.

5 The subject Policies were all issued in Ontario and delivered to Laidlaw Inc. ("LINC") (the named insured, a corporation incorporated under the laws of Canada with its head office located in Burlington, Ontario) via LINC's insurance broker and agent Robert Purves Ltd. in Toronto, Ontario. Thus it appears to me that pursuant to Ontario law, the subject Policies would be contracts deemed to have been made in Ontario and, as such, to be construed according to the law of Ontario. See Hubert v. Compagnie Equitable d'Assurance Contre le Feu (1958), 12 D.L.R. (2d) 701 (Ont. H.C.); Cansulex Ltd. v. Reed Stenhouse Ltd. et al. (1986), 18 C.C.L.I. 24 (B.C.S.C.) at pp. 39-44; Jones v. Kansa General Insurance Co. (1992), 93 D.L.R. (4th) 481 (Ont. C.A.) at pp. 487-8. One should note that in Cansulex, the British Columbia equivalent provision to s. 123 merely stated "accordingly" as opposed to s. 123 specifying "according to the law thereof", as to which "thereof" must mean "Ontario" in my view. While the subject Policies do not stipulate that the Policies are subject to or governed by the law of Ontario, that is not necessary in light of the deeming provision of s. 123. Further the subject Policies do not appear to be excepted pursuant to s. 122. Of course the statutes and laws of other jurisdictions may similarly provide that because of some connection to that jurisdiction, the laws of that jurisdiction govern the subject Policies vis-à-vis someone who is within the reach of that jurisdiction (see, for example, South Carolina Code of Laws, Title 38, Chapter 61, Insurance Contracts General, Section 10).

6 As discussed in J.G. Castel and J. Walker, Canadian Conflict of Laws, 5th ed. looseleaf (Toronto: Butterworths, 2002) at pp. 31.38-39:

> b. Insurance Contracts
>
> The large volume of business done by foreign insurance companies in Canada has prompted the federal Parliament as well as the legislatures of the various provinces to regulate insurance contracts in order to prevent the status and rights of Canadian

resident policy holders, insureds and beneficiaries, from being determined by some foreign law which could be applicable under ordinary conflict of laws rules, and to make certain that the insurance moneys will be payable locally. For instance, in a number of provinces the Insurance Act provides that [then citing a number of provincial Acts including the subject Ontario one]:

> Where the subject matter of a contract of insurance is property in [the province] or an insurable interest of a person resident in [the province], the contract of insurance, if signed, countersigned, issued or delivered in [the province] or committed to the post office or to any carrier, messenger or agent to be delivered or handed over to the insured, his assign or agent in [the province] shall be deemed to evidence a contract made therein, and the contract shall be construed according to the law thereof, and all money payable under the contract shall be paid at the office of the chief officer or agent in [the province] of the insurer in lawful money of Canada.

This section seems to indicate that the law of the province is the proper law of a contract of insurance made or deemed to be made in that province and that in such a case the parties are not free to oust the application of that law by an express choice of law clause. This is necessary to protect policyholders in their dealings with foreign insurance companies that have superior bargaining power. (emphasis added)

The authors then go on to distinguish the situation prevailing under the insurance legislation in British Columbia and Alberta concluding at p. 31.39 that: "These provisions do not, however, necessarily make the law of the province the proper law of the contract of insurance."

7 The Courts of Justice Act, R.S.O. 1990, c. C.43 provides: s. 97 ... the Superior Court of Justice ... may make binding declarations of right, whether or not any consequential relief is or could be claimed.

8 It appears to me that the provisions of Clauses 8 and 18 of the Primary Policy of the subject Policies (with application to the other subject Policies) as set out below:

> 8. Defence Costs, Settlements, Judgments (Including the Advancement of Defence Costs)
>
> ...
>
> In the event of Loss arising from a Claim or Claims for which payment is due under the provisions of this policy, then the Insurer shall:
>
> (a) first, pay such non-Indemnifiable Loss for which coverage is provided under Coverage A of this policy; and
> (b) then, with respect to whatever remaining amount of the Limit of Liability is available after payment of such non-Indemnifiable Loss, at the written request of the chief executive officer of the Named Corporation, either pay or withhold payment of such other Loss for which coverage is provided under this policy.
>
> In the event the Insurer withholds the payment pursuant to sub-paragraph (b) above, then the Insurer shall at such time and in such manner as shall be set forth in written instructions of the chief executive officer of the Named

> Corporation, remit such payment to the Company or directly to or on behalf of a Natural Person Insured.
>
> 18. Action Against Insurer
>
> Except as provided in Clause 17 of the policy, no action shall lie against the Insurer unless, as a condition precedent thereto, there shall have been full compliance with all of the terms of this policy, nor until the amount of the Insureds' obligation to pay shall have been finally determined either by judgment against the Insureds after actual trial or by written agreement of the Insureds, the claimant and the Insurer.
>
> Any person or organization or the legal representative thereof who has secured such judgment or written agreement shall thereafter be entitled to recover under this policy to the extent of the insurance afforded by this policy. No person or organization shall have any rights under this policy to join the Insurer as a party to any action against the Insureds or the Company to determine the Insureds' liability, nor shall the Insurer be impleaded by the Insureds or the Company or their legal representatives. Bankruptcy or insolvency of the Company or the Insureds or of their estates shall not relieve the Insurer of any of its obligations hereunder.

apply vis-à-vis any of the insureds which are resident in Ontario (which would include LINC as a person as the definition of "person" in the Interpretation Act, R.S.O. 1990, c. I.11 at s. 29(1) includes a corporation) and any of the individual directors and officers of LINC and its included subsidiaries (as such may be determined in other litigation). See American Home Insurance Co. v. Drake International Inc., [2002] O.J. No. 333 (S.C.J.) where Chapnick, J., reviewed the aspect of s. 123 at paragraphs 23-8, although this was ostensibly a forum selection case and should therefore be viewed in that context. It should be kept in mind that in that case Drake Personnel was the Australian subsidiary of Drake International. While Drake International appears to have had a presence in Ontario, it does not seem that Drake Personnel had any such presence such as to establish residence in Ontario; this appears to be the basis for Chapnick, J.'s, conclusion at paragraph 28. For ease of reference, I set out her views at paragraphs 23-8 but would note the omission of certain words as indicated from her quote of s. 123 in paragraph 27:

> 23. The umbrella policy is silent as to jurisdiction with respect to the governing law and place of trial where coverage is disputed. Where a contract is silent as to jurisdiction, the proper law of the contract is determined according to which system of law has "the closest and most real connection" with the transaction having regard to factors such as the place of contracting, the place of performance, the place of business of the parties and the nature and subject matter of the contract. Castel, Canadian Conflict of Laws, 4th ed., pp. 593, 598-601. See also Serpa v. Confederation Life Association (1974), 2 O.R. (2d) 484.
> 24. In my view, while the umbrella policy was contracted with Drake International in Ontario, Ontario is not the system of law that has "the closest and most real connection" to its application. It is after all a worldwide policy intended to respond to claims made worldwide. Moreover, American Home, the insurer, has a place of business in Australia and the policy is being relied on in Australia by an Australian company, Drake Personnel.
> 25. It is well settled that in a case such as this, the overall consideration is that of forum conveniens. Mr. Snowden, on behalf of American Home, points out that an umbrella

policy is a hybrid policy, in effect, that combines aspects of both a primary and an excess policy; and an insurer is not obliged to defend claims which fall wholly outside the coverage provided by the policy. In that way, the exposure of an excess insurer is more remote.

26. American Home also argues that where a policy is negotiated, issued and financed or paid for and delivered in Ontario, the law of the province is deemed to apply to the contract. In that regard, American Home relies upon the Insurance Act, R.S.O. c. I.8, as amended, in particular s. 123 as well as the judgment of the Court of Appeal in Jones v. Kansa General Insurance Co. (1992), 10 O.R. (3d) 56 (C.A.).

27. Sections 123 and 124 of the Insurance Act read:

> 123. Contracts deemed made in Ontario - Where the subject-matter of a contract of insurance is property in Ontario or an insurable interest of a person resident in Ontario, the contract of insurance, if signed, countersigned, issued or delivered in Ontario or committed to the post office or to any carrier, messenger or agent to be delivered or handed over to the Insured, or the Insured's assign or agent in Ontario shall be deemed to evidence a contract made therein, [note: there is missing from this quote the following words: "and the contract shall be construed according to the law thereof and all monies payable under"] the contract shall be paid at the office of the chief officer or agent in Ontario of the insurer in lawful money of Canada.
>
> 124.(1) Terms, etc., of contracts invalid unless set out in full - All the terms and conditions of the contract of insurance shall be set out in full in the policy or by writing securely attached to it when issued, and, unless so set out, no term of contract or condition, stipulation, warranty or proviso modifying or impairing its effect is valid or admissible in evidence to the prejudice of the insured or beneficiary.

28. It is undisputed that the contract was "made" in Ontario. The conditions precedent for application of the constituent parts of s. 123 have, however, not been established within the context of these particular factual circumstances. Moreover, the alternative clause in s. 124 is for the benefit of the insured.

In passing I would think that if Drake International were determined to be resident of Ontario, then Ontario law would be employed to determine its claims, if any.

9 As I understand it the SK Outside Directors litigation is being tried in South Carolina. It will be up to the courts of that jurisdiction to determine coverage, if any, under the subject Policies. I certainly make no determination as to whether SK is included as an insured under the subject Policies, or similarly whether the SK Outside Directors are (or for that matter any SK directors).

10 Given that LINC is resident in Ontario, then in my view the law of Ontario applies to the subject Policies. The directors and officers of SK, if covered, as beneficiaries of the LINC subject Policies, are covered as a result of their connection with LINC. I do not understand that any of the relief sought is with respect to any Excess Policy, but rather just with respect to the Homeco subject Policies.

11 Notwithstanding my determination that Homeco is entitled to the declaration it is seeking in relief item 1, whether that declaration will be enforced in the sense of respected by the South Carolina Court in the SK Outside Directors Coverage Action ultimately will be a matter for the South Carolina Court to determine, by, I assume, the principles of private international law including the doctrine of comity. I

note in any event that the condition clause 11(j) of the Settlement Stipulation (supported by SK and the SK Outside Directors) provides that the Ontario Court in this hearing is being asked to give an order "approving the right of [Homeco] under Ontario law to pay defence costs, settlements and judgments in ... chronological order ..." (emphasis added). This Court can only make an order "under Ontario law" if it is found, as I have, that Ontario law applies to the subject Policies. I note that I was advised on February 28, 2003 that by Order signed December 17, 2002, the United States District Court, District of South Carolina, approved the Stipulation of Settlement (see paragraph 9 of that Order).

12 It was submitted by Homeco in argument that condition clause 11(j) which stated "in a form acceptable to [Homeco]" gave Homeco the right to determine whether it was satisfied with this Court's conclusion and that impliedly I should be mindful of that. Firstly, I think it obvious that Homeco fully appreciates that in a declaration involving the interpretation of Ontario law, this Court is constrained to give a decision which is in accord with Ontario law and it matters not that Homeco may or may not be pleased with that result (subject of course to its appeal rights if it is in fact unhappy). Secondly and more importantly, it seems to me that that excerpt out of clause 11(j) must be construed in the overall context of clause 11(j) and in the ordinary and plain meaning that, in so far as Ontario law applies, the first past the post/first come first served principle will operate.

13 It appears to me that the provisions of Clauses 8 and 18 set out above demonstrate that the intent is to trigger Homeco's obligation to pay once a claim has been finally determined by judgment or settlement (and endorsed by Homeco) and to vest in the claimant at that time a deemed right to recover such judgment or settlement against Homeco. As well it appears clearly contemplated that finally determined claims under the subject Policies will be paid as presented on a first come, first served basis. I do not see that there is any provision in the subject Policies which would allow or require Homeco to consider claims or potential claims which have not been finally determined by judgment or settlement as opposed to its obligation to pay claims which have been finally determined. To impose a requirement on Homeco (and a restriction on a successful claimant's direct right) which would oblige Homeco to defer payment (and the claimant collection) until such time as all claims and potential claims under the subject Policies are known and finally determined would constitute an unwarranted rewriting of the subject Policies. See University of Saskatchewan v. Fireman's Fund Insurance of Canada, [1998] 5 W.W.R. 276 (Sask. C.A.) at p. 289; leave to appeal to the Supreme Court of Canada refused [1997] S.C.C.A. No. 641.

14 It seems to me that at common law as discussed in Cox v. Bankside Members Agency Ltd., [1995] 2 Lloyd's Law Reports 437 (C.A.) that the "first past the post" or "first come, first served" principle was determined to be appropriate and in the interests of overall fairness. See Sir Thomas Bingham M.R.'s view, especially at pp. 457-60. He stated at p. 457:

> It was inherent in the Judge's approach that he considered chronological priority to be the basic rule, from which any departure must be justified. This approach was not challenged, and is plainly correct. In the absence of a stay, a successful plaintiff may enforce his judgment against the defendant as soon as it is given, and if an insured defendant is insolvent he may seek to be indemnified (subject to the terms of the policy) directly by the insurer. There must be some good reason for departing from the basic rule that a successful plaintiff is entitled to the fruits of his judgment.

Saville, L.J., added at pp. 466-7:

> I can see no reason why equity should intervene to require that those first to call on the policy should have to share their recoveries with later claimants if and when the insurance became exhausted.

This was after the court considered and rejected arguments for rateable allocation based on equity, implied agreement between multiple insureds, the direct right of action, trust or some other form of fiduciary obligation. The exception as outlined by Peter Gibson, L.J., at p. 463 where "a group judgment is obtained or where more than one is obtained at the same time" is not to my mind a true exception to the first past the post principle since conceptually all such claimants would be passing the post at the same time.

15 See also Harmon v. State Farm Mutual Automobile Insurance Company, 232 So. (2d) 206 (1970 Fla. App.) where Hobson, C.J., stated at p. 206 in referring to public policy supporting the first come, first served principle:

> ... we feel that to impose a duty upon insurers to ascertain all claimants under their uninsured motorist coverages before settling with any, and to require them to settle such claims at their peril is contrary to the policy of encouraging compromises and speedy settlements, and would do more harm than good. If such a duty is to be imposed under the uninsured motorist statute, it must be done by the legislature.

Thus this concept is not foreign to U.S. jurisprudence.

16 I have found nothing in the Ontario Insurance Act which would require a deviation from the first past the post principle.

17 With respect to the "binding" element of this proceeding, I was referred to the Cox case where Sir Thomas Bingham, M.R., stated at p. 456:

> In order to seek an authoritative ruling on this issue (and also other issues, of which one is considered below), E&O underwriters issued an originating summons joining as defendants all agents and Names whom they wished to bind by the decision of the Court. The underwriters' objective, obviously legitimate, was to protect themselves against the risk of being ordered to pay twice.

There is of course nothing the matter with such an applicant wishing to get as much certainty as is possible - but that must be legally possible. The question in the Cox case as to binding non-English parties was not discussed. It seems to me that their rights were probably affected both legally and practically by the Third Parties (Rights against Insurers) Act, 1930 (U.K).

18 At paragraph 29 of the Tatulli affidavit, he has sworn that Homeco has served the various parties as set out in relief item 4. None of those so served has come forward to contest that they were not properly served nor otherwise not subject to the jurisdiction of this court. Of course that relief will also be subject to enforcement in jurisdictions outside Ontario to the extent that the rights of parties outside this jurisdiction are affected. The SK Outside Directors raised the issue that the covering letter to the material given those served did not specify the other elements of relief asked for - namely relief items 1 and 4. However it seems to me that that relief was plainly and obviously set out in the Notice of Motion served on them, that that would be the proper and appropriate place for those served to carefully review (as opposed to an "overview" in a letter), that that would be obvious that the relief being sought would to some degree or other affect their rights as otherwise they would well ask why they were being served with the material and lastly it would not be prudent to merely look at the letter and ignore the legal documentation. However a foreign court may view this differently.

19 Thus subject to the caveats as to enforceability outside Ontario, Homeco is entitled to the declarations it has requested. Declarations subject to the caveats accordingly as to relief items 1, 2, 3 and

4. Given the circumstances of these proceedings, each is to bear its own costs.

FARLEY J.

TAB 2

Case Name:

Hollinger International Inc. v. American Home Assurance Co.

Between
Hollinger International Inc., (applicant), and American Home Assurance Company, Chubb Insurance Company of Canada, ACE INA Insurance Company, Zurich Insurance Company, Royal & SunAlliance Insurance Company of Canada, Gerling Global Canada, Temple Insurance Company, Continental Casualty Company, Lloyd's Underwriters, AXA Corporate Solutions Assurance, The Ravelston Corporation Limited, Hollinger Inc., Conrad M. Black, Barbara Amiel-Black, John A. Boultbee, David Radler, Daniel W. Colson, Richard N. Perle, Mark Kipnis, Argus Corporation Limited, Ravelston Management Inc., 3396754 Canada Ltd., 504468 N.B. Inc., Hollis McCurdy, W. John McKeag, Ana Porter, Ronald Riley, Stephen Hastings and Mark Horning, (respondents)

[2006] O.J. No. 140

[2006] O.T.C. 35

34 C.C.L.I. (4th) 17

144 A.C.W.S. (3d) 1098

2006 CarswellOnt 188

Court File No. 05-CL-5951

Ontario Superior Court of Justice

C.L. Campbell J.

Heard: November 29-30 and December 1, 2005.
Judgment: January 13, 2006.

(129 paras.)

[Editor's note: Supplementary reasons for judgment were released May 11, 2006. See [2006] O.J. No. 1898.]

Civil procedure -- Judgments and orders -- Declaratory judgments -- The applications of American Home, Chubb and International successfully sought declaratory relief authorizing the funding of a

settlement reached in a derivative action commenced in the State of Delaware in the sum of US$50 million.

Corporations and associations -- Corporations -- Actions -- By corporation -- Derivative actions -- The applications of American Home, Chubb and International successfully sought declaratory relief authorizing the funding of a settlement reached in a derivative action commenced in the State of Delaware in the sum of US$50 million.

International law and conflict of laws -- Conflict of laws -- Corporations -- The applications of American Home, Chubb and International successfully sought declaratory relief authorizing the funding of a settlement reached in a derivative action commenced in the State of Delaware in the sum of US$50 million.

The applications of American Home, Chubb and International sought declaratory relief authorizing the funding of a settlement reached in a derivative action commenced in the state of Delaware in the sum of US$50 million (subject to retention amounts) -- The settlement was on behalf of claims against directors of International -- The issue before the court was whether or not the process by which the settlement came about and was to be approved by the Delaware court was fair and in accordance with the obligations of the settling parties under the Policies of Insurance in accordance with the contractual rights and entitlements of the opposing directors and Excess Insurers -- The applicants submitted that neither the insured Inside Directors nor the Excess Insurers had raised concerns that would justify the Courts withholding approval when the Primary Insurers had a contractual obligation to International to not unreasonably refuse to consent to the proposed settlement -- HELD: The court found that the process of the settlement met the test of commercial reasonableness -- On the material before the court, it was satisfied that it was a reasonable exercise of judgment on the part of those directly involved in the settlement process to conclude, as they did, that given the risk that a summary judgment motion would not succeed, a settlement should proceed without that determination -- The court was satisfied that both American Home and Chubb clearly understood the nature of their duties to the Excess Insurers and had done their best to live up to them -- Based on review of the process leading to settlement and the risk related to a summary judgment motion not proceeding, the court held that in the circumstances of the process of the settlement, that it be authorized at this time and subject to certain conditions that the Primary Insurers American Home and Chubb had exhausted their contractual limits and were released from any other claims against them from events arising under their policies -- The conditions were that the Delaware Court approve the settlement as fair and reasonable, bearing in mind the issues raised by the inside directors and excess insurers, and that any remaining issues regarding the obligation of American Home, Chubb or International's responsibilities for defence costs incurred, submitted and payable prior to completion of the settlement, would be resolved or determined by the court -- Following determination by the Delaware Court of the propriety and approval of the settlement under Delaware law, the parties could make submissions on the issue of costs.

Counsel:

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Richard H. Krempulec, Q.C. for American Home Assurance, Mary Margaret Fox for Chubb Insurance, Gary H. Luftspring for Royal & SunAlliance, Zurich and ACE INA, Steve Stieber for Encon/Axa, Christopher McKibbin for GCan (formerly Gerling), Peter F.C. Howard, Timothy M. Banks for Richard N. Perle, Jennifer S. Dent, for Richters, Receiver to Ravelston and Argus, Stephen Scholtz, Alison Kuntz for Lord Black and Lady Amiel-Black; Geoffrey Adair Q.C., Marcella Saitua for Hollinger Inc.

REASONS FOR DECISION

1 **C.L. CAMPBELL J.**:-- This Application of Hollinger International Inc. ("International") and the companion Applications of its insurers, being court file numbers 05-CL-5951A through 05-CL-5951H, first came before the Court in late July 2005.

2 By an endorsement dated July 27, 2005, those applications were adjourned to permit a further evidentiary hearing to permit clarity on some of the issues raised by the Conditional Settlement reached between International and the first layers of its insurers in respect of a derivative shareholders' action brought on behalf of International against both its Inside (management) and Outside (independent) Directors of the "Cardinal" action commenced in the State of Delaware. The conditional Settlement will be referred to variously as the Cardinal Settlement and the Settlement.

3 The July 27, 2005, Endorsement is attached as Appendix A to these Reasons [Editor's note: See [2005] O.J. No. 3244.] to provide background while avoiding repetition in this decision.

4 When this matter was heard over three days in November and December 2005, two of the insured parties who had previously opposed approval of the Conditional Settlement withdrew their opposition.

5 Hollinger Inc. ("Inc"), subject to certain conditions (referred to below) advised the Court that it was withdrawing its claims for relief set out in its Application, being part of Court File 05-CV-289537 PD2 and now consents to a dismissal of its outstanding action against American Home, and supports the position of International, American Home and Chubb in respect of their request for approval of the Cardinal Settlement.

6 The Court was advised by counsel for RSM Richter Inc., that in its capacity as receiver, receiver manager and interim receiver of The Ravelston Corporation Limited, Ravelston Management Inc. and Argus Corporation, they supported the Cardinal Settlement in the Delaware action and withdrawing the claims for relief set out in court files 05-CV-289535 PD3 and 05-CL-5951F subject to conditions (referred to below.)

7 Four additional affidavits were filed for the November hearing, those of Professor Lawrence Hamermesh, James Van Horn, The Hon. Nicholas Politan and Joseph Smick. Cross-examination on the latter three affidavits was conducted before me as part of the hearing.

8 The policies of indemnity insurance issued by American Home and Chubb (the "Primary Insurers") under which the Cardinal Settlement to be approved in the Delaware Court of Chancery is to be funded are governed by Ontario law, hence the declaratory relief is sought in this Court.

9 Under the Cardinal Settlement, International is to receive US$50 million from American Home and Chubb in respect of damages attributable to the potential legal liability of non-management Outside Directors.

10 The July endorsement described the issue on the Applications before me as follows: "Did [the Applicants] reasonably and fairly conclude a Settlement taking in consideration the potential rights and entitlements of other insureds (the Inside Directors Inc., and related companies) as well as Excess Insurers?"

11 None of the parties before me has objected to the above description. The Excess Insurers under the following form policies submit that approval should not be given to the Cardinal Settlement, as American Home and Chubb have not fulfilled their contractual obligations to the Excess Insurers under

the policies in issue.

12 The following quotation, from a letter from counsel for the third Excess Insurers to counsel for International, sets out the insurers' position. (For this purpose, there is no reason to distinguish between the third and fourth Excess Insurers):

> Based upon all the foregoing, if International and/or the Independent directors do enter into a settlement with American Home and Chubb whereby the entirety of the proceeds from the underlying insurers' policies are used to fund a settlement of the Derivative Action, such a settlement would appear to constitute a voluntary payment by the Insureds; and the Third Excess Insurers would not recognize such a settlement as exhausting the underlying policy limits.

13 The directors who oppose the Cardinal Settlement (with the exception of Richard Perle) are all "Inside Directors," being part of management of International at the relevant time: their opposition is based on the premise that they were not involved in the Settlement process, as they were entitled to be in discharge of the insurer's policy obligation.

14 The base of the opposition of both the Excess Insurers and the Inside Directors has to do with defence costs. It is the position of the Applicant Primary Insurers that the Cardinal Settlement payment will discharge their obligation under their policies. The result will be that monies that would otherwise be paid to International in respect of the Settlement will be unavailable to be used for the defence of the Inside Directors in other actions to which they are exposed. The obligation for payment of defence costs would then pass to the Excess Insurers, the result being that less money would be available from the Excess Insurers for liability payments.

15 The material before the Court leads to the conclusion that if the Settlement is not approved before this Court, the policy limits of the Applicant Primary Insurers would be entirely paid out in defence costs of either the derivative action in Delaware or other litigation in which all the directors, both Inside and Outside, as well as Inc. and other related entities, are at risk.

16 The Excess Insurers would rather see funds proposed for the Settlement used to reduce the obligation they would otherwise have in respect of defence costs.

Policy Provisions

17 The "Executive and Organization Liability Policy" issued by American Home Assurance Company is what is known as a policy of indemnity and provides that the named corporate entities, including International, are entitled to be indemnified in respect of what is defined as an "indemnifiable loss."

18 An "Indemnifiable Loss" occurs when a corporate insured has indemnified or is permitted or required to indemnify an "Insured Person" pursuant to law or contract or by-law or operating agreement of the Company.

19 "Insured Persons" include in effect officers and directors of insured corporations. "Loss" as a defined term under the Policy includes settlements, judgments and Defence Costs, which is defined under the Policy as follows:

> "Defence Costs" means reasonable and necessary fees, costs and expenses consented to by the Insurer (including premiums for any appeal bond, attachment bond or similar bond arising out of a covered judgment, but without any obligation to apply for or furnish any such bond) resulting solely from the investigation, adjustment,

> defence and/or appeal of a Claim against an Insured, but excluding any compensation of any Insured Person or any Employee of an Organization.

20 The Policy further provides that amounts incurred for legal defence shall reduce the limit of liability available to pay judgments or settlements. The provision relating to retention amounts is not relevant for the purpose of this decision.

21 The Primary Policy of American Home affords an aggregate limit of liability of US$20 million. An Excess Policy issued by Chubb affords US$25 million of coverage and an American Home Excess Policy affords a further US$5 million coverage. These three policies afford a total limit of US$50 million and for the purpose of these Reasons are referred to as the Primary Insurers.

22 A further US$80 million coverage is provided by Policies issued by what are referred to here as the Third and Fourth Excess Insurers. For the purposes of these Reasons, it is not necessary to distinguish between them.

23 General Condition "A" under the Excess Policies reads as follows:

> A. Company/Claims Participation
>
> The Insurer shall at all times have the right, but not the duty, to participate in the investigation, settlement or defence of any Claim covered by this Policy which appears to the Insurer to be likely to involve the Insurer, even if the Underlying Limit has not been exhausted. The Parent Company and the Insureds shall give the Insurer full co-operation and such information as it may require.
>
> Notwithstanding anything contained in this Policy or any of the Underlying Policies, the Insurer shall not have, and does not assume, any duty to defend any Claim under this Policy.

24 It is to be noted that in addition to the claims arising in the action to which the Cardinal Settlement applies, the Insurers were notified of a number of other claims. In respect of some of the additional claims, the Excess Insurers have denied coverage but have neither accepted nor denied coverage in respect of the claims involved in the Cardinal Settlement.

The Cardinal Action Settlement

25 The nature of the Cardinal Action and Settlement is described in the factum of International, as follows:

> The Cardinal Action seeks redress for significant injury inflicted upon International by Conrad Black and his confederates, facilitated and abetted through use of companies under Black's control. The derivative claims in the Cardinal Action against the Black Group, although technically still pending, have been effectively superseded by International's direct claims against the same parties in separate litigation in Illinois. However, the Cardinal Action derivative claims alleging a total lack of oversight of the Black Group's impugned transactions by International's independent or outside directors have not been superseded by any direct International action. Those claims were conditionally settled in the matter currently before this Court.

26 The Cardinal Settlement contains a term that this Court approve in terms of the relief contained in paragraphs 1(a) and (b) of the International application, as follows:

(a) an order declaring that American Home Assurance Company ("American Home") and Chubb Insurance Company of Canada ("Chubb") are authorized and/or required to fund, to a total of U.S. $50 million, the settlement of claims made against certain individual defendants in an action commenced by Cardinal Value Equity Partners, LP ("Cardinal") in the Court of Chancery for the State of Delaware (the "Delaware Court"), bearing Civil Action No. 105-N (the "Cardinal Settlement"), and that such funding occur following approval by the Delaware Court that the settlement is fair and reasonable and in the best interests of International's shareholders;

(b) an order declaring that payment by American Home and Chubb of the limits of their respective policies to fund the Cardinal Settlement, or of any limits remaining after other payments for covered loss ranking in priority to the Cardinal Settlement have been made, does not violate the interests of any party before the Court, shall exhaust the limits of the American Home and Chubb policies, and shall discharge American Home and Chubb from any remaining obligations under their respective policies;

27 The Settlement Agreement and other requested relief sought to be approved before this Court contemplate that the Delaware Court conduct a hearing in accordance with Delaware law that will determine fairness of the Settlement to International's shareholders.

28 In essence, the issue before this Court is whether or not the process by which the Settlement came about and is to be approved by the Delaware Court is fair and in accordance with the obligations of the settling parties under the Policies of Insurance in accordance with the contractual rights and entitlements of the opposing directors and Excess Insurers.

The Evidence

29 The evidence reveals that the Cardinal derivative litigation was commenced in Delaware on December 9, 2003, against International and all its directors at the time of the events complained of.

30 In January 2004, Cardinal agreed to stay its action pending completion of an investigation by the Special Committee of the Board of Directors of International.

31 In addition, a consolidated class action complaint was commenced in Illinois by purchasers of International securities against the Company and related entities and all its directors, both Inside and Outside (the "Illinois Securities Litigation" or "Class Action.")

32 Michael Mitrovic, president of Worldwide Financial Claims, American International Group, attested at paragraph 22 of his affidavit dated June 23, 2005, that "The Cardinal litigation and the Illinois securities litigation are afforded coverage [by his company] subject to the terms and conditions of the Primary Policy."

33 There was another action in Illinois that had been commenced by International through the Special Committee against the Inside Directors, which included Richard Perle. This claim was not covered by the primary policy because of the insured vs. insured exclusion in the policy.

34 Apparently as a result of discussions sometime in late spring or early summer of 2004 among International, its counsel and brokers, various counsel on behalf of Outside Directors, and as well American Home, it was agreed that there should be a mediation of the issues involved in both the Cardinal and Class Actions.

35 The Hon. Nicholas H. Politan, a retired judge for the United States District Court for the District of New Jersey, was chosen and agreed to act as mediator. Following a preliminary session before him, the first formal session was held in New York on August 6, 2004. Those invited to that initial session included those thought by James Van Horn (general counsel of International) to be most relevant. They included International, counsel for its Outside Directors, all insurers, the plaintiffs in the Class Action and the Cardinal Action. Some Excess Insurers were aware of the mediation but were not specifically invited to attend.

36 Mr. Van Horn was of the view that with respect to the Cardinal Action, given the Company's claim against the Inside Directors, the Settlement of the derivative claim against them would not be possible.

37 As to the defendants in the Class Action, Mr. Van Horn was of the view that any settlement would be driven by the Company and as a result representatives of other defendants would not be necessary, at least at the first session.

38 Judge Politan affirmed in his affidavit, filed and in evidence before me, that at the August 6, 2004, mediation, he determined that if progress were to be made, the number of individuals involved in the process had to be pared down.

39 Judge Politan was aware that the position taken by International as against Inside Directors would make settlement of those claims impossible, that "to the extent that if such settlement was to be funded with insurance proceeds, a condition of any settlement would be that claims against all settling insured defendants would have to be released."

40 Judge Politan further concluded that based on his "understanding that coverage was not being denied to the Outside Directors by any of the Insurers involved and based on the total amount of available coverage, that counsel for the Outside Directors did not need to be in attendance at any of the further mediation sessions." He understood that if settlement were to take place, it would likely be within the US$50 million of the Primary Insurers.

41 Prior to convening the initial session on August 6, 2004, Judge Politan had available to him the pleadings in both the Cardinal and Illinois Class actions, the decision of Judge Strine of the Delaware Court (the only proceeding in which Lord Black has testified) and had consultation with Mr. Breeden of the International Special Committee.

42 Later in August and for the remaining sessions over which he presided, Judge Politan had a copy of the 500-page Special Committee Report, which provided many specific details of allegations of wrongdoing by Lord Black and of lack of oversight by other directors, both Inside and Outside.

43 The mediation before Judge Politan ultimately did not succeed and took place in circumstances where the particulars of discussions before him, including those he had with Mr. Breeden, were subject to mediation privilege over the several sessions.

44 Judge Politan testified before me and I accept his evidence that

(a) he was satisfied when it became apparent that the Illinois Class Action would not settle, that he had before him all the relevant parties and their counsel if settlement of the Cardinal Action were to be successful;
(b) as he was aware of the "tower of insurance," (i.e., the limits of all policies) and he was satisfied that there was sufficient insurance to deal with all the plaintiffs' claims;

(c) he accepted and acted in the mediation on the premise that there was significant risk to the Outside Directors that the claims against them would survive a summary judgment motion and if so, would give rise to a significant damage claim and potential risk of liability and the incurrence of very significant defence costs;
(d) from his involvement in the process, Judge Politan is of the opinion that given the risk and potential exposure, the proposed Settlement by American Home and Chubb of US$50 million (subject to retention of $2.5 million) is a "fair and reasonable amount reflecting a compromise of the parties' positions;"
(e) that the Settlement was preceded by lengthy negotiations among highly experienced counsel who were well-prepared, extremely knowledgeable about the facts and the law, who advocated vigorously for their clients.

45 James Van Horn, general counsel of International, confirmed, and I accept, that the Cardinal Settlement was effected through a process of arm's length negotiations between sophisticated parties, each of whom was fully informed with the pertinent facts, and that US$50 million was considered a reasonable figure, particularly as the total damages of International would exceed US$400 million with costs to date in the US$10-20 million range and mounting.

46 The third witness whose affidavit was the subject of cross-examination before me was Joseph M. Smick, a coverage attorney retained by the respondent Zurich but filed on behalf of all the Excess Insurers.

47 Mr. Smick's affidavit detailed the involvement he had on behalf of his client and the Excess Insurers in the settlement process. I accept his evidence that the Excess Insurers were aware of, and not directly involved in, the mediation/settlement process.

48 I also accept that in March and April of 2005, the Excess Insurers advised International of their position that:

(a) the Excess Insurers were entitled to participate in settlement discussions;
(b) they had little information about the settlement process; and
(c) they expressed concern that a summary judgment motion might result in the dismissal of the Cardinal claims against the Outside Directors.

49 In essence the position of the Excess Insurers is that they are entitled to oppose the Settlement based on their lack of involvement in the process both now being satisfied that a summary judgement motion should have been brought as it had a more than reasonable chance of success and that they have not had a satisfactory explanation at to why US$50 million is a reasonable amount when all it really does for the Primary Insurers is resolve some defence costs and has no direct relationship to any damages claimed.

The Inside Directors

50 The position of the Inside Directors was advanced primarily by counsel on behalf of Lord and Lady Black. It is their position that in agreeing to the Cardinal Settlement, American Home has breached an entitlement they have as insureds to advance to the Blacks all fees, costs and expenses incurred by them in defence of both the International Illinois action and the U.S. consolidated Class Action, as well as those incurred in the Cardinal action and in other proceedings.

51 The basis of the position of the Blacks is that they were owed a duty by the Primary Insurers:

(i) to advise them of the mediation;
(ii) not to preclude them from participating in the mediation; and
(iii) to provide them with details of the Cardinal Settlement, which was refused until after it was executed.

52 In addition, it is urged that the effect of the Settlement results in an improper preference choice as between insureds and is improvident in the sense that US$50 million is excessive for the release of only the Outside Directors in an otherwise dormant and stayed proceeding.

Position of Richard Perle

53 Mr. Perle is in a unique position as a director of International. It is his position that the Primary Insurers are in breach of their contractual obligations to him, since he was not included in the Cardinal Settlement as an Outside Director.

54 While Mr. Perle served on the Executive Committee of International from 1996 to 2003, he has never been a member of management or an officer of International. He was, however, CEO of Hollinger Digital LLC, a subsidiary of International.

55 Mr. Perle's complaint is that his individual rights were not considered during the settlement process and that he was entitled to have them addressed prior to completion of the Settlement. I accept the evidence that Mr. Perle was characterized by Mr. Mitrovic of American Home as a "grey hat." This was largely because Mr. Perle was added as a defendant in the Special Committee Illinois action commenced by the Company on the basis of his participation in receiving certain compensation payments.

56 In essence, Mr. Perle claims that both the Primary Insurers and International failed to adequately take into account his particular situation in conducting settlement negotiations and in reaching settlement, without giving him detailed reasons why he was not so included. In so doing he says, they are in breach of their respective contractual obligations to him.

Analysis and Law

57 The basic position of International and its Primary Insurers is that the conditional Settlement that is before this Court and the court in Delaware for approval should be found to be reasonable within the applicable legal test in each jurisdiction.

58 The applicants submit that neither the insured Inside Directors nor the Excess Insurers have raised concerns that would justify the Courts withholding approval when the Primary Insurers have a contractual obligation to International to not unreasonably refuse to consent to the proposed settlement.

59 Under the Cardinal Settlement, the insured Inside Directors are not deprived of the ability to object to the Settlement in the Delaware Court. The effect of the Settlement is to resolve the derivative action as against all directors, not just the Outside Directors. What it does not do is release the Inside Directors from further claims against them by International that will continue in the action in Illinois. The Outside Directors do obtain the benefit of that release.

60 International and the Primary Insurers urge that the task before this Court is not to make a definitive finding as to whether the proposed settlement is reasonable. Rather, they suggest, and I agree, that the task of this Court is to determine whether the process by which the Settlement was concluded, taking into consideration the contractual rights and entitlements of all parties including International, the Primary Insurers, the Excess Insurers and all of those who claimed to be insured was reasonable.

61 The test in my view is, was there a reasonable basis for the Settlement, taking into account the competing interests of the various constituents? I accept that correctness of the Settlement itself is not the test; rather, was the Settlement, in all the circumstances, within the range of reasonableness, recognizing that it was a compromise?

62 In Ontario New Home Warranty v. Chevron Chemical Co. (1999), 46 O.R. (3d) 130, Winkler J. of this Court commented on the approval process of a Class Proceeding. I am of the view that his comments in the following paragraphs are appropriate to the considerations before me:

> [88] Finally, I turn to the settlement. For a settlement to be approved it must be fair, reasonable and in the best interests of the class and, as stated in Dabbs, will generally take into account factors such as:
>
> 1. likelihood of recovery or likelihood of success;
> 2. amount and nature of discovery, evidence or investigation;
> 3. settlement terms and conditions;
> 4. recommendation and experience of counsel;
> 5. future expense and likely duration of litigation;
> 6. recommendation of neutral parties, if any;
> 7. number of objectors and nature of objections; and
> 8. the presence of arm's length bargaining and the absence of collusion.
>
> [89] The exercise of settlement approval does not lead the court to a dissection of the settlement with an eye to perfection in every aspect. Rather, the settlement must fall within a zone or range of reasonableness. The range of reasonableness has been described by Sharpe J. in Dabbs v. Sun Life Assurance Co. (No. 2) (1998), 40 O.R. (3d) 429, 22 C.P.C. (4th) 381 (Gen. Div.) as follows at p. 440:
>
> > ... all settlements are the product of compromise and a process of give and take and settlements rarely give all parties exactly what they want. Fairness is not a standard of perfection. Reasonableness allows for a range of possible resolutions. A less than perfect settlement may be in the best interest of those affected by it when compared to the alternative of the risks and costs of litigation.
>
> [93] ... Further, the terms of the settlement were arrived at as a result of intensive mediation conducted by an experienced arbitrator with specific knowledge of the factual background. The settlement benefits to the plaintiff class are well within the range of reasonableness.
>
> [94] In conclusion, I find that the settlement is fair and reasonable and in the best interests of the class as a whole.

63 Having heard the additional evidence by way of affidavit and cross-examination before me, particularly that of Judge Politan and Mr. Van Horn, I make the following findings in response to the questions raised at paragraph 16 of the previous endorsement:

a) I am satisfied that given his mandate and his preliminary considerations of issues and amounts, it was neither inappropriate nor necessary to involve counsel for any of the directors or Excess Insurers in the process before Judge

Politan. He quickly became aware that the Class Action would not be included in the settlement process and that in his view, given the costs of the various actions and the remaining amount of insurance available, the Primary Insurers at least in the first instance, could represent the interests of the Outside Directors. There was no party before him suggesting settlement on behalf of the Inside Directors.

b) I am satisfied on the evidence that, given the complexities of the Class Action in Illinois, the claim of the Special Committee in Illinois and the mounting costs associated with continuance of the derivative action, that it was neither reasonable nor practical to attempt to resolve all claims involving the Outside Directors in all actions.

c) The issue of approval of the Delaware settlement will be addressed separately.

d) There was some evidence before me relating to the amount of the Settlement. The issue of mediation privilege will be addressed separately. There are several factors on which I rely to conclude that at least for the purposes of approval by this Court, the figure of US$50 million is not unreasonable:

   i. The Settlement did not take place during the mediation conducted over several sessions between August and October 2004. The parties were engaged for several more months in negotiation before it was completed.
   ii. Judge Politan was satisfied that based on the mediation process before him, the figure was within a reasonable range.

   Given the costs being absorbed by International in respect of itself and Outside Directors rising to the millions of US dollars exposure must include costs as well as risk.

e) I am satisfied that the Excess Insurers (although aware of the discussions) were not directly consulted on the issue of reasonableness, since the negotiations did not include (subject to the issue of defence costs to be addressed below) exposure to the Excess Insurers for liability indemnity.

   Concern was expressed on behalf of the Excess Insurers that the Delaware Court would only be interested at the Settlement approval hearing that the US$50 million figure provided was enough for the plaintiffs, not that in the circumstances it was too much.

   I accept that the Excess Insurers are not automatically parties with standing in respect of the Settlement approval before the Delaware Court. To the extent that any leave or approval is appropriate from this Court to allow the insurers to present their views to the Delaware Court, it is granted. I would expect that if the Delaware Court would conclude that the facts could not support liability on Outside Directors, that the Settlement would not be approved. I am supported in this approach by reference to the decision of the Court of Appeal for Ontario in Re Ravelston Corporation and Ravelston Management, [2005] O.J. No. 5351, Docket M33075 (November 10, 2005), where in reference to an issue as to whether Ravelston could be summonsed criminally in Illinois, the Court upheld Farley J.'s conclusion that it was not necessary to answer a question of foreign law but rather did the Receiver act reasonably in deciding what to do. I am satisfied that in making the Settlement subject to approval of Courts both in Ontario and in Delaware, the applicants have acted appropriately.

I note that in any event, the opposing directors are parties with standing and take the position before this Court that they are entitled to take before the Court in Delaware: that the applicants have not established that the amount of the Settlement in respect of the Outside Directors is reasonable or prudent.

f) I have been advised and accept that privilege was claimed in respect of the details of the mediation process, since that was the basis on which both the mediation was conducted and the Settlement was concluded. I have heard sufficient evidence of process that I see no basis on which it would be necessary or appropriate to violate a process into which the parties entered on the basis of confidentiality.

64 I am satisfied that the process of the Settlement meets the test of procedural reasonableness. International saw the opportunity to recover from proceeds of insurance a sum of money in partial recompense for wrongs committed against the Company.

65 The Primary Insurers who had not established a basis for denying coverage in respect of the Outside Directors legitimately felt obligated to respond to the request of its insureds being International and Outside Directors.

66 Mediation was an appropriate step to undertake. An experienced and highly qualified mediator in Judge Politan was in the best position to determine the issues of who should be involved, what could be accomplished and how the process should be carried out.

67 Judge Politan had the benefit initially through information provided by the Chairman of the Special Committee and later from the Report of that Committee itself to allow determination that a settlement of the Class Action was not possible, nor was it possible to resolve International's claims against management directors.

Summary Judgment in Delaware

68 I accept the conclusion reached by American Home, Chubb and International as being reasonable, that there was at least risk that a summary judgment motion brought in the Delaware Court on behalf of the Outside Directors might not succeed.

69 Counsel for the Excess Insurers as well as the Inside Directors submitted that this Court should find that under recent appellate authority in the appellate division of the Delaware Court of Chancery, a motion for summary judgment brought on behalf of the Outside Directors would likely succeed, thereby rendering the payment of US$50 million on their behalf under the Settlement in effect improvident.

70 This Court is not in a position to determine what would or might have been a conclusion from a summary judgment motion under Delaware law had it been brought at a time before the Settlement.

71 Suffice to say I accept that the conclusion reached by the parties to the mediation and Judge Politan the mediator, that there was risk that the summary judgment motion would not succeed, to be a reasonable one.

72 Without in any way wishing to be seen to opine on Delaware law, the recent decision in Re The Walt Disney Company Derivative Litigation, 2005 W.L. 2056651 dated August 9, 2005, illustrates the evolving nature of director and officer legal responsibilities. The decision is a successful appeal from a lower court judgment that it is urged restores the business judgment rule in Delaware.

73 Whether under statute or the common law in many jurisdictions across states and borders, the standard to be applied to particular facts illustrates an evolving area of law that makes prediction of result in any given case of director and officer negligence difficult.

74 As well, most jurisdictions (like Ontario) that have a summary judgment procedure apply their test in favour of trial where there are facts significantly contested, particularly when credibility is in issue.

75 On the material before me, I am satisfied that it was a reasonable exercise of judgment on the part of those directly involved in the settlement process to conclude, as they did, that given the risk that a summary judgment motion would not succeed, a settlement should proceed without that determination.

76 I accept the proposition that a mediation and settlement conducted under terms of confidentiality should be honoured. Indeed, it is a hallmark of most mediative processes that they are conducted in a without prejudice confidential atmosphere.

The Settlement Process

77 I am satisfied, having read and heard the evidence of the witnesses, that for the purpose of determining the reasonableness of the process (including their view on the amount of the Settlement), it is not necessary for this Court's determination to go further into the details of the determination of the quantum.

78 Issues of the quantum of the Settlement and consideration of the exposure of the Outside Directors as opposed to Inside Directors is in my view a matter for the Court in Delaware.

79 The result of the Cardinal Settlement is to reduce in complexity a significant amount of litigation as well as the associated defence costs. Among other cases that are substantially resolved is the claim by Inc in the Superior Court of Ontario restraining or preventing American Home and Chubb from completing the Settlement.

80 The claims in the Special Committee of International against the Outside Directors, as well as the claims against the Inside Directors in the Cardinal action are to be dismissed. Those against the Inside Directors are without prejudice to International's continuance of the claims against Inside Directors in the Special Committee action.

81 Unlike the cases relied on by the Excess Insurers, this is not a case of an improvident settlement. The proposed settlement is conditional on approval by two Courts in two jurisdictions. I recognize that the Outside Directors will still be involved in the Class Action but their removal from two actions will substantially reduce defence costs.

82 In the Delaware Court, an argument will be advanced by at least the Inside Directors that the Settlement should not be approved by that Court, since the proposed amount does not realistically deal with the risk faced by the Primary Insurers on behalf of the Outside Directors. I have granted leave, to the extent that this Court can, to the Excess Insurers to join in advancing those submissions in Delaware.

83 In addition, any approval of the Settlement in this Court will be conditional upon a determination by this Court of the amount (if any) of defence costs for which the Primary Insurers or International should bear responsibility. That determination will depend on what defence costs submitted in accord with the policy terms were payable to any of the insured up to the date of the Settlement Agreement.

84 As I am satisfied with respect to the process of the Settlement, taking into consideration the rights

of Excess Insurers and insureds, the onus rests on them to establish it is not fair and reasonable to all insureds and insurers.

85 In Transit Casualty Co. v. Spink Corp. (1979), 94 Cal. App. 3d 124, an excess insurer successfully recovered damages against both a primary insurer and the insured when it was called upon to contribute to a judgment exceeding the primary limits on the basis that it had not been notified by either the insured or the primary insurer of an offer of settlement that, if accepted, would have eliminated exposure on the part of the Excess Insurer.

86 As the Court noted at p. 8 of its judgment:

> The parties [being insured, primary and excess insurers] occupy a three-way relationship, which regardless of privity gap may engender reciprocal duties of care in the conduct of settlement negotiations; when a damage claim threatens to exceed the primary coverage, the reasonable foreseeability of impingement on the excess policy creates a three-way duty of care ..."

87 I accept the statement as a general proposition.

88 A number of authorities from United States Courts, among them Hartford Accident and Indemnity Co. v. Michigan Mutual Insurance Co. (1983), 93 A.D. (2d) 337 (Sup. Ct. of N.Y. App. Div.); American Centennial Insurance Co. v. Warner-Lamber Co. (1995), 681 A. 3d 1241 (Sup. Ct. of N.J.); and Schal Bovis, Inc. v. Casualty Insurance Co. 732 N.E. 2d 1082 (Ill. App. 1 Dist. 1999), emphasize the nature of the duty of good faith and in circumstances fiduciary duty that exists between insurers. The American Centennial decision refers to "The Guiding Principles for Primary and Excess Insurance Companies" as supporting and elaborating the good faith duties.

89 A similar "Agreement of Guiding Principles Between Primary and Excess Liability Insurers Respecting Claims" has been promulgated on behalf of the insurance industry by the Insurance Bureau of Canada and elaborates good faith principles.

90 In addition to these references, at least two Canadian decisions at the appellate level have recognized that the relationship and duties as between primary and excess insurers may extend beyond contract. In Broadhurst & Ball v. American Home Assurance Co. (1990), 1 O.R. (3d) 225 (C.A.), the Court of Appeal for Ontario, after noting that there was no contract term between the insurers regarding the defence, said at p. 241:

> Nonetheless, their obligations should be subject to and governed by principles of equity and good conscience, which, in my opinion, dictate that the costs of litigation should be equitably distributed between them.

91 In Aetna Insurance Co. et al. v. Canadian Surety (1994), 149 A.R. 321 (C.A.), the Alberta Court of Appeal, in the absence of contract between insurers and dealing with a complicated factual situation, said at paragraph 131:

> Understanding these relationships is important because duties may flow from a primary insurer to an excess insurer under certain circumstances.

92 I am satisfied that both American Home and Chubb clearly understood the nature of their duties to the Excess Insurers and have done their best to live up to them. The following factors support the conclusion I have reached:

1. The Excess Insurers were aware that settlement discussions were undertaken by International and the Primary Insurers.
2. The Primary Insurers advised the Excess Insurers of the position of International, that a settlement of the Cardinal action would benefit the plaintiffs in that action, the insured Outside Directors and International.
3. The Primary Insurers proceeded in good faith in the belief that settlement could be achieved without risk to the excess layers.
4. The Settlement Agreement itself required Court approval, both in the jurisdiction of the action (Delaware) and in the jurisdiction for determination of policy rights (Ontario) giving an opportunity for Excess Insurers and other insureds to voice their opposition in both forums.
5. The Settlement was made in circumstances where, given the number of claims to which they were exposed in multiple jurisdictions, there could be little doubt that the limits of the primary layers would be exhausted for indemnity for judgment and/or defence costs, with the costs of the insurers themselves adding to the their expenses.

93 The sole complaint that the Excess Insurers could have is that they were not notified of the settlement negotiations before they were conditionally concluded. I am satisfied that on the material before me, the actions of the Primary Insurers in proceeding as they did were not in breach of the duty of good faith to the Excess Insurers. Since the Excess Insurers had not agreed to coverage of the Cardinal action and had denied coverage to Inside Directors, there was little point in having the Excess Insurers at the negotiating table and they did not ask to be present.

94 I do accept that had the effect of the Settlement been to allow the Primary Insurers to avoid the payment of defence costs that had already been submitted to them and for which they were obligated to pay, that would raise a question regarding the issue of good faith.

95 It is not clear on the material that that has been the case. I am satisfied that in negotiating and finalizing the Settlement, all of Cardinal, American Home, Chubb and International believed that the claims were being resolved within the limits of the primary policies.

96 I am also satisfied that taking into account the Report of the Special Committee, American Home and Chubb reasonably concluded that the claims against Outside Directors could exceed policy limits as a matter of Delaware law. It is not for this Court to decide as between the legal opinions in Delaware law that have been filed by either side by expert opinion. Rather, I conclude based on the evidence filed on behalf of International and the Primary Insurers that there is at least a reasonable arguable opinion. The necessary approval by the Delaware Court gives the opportunity for the other side of the case to be fully argued.

Duty of the Primary Insurers

97 The Cardinal Settlement raises the question of the duty of an insurer to other insurers and insureds when a settlement occurs between primary layers the effect of which is to limit the pool available for other claims by other insureds who will look to Excess Insurers for coverage, defence costs and indemnity.

98 There is no suggestion before me that the initiation, negotiation and finalization of the Settlement as between the Cardinal plaintiffs, International and Outside Directors (including the Primary Insurers) imposed a duty on those insurers not to fund that settlement if it could be made within limits. The Primary Insurers had accepted coverage and the insured were calling on them to honour indemnity obligations.

99 The obligation on an insurer to indemnify and hold the insured harmless arises when liability of an insured to a third party is established and quantified by judgment, arbitration award or settlement [emphasis added]. See Cox v. Bankside, [1955] 2 Lloyd's Rep. 437 at 442 (G.B. Div. Comm. List.)

> When a claim is made under a first party policy the insurer must deal fairly and in good faith with the insured. This requires the insurer to make an objective analysis of the claim and to pay the claim, promptly and in full, when the criteria for payment have been met. It bears emphasis, for the point is often overlooked, that this aspect of the insurance relationship is not adversarial in nature.

Gordon Hilliker, Insurance, Bad Faith (Markham: LexisNexis Canada Inc., 2004) at p. 21.

703535 Ontario Inc. v. Non-Marine Underwriters, Lloyd's of London (2000), 184 D.L.R. (4th) 687 (Ont. C.A.) at p. 694.

100 I am satisfied that had the Primary Insurers failed to participate in the negotiations and to promptly deal with the subsequent settlement proposal, it would have exposed the Outside Directors to greater risk and put them in breach of their duty to their insured.

101 I am also satisfied that as a matter of Ontario law, without a justifiable basis, any refusal to participate in the negotiations and to respond to the proposed settlement would constitute a breach of the duties the Primary Insurers owed to the Outside Directors. The fact that there were other insureds under the policies and the fact that the potential existed for claims for indemnity to be made at some later point, did not provide a justifiable basis for the Primary Insurers to refuse to participate in the negotiations or to refuse to respond to the proposed settlement in a fair and prompt manner. See 703535 Ontario Inc., supra, at p. 695; Shea v. Manitoba Public Insurance Corp. (1991), 55 B.C.L.R. (2d) 15 (B.C.S.C.) at p. 85; Dillon v. Guardian Insurance Co. (1983), 2 C.C.L.I. 227 (Ont. H.C.) at p. 230.

102 The case of Whiten v. Pilot Insurance Co., [2002] 1 S.C.R. 595, has been given wide attention in the legal profession in Canada and among other matters, stands for the proposition that consent on the part of the insurer cannot be unreasonably withheld and failure to consent to a reasonable resettlement can constitute an independent bad faith action, exposing the insurer to punitive damages in certain circumstances (see p. 639).

103 I accept that the Primary Insurers acted reasonably in determining that the claims of the Outside Directors fell within coverage in the Cardinal action. It was suggested in argument that since the Special Committee action when initiated, initially included the Outside Directors, the effect of which would have been to trigger the "insured vs. insured" exclusion.

104 I conclude that the Special Committee was reasonable in reaching its decision that recovery of US$48 million in the Cardinal action as against the Outside Directors was reasonable and in the best interests of the Corporation.

105 Had the Special Committee let the Cardinal action proceed without taking it over on the Company's behalf as against the Inside Directors (which is the effect of the Settlement), there would have been continued exposure for the Outside Directors without eliminating all the insurers' indemnification obligations.

First Past the Post

106 The Inside Directors object to the Cardinal Settlement on the basis that it does not include them

and there may be insufficient funds in the "tower of insurance" to satisfy the defence costs and Settlement amounts to which they should be entitled.

107 In the first place, there is no suggestion in the material before me that any other insureds under the Policies have negotiated, attempted to negotiate or settled any claims against them or that any of the insurers have been requested to participate in or consent to any such resolution.

108 The recent criminal proceedings in the United States, which involve among others Lord Black, David Radler, Jack Boultbee and Peter Atkinson, all of whom were Inside Directors, would suggest that it will be some time, if ever, before the insurers accept coverage for those Inside Directors.

109 Mr. Perle now finds himself in a rather unique position among the directors. I accept that once the Special Committee included him as a defendant and kept him in as a defendant, the Primary Insurers were not presented with a settlement for which they were bound to cover on his behalf. Should he be successful in a summary judgment motion in the Special Committee action, he may well have a claim for indemnity as against International. Such claim may or may not be covered under the remaining policies. At this stage I am unable to conclude that there is any claim for bad faith on the part of the Primary Insurers or International for a failure to secure a settlement on behalf of Richard Perle.

110 There are few cases in this jurisdiction that deal with the rights as between insureds when one insured is indemnified by an insurer and the effect of the indemnity is to substantially reduce or eliminate the amount available for indemnity of another.

111 The analysis starts with the English Court of Appeal decision of Cox v. Bankside, supra. It stands among other things for the proposition that the rights of the respective parties are several rather than joint rights, thereby permitting respective insureds the ability to address, and resolve, claims independent of one another:

> Each contractual right of indemnity is in theory a separate right. When it accrues it gives rise to a new cause of action in its own right. It does not merge with the right previously accrued, so as to create a new cause of action for the joint amount of the two indemnities ...
>
> The true position is that individual third party liabilities give rise to no more than inchoate or contingent rights ... They are several, not joint rights. Each right will prove of value only if quantified liability is established before the limit of cover is reached.

112 There simply is no basis for an insurer to refuse to pay a valid and determined claim that falls within coverage without the risk of exposure to a claim for bad faith. See 703535 Ontario Inc., supra, at p. 694-5.

113 This principle was adopted by Farley J. of this Court in Re Laidlaw Inc. (2003), 46 C.C.L.I. (3d) 263 (S.C.J.) at p. 272 to the effect that the mere fact that other insureds have, or may have, claims that are not finally determined, cannot operate to prevent those otherwise entitled to indemnity from receiving it.

114 Farley J. went on to say, in respect of policy language similar to that in issue here:

> [I]t appears clearly contemplated that finally determined claims under the subject Policies will be paid as presented on a first come, first served basis. I do not see that there is any provision in the subject Policies which would allow or require Homeco to

> consider claims or potential claims which have not been finally determined by judgment or settlement as opposed to its obligation to pay claims which have been finally determined. To impose a requirement on Homeco (and a restriction on a successful claimant's direct right) which would oblige Homeco to defer payment (and the claimant collection) until such time as all claims and potential claims under the subject Policies are known and finally determined would constitute an unwarranted rewriting of the subject Policies.

115 The fact that a judgment or settlement may deplete or even extinguish proceeds available to other insureds does not detract from the principle: see Solway v. Lloyds Underwriters, [2005] O.J. No. 1331 (S.C.J.) at paragraphs 65, 69.

116 I was referred to several U.S. decisions that questioned the 'first past the post' principle. In my view, the facts can be distinguished from this case and they are not in accord with authorities in or adopted in Canada, which I conclude are compelling.

117 There are several United States decisions that are in accord with the principles set out above in Cox v. Bankside and Re Laidlaw. While each of those decisions turns on its individual facts, the most significant of these for present purposes is In Re Rite Aid Corporation Securities Litigation, 146 F. Supp. 2d 706 (E.D. Penn 2001). Rite Aid dealt with a securities class action against certain officers by which the corporation and its insurers assigned certain claims to its shareholders and settled with some but not all the defendants.

118 The non-settling defendants were held not to have standing to object to that part of the Settlement that did not affect them but did have standing to object to settlement terms that would eliminate their claims to indemnity.

119 In concluding that the insurer was not in breach of any duty of good faith, the Court rejected the proposition that an insurer may never settle claims against their policies unless the settlement involves all insureds under the policy. In relying for support on the decision in Re Anglo-American 670 A. 2d 194 (Pa. Cmwlth 1995), the Court in Rite Aid quoted the following from p. 199, adding the "caution that, in order for the insurer to accept the settlement offers, they must be reasonable" lest the insurer breach its duty of good faith. Travellers Indemnity Co. v. Citgo Petroleum Corp 166 F. 3d 761 (5th Cir. 1999) is to the same effect at p. 768. I accept the above proposition as being in accord with Ontario decisions.

Defence Costs

120 I noted at the beginning of these reasons that the major concern of both the Inside Directors and the Excess Insurers was that the US$50 million Settlement would eliminate those funds being available for defence costs.

121 I also noted the concern that since this was a settlement of a derivative action, it might be said that the insurers, the plaintiffs in the Cardinal action and International itself might not have the incentive to reach an arm's length settlement that would occur in other circumstances.

122 The withdrawal by both Inc. and the Ravelston entities of their opposition to approval of the Cardinal Settlement was made conditional. Those entities seek to be relieved from exposure to costs and to preserve their claims for defence costs that may relate to this and other proceedings if the Cardinal Settlement does not stand in priority as a claim under the policies.

123 It was submitted on behalf of one or more of the Excess Insurers that the time for determination

of whether or not the proposed settlement was reasonable would be after at least a trial of issue, which would look at all aspects of the timing, the amount and the degree of communication as well as the merits of the defence on the part of the Outside Directors.

124 I have concluded, based on the extended procedure before me, including the evidence adduced, that the process by which the Settlement was reached was fair and reasonable and in accordance with the obligation of good faith by American Home and Chubb to all its insureds and to the Excess Insurers.

125 I have concluded that the relief sought by the Applicants (being American Home, Chubb and International) should be granted subject to the following conditions:

1. That the Cardinal Settlement itself is approved both as to quantum and the legal principles involved by the Delaware Court.
2. To the extent that there are defence costs, which were submitted to and payable by the Primary Insurers prior to the date the Settlement was completed, those defence costs shall be determined by this Court and form part of the US$50 million whether payable by the insurers or by International.

Conclusion

126 The applications of American Home, Chubb and International seek declaratory relief authorizing the funding of a settlement reached in a derivative action commenced in the State of Delaware in the sum of US$50 million (subject to retention amounts). The Settlement is on behalf of claims against directors of International.

127 Based on review of the process leading to settlement, and the risk related to a summary judgment motion not proceeding, I find that in the circumstances of the process of this Settlement, that it be authorized at this time and subject to the conditions below that the Primary Insurers American Home and Chubb have exhausted their contractual limits and are released from any other claims against them from events arising under their policies.

128 The two conditions to which the relief granted is subject are:

(a) that the Delaware Court approve the Settlement as fair and reasonable, bearing in mind the issues raised by the Inside Directors and Excess Insurers.
(b) That any remaining issues regarding the obligation of American Home, Chubb or International's responsibilities for defence costs incurred, submitted and payable prior to completion of the Settlement, are resolved or determined by this Court.

129 Following determination by the Delaware Court of the propriety and approval of the Settlement under Delaware law, the parties may make written submissions on the issue of costs. If other issues arise from this decision, I may be spoken to.

C.L. CAMPBELL J.

TAB 3

Case Name:

Onex Corp. v. American Home Assurance Co.

Between
Onex Corporation, Gerald W. Schwartz, Christopher A. Govan, Mark Hilson and Nigel Wright, Plaintiffs, and American Home Assurance Company, Brit Syndicates Ltd. (Lloyd's Syndicate 2987) and Heritage Managing Agency Limited (Lloyd's Syndicate 3245), XL Insurance Company Limited, Liberty Mutual Insurance Company, Lloyd's Underwriters Syndicates No. 2623, 0623, 0033 and AIG Europe (UK) Limited, Houston Casualty Company, Defendants

[2011] O.J. No. 3031

2011 ONSC 1142

[2011] I.L.R. I-5166

98 C.C.L.I. (4th) 228

2011 CarswellOnt 5875

Docket: CV-08-00365387

Ontario Superior Court of Justice

L.A. Pattillo J.

Heard: February 14-18, 2011.
Judgment: June 30, 2011.

(191 paras.)

Insurance law -- Actions -- By insured against insurer -- Motion by insured for summary judgment on claim against insurers for defence costs and cross-motion by insurers for summary judgment dismissing action allowed in part -- Onex expended $35 million defending action commenced against plaintiffs in US -- Plaintiffs sought reimbursement for defence costs pursuant to directors' and officers' and excess insurance policies -- Claims in US were covered under policies, but excluded by exclusion clause of 2004-2005 D&O policy and because excess insurers agreed to follow form they were also excluded under excess policies -- Claims not excluded under 2002-2003 D&O policy and consequently insurer required to indemnify individual plaintiffs.

Insurance law -- Liability insurance -- Directors' and officers' insurance -- Exclusions -- Motion by insured for summary judgment on claim against insurers for defence costs and cross-motion by insurers for summary judgment dismissing action allowed in part -- Onex expended $35 million defending action

commenced against plaintiffs in US -- Plaintiffs sought reimbursement for defence costs pursuant to directors' and officers' and excess insurance policies -- Claims in US were covered under policies, but excluded by exclusion clause of 2004-2005 D&O policy and because excess insurers agreed to follow form they were also excluded under excess policies -- Claims not excluded under 2002-2003 D&O policy and consequently insurer required to indemnify individual plaintiffs.

Motion by an insured for summary judgment of its claim against the insurers for the payment of defence costs and cross-motion by the insurers for dismissal of the claim in its entirety. The defendant, American Home, issued a number of annual directors' and officers' ("D&O") insurance policies to Onex. In addition, the remaining defendant insurers issued excess, follow-form D&O policies of insurance to Onex in respect of the American Home D&O policy. In 2005, an action was commenced in the US against the plaintiffs, an Ontario corporation and its officers/ directors, seeking damages in excess of $600,000,000. American Home denied coverage of the US action under the D&O policy on the basis that the claims in the action were outside the scope of coverage, the claim was excluded because the allegations against the individual plaintiffs did not relate to their capacities as directors and officers and that the allegations involved intentional acts that were outside of the scope of the policy. However, American Home provided coverage of $15 million pursuant to a run-off policy, which was the limit of its liability pursuant to that policy. To date, Onex Corp. had expended approximately $35 million USD in the joint defence of that US action. The plaintiffs commenced this action for reimbursement for their defence costs in the US action pursuant to the D&O insurance policies and excess D&O insurance policies issued by the defendant insurers to Onex. The plaintiff sought summary judgment in the action requiring the insurers to pay defence costs that they had incurred defending the US action pursuant to the terms of the D&O and excess insurance policies. In response, the insurers sought summary judgment dismissing the action in its entirety. The US action had since been settled for US $9.25 million. As a result of the settlement of the US action, the plaintiff's claim in respect of liability and defence costs did not impact certain layers of the excess D&O policies with the result that the parties agreed to the dismissal of the action against two of the excess insurers.

HELD: Motion and cross-motion allowed in part. As the insurance policies in issue were clear and unambiguous, all of the issues between the parties raised on the motion and cross-motion could be determined by way of summary judgment. The claims asserted against the individual plaintiffs in the US action were covered under the D&O policies as the allegations in that action constituted a claim against an insured person for a wrongful act as defined in the insurance policies. However, the claims were excluded by one of the exclusion clauses of the 2004-2005 American Home D&O policy and because the excess insurers agreed to follow the form of the American Home D&O policy, they were also excluded under excess policies. The claims were not, however, excluded from coverage under the 2002-2003 American Home D&O policy and, consequently, American Home was required to indemnify the individual plaintiffs for their defence costs in respect of the US action pursuant to the 2002-2003 D&O policy.

Statutes, Regulations and Rules Cited:

Rules of Civil Procedure, Rule 20, Rule 20.04

Counsel:

Geoffrey D.E. Adair, Q.C. and Alexa Sulzenko, for the Plaintiffs.

Marcus B. Snowden and Fabia Wong, for the Defendant American Home Assurance Company.

Allan L.W. D'Silva, Ellen M. Snow and Paloma Ellard, for the Defendants Brit Syndicates Ltd. (Lloyd's

Syndicate 2987) and Heritage Managing Agency Limited (Lloyd's Syndicate 3245), XL Insurance Company Limited, Liberty Mutual Insurance Company and Houston Casualty Company.

L.A. PATTILLO J.:--

Introduction

1 On May 10, 2005, Richard M. Kipperman, in his capacity as Trustee for the Magnatrax Litigation Trust, commenced an action in the United States District Court for the Northern District of Georgia (the "Kipperman Action") against, amongst others, the Plaintiffs in this action, Onex Corporation ("Onex"), Gerald W. Schwartz ("Schwartz"), Christopher A. Govan ("Govan"), Mark Hilson ("Hilson") and Nigel Wright ("Wright") claiming damages in excess of $600,000,000. The Complaint related to the operations of Magnatrax Corporation ("Magnatrax"), a former subsidiary of Onex, and alleged that the conduct of the defendants resulted in Magnatrax and its subsidiaries becoming "hopelessly insolvent, inadequately capitalized and not able to pay their debts."

2 To date, Onex has expended approximately $35 million USD in the joint defence of the Kipperman Action with Schwartz, Govan, Hilson and Wright.

3 The Plaintiffs commenced this action by statement of claim dated October 10, 2008 claiming reimbursement for their defence costs in the Kipperman Action pursuant to certain directors' and officers' ("D&O") liability insurance policies issued by the defendant American Home Assurance Company ("American Home") and excess D&O insurance policies issued by the remaining Defendants to Onex (the "Action").

4 The Plaintiffs move for summary judgment in the Action requiring American Home to pay defence costs they have incurred defending the Kipperman Action pursuant to the terms of the D&O liability insurance policy issued by American Home to Onex for the period 2004-2005 or alternatively pursuant to a similar policy issued for the 2002-2003 period.

5 The Plaintiffs also seek summary judgment against the Defendants Brit Syndicates Ltd. (Lloyd's Syndicate 2987) and Heritage Managing Agency Limited (Lloyd's Syndicate 3245), XL Insurance Company Limited, Liberty Mutual Insurance Company and Houston Casualty Company (collectively the "Excess Insurers") to pay defence costs pursuant to excess follow-form D&O liability insurance policies issued by the Excess Insurers to Onex in excess of American Home's D&O policy for the period 2004-2005.

6 In response, each of American Home and the Excess Insurers move for summary judgment against the Plaintiffs requesting the Action be dismissed in its entirety.

7 The Plaintiffs' claims against the remaining Defendants, Lloyd's Underwriters Syndicates No. 2623, 0623, 0033 and AIG Europe (UK) Limited, also excess insurers for the 2004-2005 D&O policy, were settled prior to the argument of the motions and the Action has been dismissed against them, on consent.

8 On April 6, 2011, I received a letter from counsel for the Excess Insurers indicating that they had been advised by counsel for the Plaintiffs that the Kipperman Action has been settled for US $9.25 million. A Stipulation of Dismissal was filed with the US District Court for the Northern District of Georgia on March 24, 2011. The letter requested that I postpone releasing my decision pending discussions between the parties

9 Following that notice, I have now been advised by the parties that as a result of the settlement of the Kipperman Action, the total amount of the Plaintiffs' claim in the Action in respect of both liability and defence costs will not impact the third and fifth excess layers of D&O coverage insured by excess D&O policies issued by the Defendants Liberty Mutual Insurance Company and Houston Casualty Company respectively for the 2004-2005 period. As a result, the parties have agreed that the Action should be dismissed against Liberty Mutual Insurance Company and Houston Casualty Company on consent with the issue of costs to be dealt with following my decision on the motions.

The Facts

10 The following are the material facts concerning the issues raised by the motions as found by me based upon the voluminous material submitted by the parties. I do not believe that any of the facts as I have found them are in dispute between the parties. The disputes concerning facts centre around the subjective statements of the parties and their agents about the events in issue, which I will have more to say about later.

Background

(i) The Parties

11 Onex is an Ontario corporation in the business of private equity investment and asset management. Onex, by itself and with partners, regularly acquires operating businesses with a view to creating value and subsequently either retaining them or disposing of them. Onex's directors and officers often serve in a duel capacity of officer and director of its subsidiaries while they remain officers and directors of Onex.

12 At all material times, Schwartz, Govan, Hilson and Wright were directors and/or officers of Onex. Hilson and Wright were also directors and officers of Magnatrax.

13 American Home (now known as Chartis Insurance Company of Canada) is an insurance company who was, at all material times, a member of the American International Group. As more particularly described herein, American Home issued a number of annual D&O liability insurance policies to Onex and one D&O policy to Magnatrax during the period 2002 - 2005.

14 The Excess Insurers are insurers who issued excess, follow-form D&O policies of insurance to Onex in respect of the American Home D&O policy for the 2004-2005 period, as more particularly described herein.

(ii) Non-Parties

15 Magnatrax was incorporated in April 1999 in Delaware by Onex. During the period from May 1999 to March 2000, Magnatrax and/or its subsidiaries purchased several American and Canadian manufacturing companies which were in the business of manufacturing and selling pre-engineered metal building and other diversified construction products and services for commercial, non-residential applications and limited residential applications. Magnatrax remained a subsidiary of Onex from the date of its incorporation until November, 2003.

16 Aon Reed Stenhouse Inc. ("Aon") is an insurance broker who at all material times acted on behalf of Onex and Magnatrax as their agent and broker of record in respect of the insurance policies at issue in the Action. Aon is not a party to the Action.

(iii) The Onex 2002-2003 D&O Policy

17 Onex, like most public companies, regularly purchased D&O liability insurance to protect both its own directors and officers and also the directors and officers of its subsidiaries from claims arising from their actions while acting in their capacity as directors and officers.

18 Effective November 29, 2002, American Home issued to Onex, its subsidiaries and other named Onex entities, Executive and Organization Liability Insurance Policy number 240 22 88 for the period of November 29, 2002 to November 29, 2003 (the "2002-2003 D&O Policy"). The 2002-2003 D&O Policy covered officers and directors of Onex and its subsidiaries in respect of liability for claims first made against them and reported during the policy period and had an aggregate limit of liability for all loss, including defence costs, of US $15 million.

19 In addition to the 2002-2003 D&O Policy from American Home, Onex also obtained three excess follow-form policies from three different insurers each with a limit of US $15 million, giving it D&O liability coverage for the period from November 29, 2002 to November 29, 2003 in the total amount of US $60 million.

20 The 2002-2003 D&O Policy provided that, generally, coverage applied to claims which were both made against the Insured and reported to American Home during the Policy period. The 2002-2003 D&O Policy contained the following Notice in capital letters at the beginning of the Policy:

> NOTICE: COVERAGES A, B AND C ARE CLAIMS MADE. THE COVERAGE OF THIS POLICY IS GENERALLY LIMITED TO LIABILITY FOR CLAIMS THAT ARE FIRST MADE AGAINST THE INSUREDS AND CRISIS FIRST OCCURRING DURING THE POLICY PERIOD AND REPORTED IN WRITING TO THE INSURED PURSUANT TO THE TERMS HEREIN.

21 The 2002-2003 D&O Policy provided for three different types of coverage. The Executive Liability portion, referred to as Coverage A, provided as follows:

> INSURING AGREEMENTS
>
> With respect to Coverage A, B and C, solely with respect to Claims first made against an Insured during the Policy Period or the Discovery Period (if applicable) and reported to the Insurer pursuant to the terms of this policy, and subject to the other terms, conditions and limitations of this policy, this policy affords the following coverage:
>
> Coverage A: Executive Liability Insurance
>
> This policy shall pay the Loss of any Insured Person arising from a Claim (including, but not limited to, an Employment Practices Claim, an Oppressive Conduct Claim, a Canadian Pollution Claim and a Statutory Claim) made against such Insured Person for any Wrongful Act of such Insured Person, except when and to the extent that an Organization has indemnified such Insured Person. Coverage A shall not apply to Loss arising from a Claim made against an Outside Entity Executive.

22 The capitalized words in the above paragraphs are all defined terms contained in clause 2 of the 2002-2003 D&O Policy.

(iv) The Magnatrax Run-Off Policy

23 In early January 2003, Onex was considering a sale of Magnatrax to a third party. It advised Aon and asked it to explore the possibility of obtaining a run-off D&O liability policy for Magnatrax.

24 As noted, the 2002-2003 D&O Policy covered directors and officers of both Onex and its subsidiaries which included Magnatrax. If Magnatrax ceased to be a subsidiary of Onex, however, it and its directors and officers would no longer be covered under the 2002-2003 D&O Policy. Accordingly, in order to protect Magnatrax's directors and officers from "Claims" arising from alleged "Wrongful Acts" said to have been committed by them prior to the date Magnatrax ceased to be a subsidiary of Onex but made against them after that date, it would be necessary for Magnatrax to obtain separate coverage for its directors and officers for a term of several years until such claims could no longer be brought. Such a policy is referred to as a "run-off" policy.

25 In response to Onex's request, Aon approached American Home for a quote for a run-off D&O liability policy for Magnatrax's directors and officers.

26 On January 10, 2003, American Home provided Aon with a quote for an Executive and Organization Liability Insurance Policy for Magnatrax with a limit of US $15 million for a six year run-off period. The quotation provided on page 2 thereof for a number of endorsements, including #13 - Non-Pyramiding of Limits; and #14 - Absolute Onex Corporation Exclusion - Carve-out for co-defendant with Onex Corporation. Underneath the listed Exclusions, the following appeared: "NOTE: Endorsements to be added to Onex Corporation Policy 1. Absolute Exclusion from Magnatrax Corporation; 2. Non-Pyramiding of Limits".

27 Aon had a number of concerns with American Home's quote. In particular, it was concerned that the proposed Magnatrax run-off policy would only include coverage for Onex's directors or officers in circumstances where they were named as co-defendants in a claim along with any Magnatrax directors and officers.

28 Before Aon could resolve its concerns with American Home arising from the quote, Aon was advised by Onex sometime in late January 2003 that the proposed sale of Magnatrax was off. As a result, discussions between Aon and American Home concerning a Magnatrax run-off D&O liability policy ceased.

29 Approximately five months later, on the evening of Sunday May 11, 2003, Charles Fogden, the account manager at Aon responsible for Onex, received a telephone call at his home from Hilson and other members of the Magnatrax Board of Directors advising him that Magnatrax intended to file for bankruptcy protection in the United States. Fogden was asked, on behalf of the Magnatrax Board, to arrange a primary run-off D&O policy for Magnatrax with American Home with a US $15 million limit effective on or about May 12, 2003 in the form arranged when considering the sale earlier in January, 2003.

30 On May 12, 2003, Fogden arranged for Aon to contact American Home as a result of which American Home issued a temporary and conditional binder of coverage for Executive and Organization Liability Policy number 350 35 03 for Magnatrax for the period from May 12, 2003 to May 12, 2009 with a limit of US $15 million (the "Magnatrax Run-Off Policy"). On page two of American Home's binder, 13 Endorsements were listed. In particular, Endorsements #12 and #13 were: "12. Non-pyramiding of Limits (To Be Manuscripted) and 13. Absolute Onex Corporation Exclusion - Carve-put [sic] for co-defendant with Onex Corporation (To Be Manuscripted)".

31 Underneath the Endorsements, the following wording appeared:

NOTE: Endorsements to be added to Onex Corporation Policy

1. Non-pyramiding of Limits (To Be Manuscripted)
2. Absolute Exclusion from Magnatrax Corporation (To Be Manuscripted)

32 The words "To Be Manuscripted" meant that the wording of the endorsement to be added to the policy was to be drafted.

33 At some point after inception of the Magnatrax Run-Off Policy, American Home provided the Policy wording to Magnatrax comprised of both the general policy wording and the specific endorsements. The general wording of the Magnatrax Run-Off Policy is identical to the wording in the 2002-2003 D&O Policy save and except for the fact that Magnatrax is the Named Entity. While some of the Endorsements are also the same, some are different. In that regard, the Endorsements noted as #12 and #13 in the temporary and conditional binder of coverage dated May 12, 2003, appear as Endorsements #16 and #14 respectively in the Magnatrax Run-Off Policy.

34 Endorsement #16 deals with co-ordinating the limits of liability between the Magnatrax Run-Off Policy and the 2002-2003 D&O Policy in the event of a Claim. It provides as follows:

> In consideration of the premium charged, it is hereby understood and agreed that, with respect to any Claim under this policy for which coverage is provided by one or more other policies issued by the Insurer or any other member of the American International Group (AIG), (or would be provided but for the exhaustion of the limit of liability, the applicability of the retention/deductible amount or coinsurance amount, or the failure of the Insured to submit a notice of a Claim), the Limit of Liability provided by virtue of this policy shall be reduced by the limit of liability provided by said other AIG policy.
>
> Notwithstanding the above, in the event such other AIG policy contains a provision which is similar in intent to the foregoing paragraph, then the foregoing paragraph will not apply, but instead:
>
> 1) the Insurer shall not be liable under this policy for a greater proportion of the Loss than the applicable Limit of Liability under this policy bears to the total limit of liability of all such policies, and
> 2) the maximum amount payable under all such policies shall not exceed the limit of liability of the policy that has the highest available limit of liability.
>
> Nothing contained in this endorsement shall be construed to increase the limit of liability of this policy.

35 Endorsement #4 of the Magnatrax Run-Off Policy deals with the exclusion of Onex but provides a carve-out for Onex directors and officers in certain circumstances. It provides as follows:

> In consideration of the premium charged, it is hereby understood and agreed that the term "Organization" is amended to include the following entity, subject to the terms, conditions and limitations of this policy.
>
> ENTITY

Onex Corporation

Coverage as is afforded under this policy with respect to a Claim made against Onex Corporation or any Insured Persons thereof shall only apply if: (1) such Claim relates to a Wrongful Act committed by an Insured (other than Onex Corporation or an Insured Person thereof); and (2) an Insured (other than Onex Corporation or an Insured Person thereof) is and remains a defendant in the Claim along with Onex Corporation or any Insured Person thereof.

In all events coverage as is afforded under this policy with respect to a Claim made against Onex Corporation or any Insured Person thereof shall only apply to Wrongful Acts committed or allegedly committed prior to May 12, 2003.

36 In conjunction with the Magnatrax Run-Off Policy and as provided in the temporary and conditional binder of coverage dated May 12, 2003, American Home issued Endorsement #14 to the 2002-2003 D&O Policy effective May 12, 2003. Endorsement #14, entitled "Specific Entity/Subsidiary Exclusion", provides as follows:

> In consideration of the premium charged, it is hereby understood and agreed that the Insurer shall not be liable for Loss alleging, arising out of, based upon or attributable to or in connection with any Claim brought by or made against the Entity listed below and/or any Insureds thereof.
>
> 1. MAGNATRAX Corporation (including any subsidiary or affiliate thereof)
>
> It is further understood and agreed that the Definition of Subsidiary shall not include MAGNATRAX Corporation. Further, the Insurer shall not be liable to make any payment for Loss in connection with any Claim made against an insured alleging, arising out of, based upon or attributable to any breach of duty, act, error or omission of MAGNATRAX Corporation, or any director, officer, member of the board of managers or employee thereof.

37 Notwithstanding the temporary and conditional binder of coverage for the Magnatrax Run-Off Policy provided that an endorsement would be added to the 2002-2003 D&O Policy in respect of the non-pyramiding of limits, no such endorsement was ever added.

38 No excess insurance beyond the U.S. $15 million limit provided by the Magnatrax Run-Off Policy was ever sought or obtained.

(v) Magnatrax's Bankruptcy Proceedings

39 On May 12, 2003, the same day that American Home agreed to bind the Magnatrax Run-Off Policy, Magnatrax, together with 16 of its direct and indirect subsidiaries each filed a voluntary petition for reorganization under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware.

40 On May 22, 2003, the Office of the United States Trustee formed an official committee of unsecured creditors (the "Creditors' Committee") who in turn selected the law firm of Foley & Lardner ("Foley") to act as its counsel. Pursuant to powers under the Bankruptcy Code, the Creditors' Committee

carried out a detailed investigation of various matters relating to the activities of Magnatrax and its subsidiaries including certain acquisition transactions and their financing.

41 On August 19, 2003, the Creditors' Committee reached an agreement with, among others, Magnatrax and its subsidiaries on a Plan of Reorganization dated September 17, 2003 (the "Magnatrax Plan of Reorganization") which was subsequently confirmed by the U.S. Bankruptcy Court on November 17, 2003. As a result of the U.S. Bankruptcy Court approval of the Magnatrax Plan of Reorganization, Onex ceased to have any ownership interest in Magnatrax at that time.

42 On January 20, 2004, Magnatrax emerged from Chapter 11 protection.

(vi) The Foley Letter

43 By letter dated August 1, 2003, Foley wrote to counsel for Magnatrax on behalf of the Creditors' Committee (the "Foley Letter"), stating that it believed Magnatrax and its subsidiaries had various causes of action against, among others, Onex, its affiliates and officers and directors. The Foley Letter states, in part:

> ... the [Creditors'] Committee believes that [Magnatrax and its subsidiaries] have various claims against parties involved in the May 1999, September 1999, and March 2000 transactions, as well as the credit facilities and related agreements supporting those transactions. More specifically, the [Creditors'] Committee asserts that numerous claims finding their genesis in fraudulent transfers, breach of fiduciary duty, aiding and abetting both breach of fiduciary duty and fraudulent transfers, equitable subordination, unjust enrichment, declaratory relief, preference actions, and possibly other claims yet to be identified, should all be pursued.

44 The Foley Letter goes on to list a number of entities and individuals against whom some or all of the claims should be pursued, and specifically refers to Onex and its officers and directors.

45 The Foley Letter concludes by requesting Magnatrax's "immediate confirmation" that Magnatrax and its subsidiaries will prosecute the listed claims against all of the individuals and entities noted and if they did not intend to do so, to provide immediate confirmation so that the Creditors Committee could then do so on their behalf.

46 On August 7, 2003, Magnatrax's counsel forwarded the Foley Letter to Mr. Fogden at Aon by email inquiring as to what notice should be sent to insurers on behalf of Magnatrax and its officers and directors. Mr. Fogden replied by email on August 8, 2003 that they would put American Home on notice.

47 On November 28, 2003, the day before the 2002-2003 D&O Policy expired, Aon faxed the Foley Letter to American Home. The fax covering page references the Magnatrax Run-Off Policy in the reference line at the outset and states:

> Enclosed is a letter of August 1, 2003 from Foley & Lardner, Attorneys at Law, which contains information on a situation which could in future give rise to a claim under the above mentioned policy.
>
> Under separate cover we are also reporting this issue under a Directors & Officers policy for Onex Corporation which is also written through your office.

48 Also on November 28, 2003, Aon sent a similar fax to American Home in respect of the 2002-

2003 D&O Policy.

49 American Home subsequently acknowledged receipt of the Aon claims letters and advised that it was setting up claim files for both the 2002-2003 D&O Policy and the Magnatrax Run-Off Policy to enable a "full assessment of coverage" to be made. American Home reserved its rights, privileges and defences under the Policies.

50 Having heard nothing further about the claim for more than a year from the initial notice, American Home wrote to Aon in December 2004, asking if there still existed a threat of a "Claim" and indicating that in the absence of further developments, American Home intended to close its files in 60 days. American Home once again reserved all rights under both the 2002-2003 D&O Policy and the Magnatrax Run-Off Policy. In the absence of any further information from either Magnatrax or Onex concerning the information in the Foley Letter, American Home closed its claim files on March 16, 2005.

(vii) The Onex 2003-2004 D&O Policy

51 In the fall of 2003, American Home renewed the 2002-2003 D&O Policy by issuing Executive and Organization Liability Insurance Policy No. 378 16 65 to Onex with primary limits of US $15 million for the period from November 29, 2003 to November 29, 2004 (the "2003-2004 D&O Policy").

52 The 2003-2004 D&O Policy was very similar to the wording of the 2002-2003 D&O Policy. The general policy wording was identical. The wording of the endorsements was for the most part similar although there were some differences. In particular, Endorsement 13 provided a Specific Entity Exclusion for claims involving Magnatrax which had the identical wording of the Specific Entity Exclusion found in the 2002-2003 D&O Policy at Endorsement 14.

53 In addition to the 2003-2004 D&O Policy, Onex again obtained excess directors and officers insurance for the same period.

(viii) The Onex 2004-2005 D&O Policy

54 In the fall of 2004, Aon, on behalf of Onex, once again solicited renewals for Onex's D&O liability insurance program for the 2004 - 2005 period.

55 On November 11, 2004, American Home provided Aon with a quote to renew the 2003-2004 Onex Policy on the basis of an aggregate limit of liability of US $15 million for the period from November 29, 2004 to November 29, 2005 (the "Quote"). The Quote identified a number of endorsements that would be included in the Onex D&O Policy once issued. Amongst the endorsements listed was a Specific Entity Exclusion for Magnatrax.

56 On November 25, 2004, American Home issued its temporary and conditional binder of insurance coverage for D&O liability policy 358 12 14 for the period from November 29, 2004 to November 29, 2005 on the basis of an aggregate limit of liability of US $15 million (the "2004-2005 D&O Policy") as had been previously set out in the Quote (the "Binder"). The Binder provided a list of twenty endorsements which would be included in the Policy, including Endorsement #13, a Specific Entity Exclusion for Magnatrax.

57 In order to obtain excess D&O liability insurance for Onex over and above the limits of the 2004-2005 D&O Policy from American Home, Aon provided the Excess Insurers with a Directors' and Officers' Liability Insurance renewal application form containing information about Onex's company background and its performance over the last policy period, along with the Quote and the Binder.

58 Based on this information, each of the Excess Insurers agreed to provide "follow form" coverage to the 2004-2005 D&O Policy, thereby incorporating into each excess layer the terms and conditions set out in the 2004-2005 D&O Policy. The excess insurance over and above the US $15 million provided by the 2004-2005 D&O Policy totalled US$75 million.

59 In particular, the Excess Insurers provided the following coverage:

(a) The First Excess Insurer, Brit Syndicates Ltd. (Lloyd's Syndicate 2987) and Heritage Managing Agency Limited (Lloyd's Syndicated 3245), provided its binder for the First Excess Layer on November 29, 2004 offering coverage on the basis of limits of liability of US$20 million in excess of $15 million provided to Onex by American Home pursuant to the 2004-2005 D&O Policy;

(b) The Second Excess Insurer, XL Company Limited, provided its binder for the Second Excess Layer on November 29, 2004 offering coverage on the basis of limits of liability of US$20 million in excess of the US $35 million provided to Onex by American Home and the Excess Insurers pursuant to the 2004-2005 D&O Policy;

(c) The Third Excess Insurer, Liberty Mutual Insurance Company, provided its binder on the Third Excess Layer on December 7, 2004 on the basis of liability of US$20 million in excess of the US$55 million provided to Onex by American Home and the Excess Insurers pursuant to the 2004-2005 D&O Policy; and

(d) The Fifth Excess Insurer, Houston Casualty Company, provided its binder on the Fifth Excess Layer on December 1, 2004 offering on the basis of limits of liability of US$5 million in excess of the US $85 million provided to Onex by American Home and the Excess Insurers pursuant to the 2004-2005 D&O Policy.

(Collectively the "Excess Policies")

60 The policy wording for the 2004-2005 D&O Policy was not sent to Aon for its review until May 10, 2005. Following its receipt, discussions took place between Aon and American Home concerning the wording of some of the endorsements. In particular, Aon took the position that proposed Endorsement #13, which was the Specific Entity/Subsidiary Exclusion in respect of Magnatrax which had been present as Endorsement #14 in the 2002-2003 D&O Policy and Endorsement #13 in the 2003-2004 D&O Policy should be changed to a Prior Acts Exclusion to provide coverage for Magnatrax officers and directors for the period May 12, 2003 to January 20, 2004, which was the time Magnatrax and its subsidiaries were in Chapter 11. American Home agreed and on July 5, 2005, it sent Aon Endorsement #23 entitled Prior Acts Exclusion For Listed Entities which became part of the 2004-2005 D&O Policy.

61 Endorsement #23 of the 2004-2005 D&O Policy provides:

> In consideration of the premium charged, it is hereby understood and agreed that the term Subsidiary is amended to include the entity(ies) listed below, but only for Wrongful Acts committed by such entity(ies) and/or any Insureds thereof which occurred subsequent to such entity's respective acquisition/creation date listed below and prior to the time the Named Entity no longer maintains Management Control of such entity(ies), respectively, either directly or indirectly through one or more other Subsidiaries. Loss arising from the same or related Wrongful Act shall be deemed to arise from the first such same or related Wrongful Act.
>
> ENTITY(IES) ACQUISITION/CREATION DATE

1. MAGNATRAX Corporation [...] May 12, 2003

For the purpose of the applicability of the coverage provided by this endorsement, the entities listed above and the Organization will be conclusively deemed to have indemnified the Insureds of [...] each respective entity to the extent that such entity or the Organization is permitted or required to indemnify such Insureds pursuant to law or contract or the charter, bylaws, operating agreement or similar documents of an Organization. The entity and the Organization hereby agree to indemnify the Insureds to the fullest extent permitted by law, including the making in good faith of any required application for court approval.

62 The policy wording for the 2004-2005 D&O Policy was provided by Aon to the Excess Insurers for the first time on July 13, 2005. The Excess Insurers did not agree to the wording changes agreed to between Aon and American Home subsequent to providing their binders of coverage. In particular, they did not agree to Endorsement #23.

(ix) The Kipperman Action

63 Section 4.21 of the Magnatrax Plan of Reorganization provides, among other things, for the establishment of a Litigation Trust and the transfer and assignment by Magnatrax and its subsidiaries of all right, title or interest of Magnatrax and its subsidiaries in and to the "Assigned Causes of Action" to the Litigation Trust. Section 1.20 defines "Assigned Causes of Action" to mean all right, title and interest of Magnatrax and its subsidiaries "to pursue, litigate, settle or otherwise resolve any Cause of Action against Onex Corporation or any Onex Affiliate". Section 1.110 defines "Onex Affiliate" to include a number of Onex's related companies and any person who possesses the power, directly or indirectly, to direct or cause the direction of the management and policies of Onex or its related companies.

64 As noted at the outset, the Kipperman Action was commenced on May 10, 2005 by Kipperman in his capcity as Trustee of the Magnatrax Litigation Trust.

65 The Complaint in the Kipperman Action is 70 pages in length and asserts 19 causes of action against Onex and certain of its subsidiaries and affiliates and Schwartz, Govan, Wright and Hilson. Also named are Robert C. Blackmon Jr. and Robert T. Ammerman who were directors and officers of Magnatrax.

66 The Complaint alleges that defendants in the Kipperman Action, including the individual Plaintiffs:

(a) incorporated Magnatrax as a vehicle for highly leveraged acquisitions of several American and Canadian manufacturing companies, which occurred from May 1999 to March 2000;
(b) along with affiliates, seized control of Magnatrax and its subsidiaries by a self-dealing management agreement, placing Onex personnel on boards of and in key management positions with Magnatrax entities;
(c) used that control to obtain millions of dollars for themselves while imposing significant debt on Magnatrax entities, forcing Magnatrax into bankruptcy in May 2003 from which it emerged in late 2003, leaving hundreds of millions in pre-bankruptcy unpaid debt discharged;
(d) through the co-defendants' conduct, left the Magnatrax entities insolvent,

inadequately capitalized and unable to pay debts while millions of dollars were diverted to the defendants.

67 Of the 19 claims asserted in the Kipperman Action, four are asserted against the individual Plaintiffs: i) breach of fiduciary duty (Count X); ii) aiding and abetting breach of fiduciary duty (Count XI); iii) civil conspiracy (Count XII); and unjust enrichment (Count XIX). Swartz, Govan, Hilson are included in the term "Management Defendants" in the Complaint.

68 Paragraph 107 of the Complaint pleads that Onex was the *de facto* board and alter ego of Magnatrax and its subsidiaries and "Swartz and Govan were *de facto* members of the boards of Magnatrax and each of them owed the acquired companies and their creditors' fiduciary duties of care and loyalty which they breached."

69 Count X which deals with breach of fiduciary duty alleges, in part, that Swartz and Govan "directed and controlled all of Onex's conduct under the Management Agreement and other conduct by which Onex controlled the Magnatrax entities" therefore assuming the role of *de facto* board members of all Magnatrax entities (para. 198). Paragraph 200 pleads that while acting at the behest of and beholden to Onex, the Management Defendants breached their fiduciary duties to Magnatrax and its subsidiaries. A number of examples are pleaded. Paragraphs 212 to 214 plead that Hilson, Wright, Govan and Schwartz had conflicts of interest while acting as a director/officer of Onex and a director/officer of Magnatrax or a *de facto* director.

70 Count XI deals with the claim of aiding and abetting breach of fiduciary duty. Paragraph 218 pleads that Schwartz knowingly induced, participated and substantially assisted in the breaches of fiduciary duty by Govan, Hilson, Wright and others. The same allegation is pleaded against Govan, Hilson and Wright in paragraphs 219 to 221 of the Complaint.

71 Count XII which deals with the allegation of civil conspiracy is somewhat sparse. It alleges that all defendants wilfully conspired to embark on a scheme to divert value from Magnatrax to themselves (para. 226); to fraudulently transfer assets from Magnatrax to the benefit of themselves (para. 227); and to breach fiduciary duties (para. 228).

72 Count XIX alleges unjust enrichment. Paragraph 283 pleads that as a result of complete domination and control and breaches of fiduciary duties, the defendants received a benefit from their management of the Magnatrax entities.

(x) Notice to American Home of the Kipperman Action

73 On July 4, 2005, Aon, on behalf of Onex, sent a copy of the Complaint in the Kipperman Action to American Home and stated that it was notice of a Claim under the 2004-2005 D&O Policy.

74 By letter dated September 15, 2005, American Home denied coverage of the Kipperman Action under the 2004-2005 D&O Policy on the basis that:

(i) the allegations in the Kipperman Action all pre-date May 12, 2003 and are therefore outside the scope of coverage;
(ii) the claim is excluded as the allegations in the Kipperman Action relate to the individual Plaintiffs' actions in respect of Magnatrax and are not claims made against the individual Plaintiffs in their capacities as directors and officers of Onex; and
(iii) the allegations in the Kipperman Action involve intentional acts which are outside the scope of the 2004-2005 D&O Policy.

75 Although American Home also initially denied coverage for the Kipperman Action under the Magnatrax Run-Off Policy, on August 28, 2006, its counsel sent a letter to counsel for the Plaintiffs indicating that, based on further review, American Home determined that the Magnatrax Run-Off Policy did provide coverage to Schwartz, Govan, Hilson and Wright as well as Messrs. Ammerman and Blackmon.

76 American Home subsequently paid US $1,118,008.10 to Messrs. Ammerman and Blackmon and US $13,881,991.90 to the Plaintiffs in respect of defence costs incurred in the Kipperman Action pursuant to the Magnatrax Run-Off Policy. The total amount of US $15 million paid by American Home is the limit of its liability pursuant to the Magnatrax Run-Off Policy.

Positions of the Parties

(a) The Plaintiffs

77 The Plaintiffs submit that Schwartz, Govan, Hilson and Wright, in their capacity as directors and/or officers of Onex are entitled to coverage for the Kipperman Action pursuant to a D&O Policy issued by American Home. In that regard they submit that the Kipperman Action is a "Claim" made and reported during the period of the 2004-2005 D&O Policy and is therefore covered by that Policy. Accordingly, American Home and the Excess Insurers are required to indemnify the individual Plaintiffs' for their "Loss" arising from the Kipperman Action, and in particular defence costs incurred, pursuant to the terms of the 2004-2005 D&O Policy and the Excess Policies.

78 The Plaintiffs take issue with the Defendants' position that the Foley Letter constitutes notice of circumstances in accordance with the terms of the 2002-2003 D&O Policy such that the Kipperman Action constitutes a "Claim" made during the period of that Policy. In the alternative, if the 2002-2003 D&O Policy applies, the Plaintiffs submit that American Home is required to indemnify the individual Plaintiffs' in accordance with the terms and to the limits of liability of that Policy. The Plaintiffs assert no claim against the 2002-2003 D&O Policy's excess insurers nor are they parties to the action.

79 The Plaintiffs further submit that the payment by American Home of the US $15 million pursuant to the provisions of the Magnatrax Run-Off Policy does not impact upon or reduce American Home's liability either under the 2004-2005 D&O Policy or the 2002-2003 D&O Policy.

(b) American Home

80 American Home's position is that coverage for the Kipperman Action is only available under the Magnatrax Run-Off Policy and it has paid the full extent of its liability under that Policy to the Plaintiffs.

81 To the extent that the Kipperman Action constitutes a Claim for a Wrongful Act of an Insured under the terms of either the 2002-2003 D&O Policy or the 2004-2005 D&O Policy, American Home submits that the Foley Letter constitutes sufficient notice of circumstances within the period of the 2002-2003 D&O Policy that it is that Policy which applies to the Kipperman Action. American Home further submits, however, that based on the terms of the 2002-2003 D&O Policy and specifically Endorsement #14, the Specific Entity/Subsidiary Exclusion for Magnatrax, there is no coverage under the 2002-2003 D&O Policy in respect of the Kipperman Action.

82 Finally, American Home submits that there is no coverage for the Kipperman Action pursuant to the 2004-2005 D&O Policy having regard to Exclusion 4(d) which specifically excludes coverage for previously reported claims.

(c) Excess Insurers

83 The Excess Insurers join in American Home's submission that the Kipperman Action is a Claim first made and reported during the 2002-2003 D&O Policy period and therefore the Kipperman Action is a pre-existing claim which is excluded from coverage under the 2004-2005 D&O Policy by Exclusion 4 (d) of the latter Policy.

84 In the alternative, the Excess Insurers submit that if the 2004-2005 D&O Policy applies, coverage by the Excess Insurers under that Policy is excluded in accordance with the terms of Endorsement #13, the Specific Entity/Subsidiary Exclusion in respect of Magnatrax, which the Excess Insurers submit remained a term of the Excess Policies. The Excess Insurers further submit that the allegations in the Kipperman Action do not trigger coverage under the 2004-2005 D&O Policy.

85 Finally, the Excess Insurers submit that in the event that the Court does not accept their arguments that there is no coverage under the 2004-2005 D&O Policy, the Excess Insurers submit the Plaintiffs' summary judgment motion cannot succeed as there remain genuine issues between the parties requiring a trial.

The Issues

86 Given the positions of the parties, the following are the issues that must be determined on these motions:

1. Is summary judgment appropriate for these motions?
2. Are the defence costs incurred by the individual Plaintiffs in the Kipperman Action covered by the terms of the 2002-2003 D&O Policy and the 2004-2005 D&O Policy?
3. If the answer to 2 is yes, which Policy applies in respect of the Kipperman Action, the 2002-2003 D&O Policy or the 2004-2005 D&O Policy?
4. Depending on which Policy applies, do the exclusions or limitations of that Policy exclude coverage of Loss arising from the Kipperman Action?

Principles of Insurance Contract Interpretation

87 The issues raised by the parties require the court to interpret and give reasonable meaning to the provisions of the 2002-2003 D&O Policy, the 2004-2005 D&O Policy and the Magnatrax Run-Off Policy.

88 The principles of insurance contract interpretation have been developed and discussed by Canadian Courts at some length for many years. Most recently, they were summarized by Rothstein J. in *Progressive Homes Ltd. v. Lombard General Insurance Co. of Canada*, [2010] 2 S.C.R. 245 (S.C.C.) at paras. 21-24 as follows:

> 21 Principles of insurance policy interpretation have been canvassed by this Court many times and I do not intend to give a comprehensive review here (see, e.g., *Gibbens v. Co-operators Life Insurance Co.*, 2009 SCC 59, [2009] 3 S.C.R. 605 (S.C.C.), at paras. 20-28; *Jesuit Fathers*, [2006] 1 S.C.R. 744, at paras. 27-30; *Scalera*, at paras. 67-71; *Brissette v. Westbury Life Insurance Co.*, [1992] 3 S.C.R. 87 (S.C.C.), at pp. 92-93; *Consolidated-Bathurst Export Ltd. c. Mutual Boiler & Machinery Insurance Co.* (1979), [1980] 1 S.C.R. 888 (S.C.C.), at pp. 899-902). However, a brief review of the relevant principles may be a useful introduction to the interpretation of the CGL policies that follow.

> 22 The primary interpretive principle is that when the language of the policy is unambiguous, the court should give effect to clear language, reading the contract as a whole (*Scalera*, at para. 71).
>
> 23 Where the language of the insurance policy is ambiguous, the courts rely on general rules of contract construction (*Consolidated-Bathurst*, at pp. 900-902). For example, courts should prefer interpretations that are consistent with the reasonable expectations of the parties (*Gibbens*, at para. 26; *Scalera*, at para. 71; *Consolidated-Bathurst*, at p. 901), so long as such an interpretation can be supported by the text of the policy. Courts should avoid interpretations that would give rise to an unrealistic result or that would not have been in the contemplation of the parties at the time the policy was concluded (*Scalera*, at para. 71; *Consolidated-Bathurst*, at p. 901). Courts should also strive to ensure that similar insurance policies are construed consistently (*Gibbens*, at para. 27). These rules of construction are applied to resolve ambiguity. They do not operate to create ambiguity where there is none in the first place.
>
> 24 When these rules of construction fail to resolve the ambiguity, courts will construe the policy *contra proferentem* -- against the insurer (*Gibbens*, at para. 25; *Scalera*, at para. 70; *Consolidated-Bathurst*, at pp. 899-901). One corollary of the *contra proferentem* rule is that coverage provisions are interpreted broadly, and exclusion clauses narrowly (*Jesuit Fathers*, at para. 28).

89 The application of the above principles to the task of interpreting an insurance contract was summarized by Cronk J.A. in *Lombard Canada Ltd. v. Zurich Insurance Co.* (2010), 101 O.R. (3d) 371 (C.A.) at paras. 32-34 as follows:

> **32** The foundation for the relevant principles and process for the interpretation of an insurance contract is *Consolidated Bathurst Export Ltd. v. Mutual Boiler & Machinery Insurance Co.*, [1980] 1 S.C.R. 888. At pp. 899 - 901 of that case, Estey J., writing for the majority, explains the two phases of the analysis for the interpretation of any contract, including an insurance contract.
>
> **33** The first is the interpretive phase based on the guidelines for construction. Subjective intention is irrelevant at this stage of the process, although the words used may be "possibly read in light of the surrounding circumstances which were prevalent at the time": see *Eli Lilly*, [1998] 2 S.C.R. 129, at para. 54. If the meaning is plain on the face of the contract, it is unnecessary to proceed further: see *Non-Marine Underwriters, Lloyd's of London v. Scalera*, [2000] 1 S.C.R. 551, at para. 71. However, if the interpretive phase results in two equally reasonable interpretations, the contract is ambiguous. In those circumstances, the court turns to the second phase of the inquiry. At this phase, the court may consider extrinsic evidence: see *Eli Lilly*, at para. 55. As well, the court may consider the applicability of *contra proferentem*: see *Consolidated Bathurst*, at p. 901.
>
> **34** In the interpretive phase, the onus is upon the insured to show that the loss is covered by the policy in question. Once the insured has done so, the burden shifts to the insurer to show otherwise, including by reason of the operation of an exclusion or limitation in the insurance contract: see *Continental Insurance Co. v. Dalton Cartage Co.*, [1982] 1 S.C.R. 164; *Canadian National Railway Co. v. Royal and Sun Alliance Insurance Co. of Canada*, [2008] 3 S.C.R. 453, at para. 34; *Co-Operators Life*

Insurance Co. v. Gibbens, [2009] 3 S.C.R. 605, at para. 51; Denis Boivin, *Insurance Law* (Irwin Toronto: Irwin Law, 2004) at p. 190. In interpreting a provision, the court will also recognize that coverage provisions are "construed broadly and exclusion clauses narrowly": see *Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co.*, [1993] 1 S.C.R. 252, at p. 269; *Scalera*, at para. 70.

Claims Made Liability Insurance Policies

90 In *Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co.*, [1993] 1 S.C.R. 252 (S.C.C.), the Supreme Court discussed "claims made" liability insurance policies. The Court points out, at para. 14 of the decision, that when considering a "claims-made" policy, it is important to examine the particular wording of the policy in issue as a whole to determine the nature of the policy and how coverage applies.

Summary Judgment

91 Prior to embarking on the interpretation of the Policies as they relate to the issues between the parties, I want to address at the outset the Excess Insurers submission that, in the event that the court rejects their defences, the Plaintiff's motion for summary judgment cannot succeed because there are genuine issues which require a trial.

92 As noted, the Excess Insurers submit that their motion for summary judgment, which is premised on their defences to the Plaintiffs' claim being successful, should be allowed. In the event, however, that their defences are not accepted by the Court, the Excess Insurers submit that the Plaintiffs' motion for summary judgment cannot succeed because there are genuine issues which require a trial.

93 Rule 20.04 provides that the Court shall grant summary judgment if it is satisfied that there is no genuine issue requiring a trial. While the Rule now specifically permits the motions judge to weigh the evidence presented on the motion, evaluate the credibility of a deponent and draw reasonable inferences from the evidence, it does not eliminate a trial in circumstances where interests of justice require that the issues be resolved, not on the motion record, but rather with viva voce evidence. Depending on the issue to be decided, this may be accomplished either as part of the summary judgment motion itself by ordering oral evidence (Rule 20.04(2.2)) or by requiring a full trial. See: *New Solutions Extrusion Corp. v. Gauthier*, [2010] O.J. No. 661 (S.C.J.); *Canadian Premier Life Insurance Co. v. Sears Canada Inc.*, [2010] O.J. No. 3987 (S.C.J.).

94 I agree with the guiding principles for Rule 20 as set forth by Pepall J. in *Canadian Premier Life Insurance*, supra, at para. 70:

* The court must be satisfied that there is no genuine issue requiring a trial.
* To be satisfied, the court may weigh the evidence, evaluate the credibility of a deponent, draw any reasonable inference from the evidence, and order that oral evidence be presented. By implication, these powers may involve the making of factual findings including a finding of a material fact.
* The motions judge should take a hard look at all of the evidence to determine whether there is a genuine issue requiring a trial.
* The burden of proof to establish that there is no genuine issue requiring a trial is on the moving party.
* The respondent may not rest solely on the allegations or denials in its pleading.
* Each side should put its best foot forward.
* The Rule should be interpreted broadly so as to achieve the objectives of reduction of delay and costs, access to justice, and flexibility. At the same time,

> it must be acknowledged that elimination of trials is not an objective. At its core, justice is the ultimate objective. It is not to be sacrificed in the interests of speed and economy. That said, Rule 20 clearly contemplates that justice, speed and economy are not mutually exclusive attributes.

95 The purpose of summary judgment is to finally dispose of non-complex cases in a summary cost effective manner. That does not mean that summary judgment is restricted or should be restricted to smaller cases. Actions where the motion has an extensive evidentiary record can also be subject to summary judgment. In such circumstances, however, the court must be particularly vigilant in ensuring that the issues can be decided on the record without the safeguards provided by a trial. See: *Canadian Premier Life Insurance*, supra, at para. 71.

96 The record in this case is comprised of nine volumes. In addition to the D&O Policies in issue, it contains 16 affidavits, transcripts of extensive cross-examinations and numerous documents.

97 The facts as I have recited them, although lengthy and somewhat complex, are not, in the final analysis, in dispute between the parties. They serve to set out the factual matrix of the D&O Policies in issue. What is in dispute factually are the various assertions of intention by the various parties. In my view it is not necessary to resolve any of those factual disputes to resolve the motions. As will become apparent from my reasons that follow, such evidence is not admissible given my view that the provisions of the D&O Policies in issue are clear and unambiguous.

98 Accordingly, notwithstanding that the Record in this case is extremely large, I am satisfied that all of the issues between the parties as raised in the Plaintiffs' motion and the Defendants' cross-motions can be determined by way of summary judgment.

Are the defence costs incurred by the individual Plaintiffs in the Kipperman Action covered by the 2002-2003 D&O Policy and the 2004-2005 D&O Policy?

99 As noted in *Lombard Canada v. Zurich Insurance,* supra, at para. 34, the onus is on the Plaintiffs to establish that their defence costs are covered by either the 2004-2005 D&O Policy or the 2002-2003 D&O Policy. In order to determine whether the Plaintiffs have met their onus, it is necessary to consider two questions: first, whether the Claims asserted against the Individual Plaintiffs in the Kipperman Action are covered under the Onex D&O Policies and second, whether the Plaintiffs are entitled to payment of their defence costs in advance of a final determination in the Kipperman Action.

a) Do the allegations in the Kipperman Action constitute a Claim against an Insured Person for a Wrongful Act as those terms are defined in both the 2002-2003 Onex Policy and the 2004-2005 Onex Policy?

100 The basic coverage wording in each of the 2002-2003 D&O Policy, the 2004-2005 D&O Policy and the Magnatrax Run-Off Policy is identical. Coverage A, which is Executive Liability, requires American Home to pay the "Loss" arising from a "Claim" made against an "Insured Person" alleging a "Wrongful Act" by such Insured Person.

101 Clause 2 of the Policies sets out the definitions and defines Claim as follows:

> (c) "Claim" means:
>
> (1) a written demand for monetary, non-monetary or injunctive relief;
> (2) a civil, criminal, administrative, regulatory or arbitration proceeding for monetary, non-monetary or injunctive relief which is commenced by:

(i) service of a Writ of Summons, Statement of Claim or similar originating legal document;
(ii) return of a summons, information, indictment or similar document (in the case of a criminal proceeding); or
(iii) receipt or filing of a notice of charges; or

(3) a civil, criminal, administrative or regulatory investigation of an Insured Person:

(i) once such Insured Person is identified in writing by such investigating authority as a person against whom a proceeding described in Definition (c) (2) may be commenced; or
(ii) in the case of an investigation by any PSC or similar foreign securities authority, after the service of a subpoena upon such Insured Person.

The term "Claim" shall include any Securities Claim, Employment Practices Claim, Oppressive Conduct Claim, Canadian Pollution Claim and Statutory Claim.

102 It is clear in my view that the Kipperman Action constitutes a "Claim" as that term is defined in the Policies. It is a civil proceeding commenced by Complaint which is an originating legal document in the United States District Court as provided in clause 2(c)(2) of the above definition.

103 Clause 2 of the Policies further provides:

(q) "Insured Person" means any:

(1) Executive of an Organization;
(2) Employee of an Organization; or
(3) Outside Entity Executive.

(l) "Executive" means any:

(1) past, present and future duly elected or appointed director, officer, trustee or governor of a corporation, management committee member of a joint venture and member of the management board of a limited liability company (or equivalent position), including a de facto director, officer, trustee, governor, management committee member or member of the management board of such entities;

(w) "Organization" means:

(1) the Named Entity;
(2) each Subsidiary; and
(3) in the event of a bankruptcy proceeding shall be instituted by or against the foregoing entities in the United States the resulting debtor-in-possession (or equivalent status outside the United States), if any.

104 As Onex is a Named Entity in both the 2002-2003 D&O Policy and the 2004-2005 D&O Policy, it is an "Organization" as defined in clause 2(w)(1) of those Policies and Schwartz, Govan, Hilson and

Wright, as directors and/or officers of Onex, are each "Insured Persons" as defined by clause 2(q)(1) of those Policies.

105 Further, based on a review of the entire Complaint in the Kipperman Action and in particular the allegations against Schwartz, Govan, Hilson and Wright, it is my view that the claims against the individual Plaintiffs are asserted against them in their capacity both as directors and officers of Onex and as directors (or de facto directors in the case of Schwartz and Govan) and officers of Magnatrax. The overarching theme of the Complaint is that Onex, as directed by the individual Plaintiffs in their capacity as Onex directors and officers, engineered the demise of Magnatrax and its subsidiaries for their collective benefit. In that regard, the claims of aiding and abetting breach of fiduciary duty, civil conspiracy and unjust enrichment particularly relate to activities of Schwartz, Govan, Hilson and Wright in their capacity as directors and officers of Onex.

106 "Wrongful Act" is defined in clause 2(ee) as follows:

> (ee) "Wrongful Act" means:
>
> (1) any actual or alleged breach of duty, neglect, error, misstatement, misleading statement, omission or act or any actual or alleged Employment Practices Violation:
>
> (i) with respect to any Executive of an Organization, by such Executive in his or her capacity as such or any matter claimed against such Executive solely by reason of his or her status as such;
> (ii) with respect to any Executive of an Organization, by such Employee in his or her capacity as such, but solely in regard to any: (a) Securities Claim; or (b) other Claim so long as such other Claim is also made and continuously maintained against an Executive of an Organization; or
> (iii) with respect to any Outside Entity Executive, by such Outside Entity Executive solely by reason of his or her status as such;

107 In my view, the claims asserted in the Kipperman Action against Schwartz, Govan, Hilson and Wright acting in their capacity as directors and/or officers of Onex, constitute a "Wrongful Act" as defined in clause 2(ee) of the Policies. The claims involve alleged acts by the individual Plaintiffs in their capacity as directors and officers of Onex.

108 The Excess Insurers submit that the claims in the Kipperman Action involve intentional acts which are outside the scope of coverage of the Policies. As noted, "Wrongful Act" includes "any actual or alleged breach of duty, neglect, error, misstatement, misleading statement, omission or act...." A "Claim" includes a criminal proceeding or investigation, any Securities Claim, Employment Practice Claim, and Oppressive Conduct Claim. While the provisions of the Policies exclude certain specific acts such as deliberate criminal or fraudulent acts, it is clear in my view from the definition of "Wrongful Acts" in the Policies that, subject to the listed exclusions which are not applicable in respect of the claims asserted here, the Policies provide coverage in respect of intentional acts.

109 In its counsel's letter of August 28, 2006 agreeing that the claims against Schwartz, Govan, Hilson and Wright in the Kipperman Action were covered under the Magnatrax Run-Off Policy, American Home conceded that such claims would be afforded coverage as Insured Persons of Onex by virtue of Endorsement #4 to the Magnatrax Run-Off Policy so long as an Insured other than Onex or an

Insured Person thereof remains a defendant in the Kipperman Action. Implicit in this concession, in my view, is that the claims alleged in the Kipperman Action constitute a "Wrongful Act" within the meaning of the Policy. As noted, the material wording in respect of coverage in the Magnatrax Run-Off Policy is identical to the wording in each of the 2002-2003 D&O Policy and the 2004-2005 D&O Policy.

110 Accordingly, I am of the view that the Plaintiffs have met their onus. Based on the plain wording of the Policies, the claims asserted against Schwartz, Govan, Hilson and Wright in the Kipperman Action are Claims made against Insured Persons for Wrongful Acts as those terms are defined in the Policies and therefore fall within Coverage A, the basic coverage section of each of the Policies.

b) Are the Plaintiffs are entitled to payment of their defence costs in advance of a final determination in the Kipperman Action?

111 Both the 2002-2003 D&O Policy and the 2004-2005 D&O Policy define "Loss" in clause 2(r) to include Defence Costs which is further defined to mean reasonable and necessary fees, costs and expenses consented to by the Insurer resulting solely from the investigation, adjustment, defence and/or appeal of a Claim against an Insured.

112 Clause 2(r) of the Policies defines "Loss" as follows:

(r) "Loss" means damages (including aggravated damages), settlements, judgments (including pre/post-judgment interest on a covered judgment), Defence Costs and Crisis Loss; however, "Loss" (other than Defence Costs) shall not include: (1) civil or criminal fines or penalties; (2) taxes; (3) punitive or exemplary damages; (4) multiplied portion of multiplied damages; (5) any amounts for which an Insured is not financially liable or which are without legal recourse to an Insured; and (6) matters which may be deemed uninsurable under the provincial or state law pursuant to which this policy shall be construed.

113 Clause 2(h) further defines "Defence Costs" as follows:

(h) "Defence Costs" means reasonable and necessary fees, costs and expenses consented to by the Insurer (including premiums for any appeal bond, attachment bond or similar bond arising out of a covered judgment, but without any obligation to apply for or furnish any such bond) resulting solely from the investigation, adjustment, defence and/or appeal of a Claim against an Insured, but excluding any compensation of any Insured Person or any Employee of an Organization.

114 The Policies have the following Notice at the beginning of each of the Policies wordings:

NOTICE: THE INSURER DOES NOT ASSUME ANY DUTY TO DEFEND. THE INSURER MUST ADVANCE DEFENCE COSTS, EXCESS OF THE APPLICABLE RETENTION, PURSUANT TO THE TERMS HEREIN PRIOR TO THE FINAL DISPOSITION OF THE CLAIM.

115 Clause 8 in each of the Policies, as set forth in Endorsement #11 in each of the Policies, provides in part, as follows:

8. DEFENCE COSTS, SETTLEMENTS, JUDGMENTS (INCLUDING THE ADVANCEMENT OF DEFENCE COSTS)

(a) Under Coverage A,B and C of this policy, except as hereinafter stated, the Insurer

shall advance, excess of any applicable retention amount, covered Defence Costs no later than ninety (90) days after the receipt by the Insurer of such defence bills. Such advance payments by the Insurer shall be repaid to the Insurer by each and every Insured Person or Organization, severally according to their respective interests, in the event and to the extent that any such Insured Person or Organization shall not be entitled under this policy to payment of such Loss.

(b) The Insurer does not, under this policy assume a duty to defend. The Insureds [sic] Person and, with respect to Coverage B, the Organization, shall defend and contest any Claim made against them. ...

116 In my view, the above wording of the Policies is clear and unambiguous. The Insurer, American Home and the Excess Insurers, have a duty to advance defence costs prior to the final disposition of the Kipperman Action.

117 The Plaintiffs submit that the principles developed by the courts in the duty to defend cases provide useful guidance in determining when the obligation to advance pay defence costs arises. The duty to defend cases impose a duty to defend on an insurer in circumstances where the policy provides for such duty and a claim or claims are advanced in a pleading which, if true, might arguably amount to an occurrence for which there is coverage under the provisions of the policy. Only the policy and the "true nature" of the claims in the pleading are considered by the court in determining whether a duty to defend has been triggered. See: *Nichols v. American Home Assurance Company*, [1990] 1 S.C.R. 801 (S.C.C.); *Non-Marine Underwriters, Lloyd's of London v. Scalera,* [2000] 1 S.C.R. 551 (S.C.C.); *Monenco Ltd. v. Commonwealth Insurance Co.*, [2001] 2 S.C.R. 699 (S.C.C.); *Cooper v. Farmers' Mutual Insurance Co.* (2002), 59 O.R. (3d) 417 (C.A.); *Halifax Insurance Co. of Canada v. Innopex Ltd.* (2004), 72 O.R. (3d) 522 (C.A.).

118 Based on the principles established in the duty to defend cases, the Plaintiffs submit that the Defendants' duty to advance defence costs under the Policies is triggered in this case having regard to the claims advanced in the Complaint and that such claims, if true, "arguably" amount to a Wrongful Act for which there is coverage under one or other of the Policies.

119 American Home submits that, at best, the duty to defend cases are of limited assistance in determining whether a duty to advance defence costs has been triggered under a policy. It points to *Continental Insurance Co. v. Dia Met Minerals Ltd.* (1996), 20 B.C.L.R. (3d) 331 (B.C.C.A.) where the British Columbia Court of Appeal, in the circumstances of that case, held that the pleadings alone should not govern the apportionment of defence costs.

120 *Dia Met*, *supra*, involved consideration of the extent of an insurers' obligation to pay the insureds' defence costs under a directors and officers liability policy where the policy required the insurers, among other things, to "defend any suit against the officers and directors seeking loss payable under the terms of this policy." The policy did not give the insurer the right to appoint counsel.

121 The officers and directors of Dia Met were sued and some, but not all of the claims advanced in the action against them related to acts done in their capacity as directors and officers of Dia Met. The insured retained their own counsel. The insurers initially offered to provide counsel of their choice to the insured subject to a reservation of rights. The insured refused. In a subsequent proceeding, the British Columbia Supreme Court decided, pursuant to the provisions of the policy, that the insured retained their rights to control the defence. The issue remained, however, as to what portion of the defence costs the insurers were required to pay given that some of the claims asserted in the action were outside the scope of coverage of the policy. On a subsequent motion for directions, the Chambers judge, after noting that it was impossible to proportion costs with any accuracy in the absence of a final determination of the action, applied an arbitrary allocation as submitted by the insurer.

122 In allowing the appeal, Newbury J.A. noted the "almost insurmountable difficulty of apportioning defence costs, on the basis of pleadings alone, before or even after trial." She held that the obligation to indemnify in respect of defence costs should be assessed retrospectively and ordered the insured to provide the insurers with sufficient information to enable the apportionment of the costs, the action having settled prior to the appeal being heard.

123 In my view, *Dia Met* is very different from this case both in terms of its facts and the issue it was dealing with. What is particularly important is that the insurance policy in issue in *Dia Met* was very different in respect of the duty to pay defence costs than the Policies in issue here. As I read the decision, the policy in *Dia Met* was a duty to defend policy where, because of an absence in the policy of a waiver by the insured of their right to select and instruct counsel and the actions of the insured in retaining their own counsel, the court held the insurer was obligated to indemnify the insured's defence costs.

124 It is clear that there is a distinction between the duty to defend and the duty to indemnify in insurance policies. The former is broader than the latter and depends on the nature of the claim, not on the judgment that results from the claim: *Nichols*, supra, at para. 17. It follows, therefore, that where a policy provides that the obligation to pay defence costs is part of the duty to indemnify and nothing more, it is appropriate to assess such costs retrospectively, as was held in *Dia Met*.

125 That, however, is not the case with the Policies in issue here. The Policies clearly state that American Home assumes no duty to defend. While the obligation to pay defence costs is part of the indemnity language of the Policies, the provisions of the Policies clearly provide that American Home has mandatory duty to advance defence costs, excess of the applicable retention, pursuant to the terms of the Policies, prior to the final disposition of a claim. Clause 8 provides that the Insurer "shall advance". The amounts advanced are referred to as "advance payments." Clause 8 further provides that to the extent and in the event that the Insured is not entitled under the Policy to such payment (i.e. for claims not covered), they are obligated to repay American Home such defence costs advanced. Finally, Clause 8 provides for an allocation where defence costs are jointly incurred with other companies or individuals.

126 Based on the clear and unambiguous wording of the Policies in issue dealing with the obligation to pay defence costs, in my view the duty to advance defence costs in the Policies is broader than the duty to indemnify and accordingly because it arises prior to a final determination of the issues in the action, any determination of whether such duty arises must be based on the claim advanced, similar to the duty to defend. What are "covered Defence Costs" can only be determined based on the claims being asserted in the action.

Which Policy applies in respect of the Kipperman Action, the 2002-2003 D&O Policy or the 2004-2005 D&O Policy?

127 Paragraph 7(c) of the Onex D&O Policies states in relevant part as follows:

> (c) If during the Policy Period ... an Organization or an Insured shall become aware of any circumstances which may reasonably be expected to give rise to a Claim being made against an Insured and shall give written notice to the Insurer of the circumstances, the Wrongful Act allegations anticipated and the reasons for anticipating such a Claim, with full particulars as to dates, persons and entities involved, then a Claim which is subsequently made against such Insured and reported to the Insurer alleging, arising out of, based upon or attributable to such circumstances or alleging any Wrongful Act which is the same as or related to any

> Wrongful Act alleged or contained in such circumstances, shall be considered made at the time such notice of such circumstances was given.

128 The Plaintiffs submit that the forwarding of the complaint in the Kipperman Action to American Home on July 4, 2005, during the currency of the 2004-2005 D&O Policy constitutes notice of a Claim under that Policy and accordingly the 2004-2005 D&O Policy applies. The Defendants, on the other hand, submit that the Foley Letter which was sent to American Home on behalf of the Plaintiffs during the currency of the 2002-2003 Onex Policy constitutes sufficient notice of circumstances which may reasonably be expected to give rise to a "Claim" as provided in clause 7(c) of that Policy such that it applies to the Kipperman Action.

129 Paragraph 7(c) of the 2002-2003 D&O Policy is clear and unambiguous in its wording. It operates to extend the "claims-made and reported" nature of the Policy by providing coverage for a Claim made after the policy period where "circumstances which may reasonably be expected to give rise to a Claim" have been reported to American Home during the policy period.

130 Such a provision is not unusual in claims made directors and officers' policies. In the publication: *Insurance Law in Canada*, (Toronto: Carswell, 1999) at p. 18-164.5, para. 18.15(j)(iv), Professor Craig Brown states:

> D&O policies usually permit, but do not require the report of circumstances that may lead to a claim. The clause may stipulate the type of information that is to be reported. Where such a report is made in accordance with the policy terms, any subsequent claim arising out of the reported circumstances is deemed to have occurred at the time the notice was given.
>
> This is a very valuable coverage for the directors and officers, particularly where the policy is due to be terminated by reason of non-renewal, cancellation, or insolvency. In the absence of such a clause, there would be no coverage where the insured learned of circumstances that could lead to a claim, but where the claim was not made until after termination of the insurance. Coverage may be preserved by giving the appropriate notice pursuant to this clause.

131 American Home and the Excess Insurers submit that the Foley Letter, sent by Aon to American Home on November 28, 2003 constitutes notice of circumstances pursuant to paragraph 7(c) of the 2002-2003 D&O Policy resulting in the subsequent Kipperman Action being a Claim made during the period of the 2002-2003 D&O Policy.

132 The Plaintiffs submit that the Foley Letter does not constitute notice of circumstances under paragraph 7(c) of the 2002-2003 D&O Policy because the Foley Letter did not comply with the requirements of 7(c) because it did not contain the specified particulars.

133 In support of the issue of whether the Foley Letter constitutes notice of circumstances under paragraph 7(c) of the 2002-2003 D&O Policy, the Excess Insurers have filed the affidavit of Geoffrey Raicht, a partner with the law firm of McDermott Will & Emery LLP in New York City. Mr. Reicht has extensive experience in U.S. bankruptcy and insolvency proceedings and he is tendered as an expert in the area. His affidavit attaches a report which provides a basic overview of the structure of U.S. bankruptcy law relevant to the Action; provides a delineation of the developments in Magnatrax's Chapter 11 proceedings, including the progression of procedural steps which occurred as obtained from the US Bankruptcy Court files; and provides a comparison of the entities and causes of action as contained in the Foley Letter and the Kipperman Action.

134 Based on Mr. Reicht's education and experience, I have no hesitation in accepting his expertise and his evidence concerning US bankruptcy law and the steps which took place in Magnatrax's Chapter 11 proceedings. I am not, however, prepared to consider or rely on his comparison of the entities and claims asserted in the Foley Letter and the Kipperman Action. In my view Mr. Reicht's evidence on the issue of the factual similarities between the Foley Letter and the claims in the Kipperman Action is neither admissible nor helpful. It is an issue that can be determined by me having regard to the documents themselves.

135 There is no Canadian authority directly dealing with the issue of what constitutes sufficient notice of circumstances under a directors and officers' liability policy to entitle a subsequent claim arising out of such notice to be deemed to have occurred during the policy period. There are, however, a number of American authorities which have considered the issue in the context of directors and officers liability policies. These authorities are relied upon by both the Plaintiffs and the Defendants. While such authority is not binding on me, it is of assistance in determining the issue of whether the Foley Letter constitutes sufficient notice under paragraph 7(c) of the 2002-2003 Onex Policy.

136 Having said that, I am in agreement with the US cases which hold that in determining whether notice by an insured to an insurer is sufficient, an objective test should be applied having regard to the wording of the policy. The test is whether the insured objectively complied with the notice provision in the Policy: *Continental Ins. Co. v. Superior Court* 37 Cal. App. 4th 69 (1995), California Court of Appeal, Second District, Division 3; *McCullough v. Fidelity & Deposit Co.* 2 F3d 110 (1993), Court of Appeal, Fifth Circuit

137 In my view, the wording of paragraph 7(c) of the 2002-2003 Onex Policy is clear. In order for a Claim made after the policy period to be covered under the 2002-2003 Onex Policy, Onex must provide written notice to American Home during the Policy Period of the following:

1. circumstances which may reasonably be expected to give rise to a claim being made against a director or officer of Onex;
2. the Wrongful Act allegations anticipated; and
3. the reasons for anticipating a Claim, with full particulars as to dates, persons and entities involved.

138 In addition, clause 7(c) further requires that the Claim which is subsequently made and reported to American Home must be the same as or related to any Wrongful Act contained or alleged in the notice.

Timing of the Notice

139 There is no issue that the Foley Letter was provided to American Home on November 28, 2003, within the Policy Period of the 2002-2003 Onex D&O Policy.

Circumstances Which May Reasonably Be Expected to Give Rise To A Claim

140 In my view, the Foley Letter set out the circumstances which may reasonably be expected to give rise to a claim being made against a director or officer of Onex.

141 The Foley Letter was forwarded to American Home by Aon with the latter noting that it contains information which could in the future give rise to a claim. The Foley Letter, written on behalf of the Creditors' Committee in the Magnatrax Bankruptcy, refers to claims by Magnatrax and its subsidiaries against "parties involved in the May 1999, September 1999 and March 2000 transactions, as well as

credit facilities and related agreements supporting those transactions." It further asserts claims related to the "Restructuring and Lockup Agreement." It is clear that those transactions and Agreement involved Magnatrax and the other entities and individuals named in the letter.

142 Further, the Foley Letter specifically lists the "numerous claims" that the Creditors' Committee alleges exist and lists the entities, including Onex, and the individuals, including the officers and directors of Onex, against whom the claims should be pursued.

143 Finally, the Foley Letter makes it clear that in the absence of Magnatrax and its subsidiaries prosecuting all of the claims listed against all of the entities and individuals listed in the Letter, the Creditors' Committee will do so.

The Wrongful Acts

144 In my view, the Foley Letter also clearly lists the Wrongful Acts complained of.

145 The Foley Letter states that the claims to be asserted include fraudulent transfers, breach of fiduciary duty, aiding and abetting both breach of fiduciary duties and fraudulent transfers, equitable subordination, unjust enrichment, declaratory relief, preference actions and other claims to be identified and that the parties against whom some or all of the claims should be pursued include Onex and its affiliates and officers and directors of Onex.

The Reasons For Anticipating A Claim With Full Particulars

146 The Foley Letter clearly sets forth, in my view, both on its face and in its content, the reasons why Onex and its directors and officers should anticipate a Claim.

147 Rather than a notice from the insured, the Foley Letter is a lawyers' letter written by a lawyer acting for the Creditors' Committee who is opposite in interest to Magnatrax and Onex.

148 Further, it clearly indicates an intention to pursue the claim. It requests "immediate" confirmation from Magnatrax that it will prosecute the claims set out in the letter against the entities noted which includes the officers and directors of Onex. It then goes on to state that in the event Magnatrax does not intend to fully prosecute such claims, the Creditors' Committee requests Magnatrax's "immediate" confirmation that the Creditors' Committee can pursue such claims on Magnatrax's behalf. As Mr. Reicht points out in his report, such a request is a necessary step in U.S. bankruptcy proceedings in order for the Creditors Committee to subsequently obtain derivative standing from the U.S. Bankruptcy Court to assert such claims.

149 The Plaintiffs submit that the Foley Letter does not satisfy the specificity requirements of clause 7 (c) of the 2002-2003 D&O Policy in that it does not set out full particulars as to dates, persons and entities involved. In particular they submit that Onex did not describe the nature of the commercial transactions or its role in them; did not specify a single wrongful act they thought might be alleged against them; provided no particulars as to the dates, persons or entities involved or the names of the directors and officers that had anything to do with Magnatrax.

150 In my view, when viewed as a whole, the Foley Letter contains sufficient particulars to meet the requirements of clause 7(c). As noted it sets out the specific transactions and agreement involved, the dates of the transactions, the claims which are alleged to exist and the entities and individuals involved. Clause 7(c) contains no requirement to set out Onex's roll in the transactions. While the Foley Letter does not list the individual officers and directors of Onex by name, it does refer to them generally. In my view, that is sufficient, particularly given that the Foley Letter was written by a third party and not

Onex. It is not reasonable in the circumstances to require Onex to list the specific names of its directors and officers that the Creditors' Committee may or may not proceed against.

151 In support of their argument that the Foley Letter is deficient, the Plaintiffs submit that at the time it was sent to American Home, they had more information than was in the notice. As noted, the Foley Letter was sent to Aon in August 2003 shortly after it was received by Magnatrax and Onex but for reasons not explained in the evidence, it was not sent to American Home until November 28, 2003, the eve of the expiry of the 2002-2003 D&O Policy.

152 The Defendants counter by submitting that the Plaintiffs should not be entitled to rely on Onex's failure to provide sufficient detail to American Home at the time it sent the Foley Letter or on its subsequent failure to provide additional information concerning the claims as was requested by the American Home.

153 While there is no direct evidence before me that Onex had more information about the Creditors' Committee's claim than contained in the Foley Letter when it was sent to American Home, it is likely that is the case given Onex's involvement in the negotiations and subsequent agreement to the Magnatrax Plan of Reorganization in the US bankruptcy proceedings. In my view, however, the fact that Onex may have had more knowledge about the claims than was in the Foley Letter at the time it was submitted to American Home or thereafter does not impact on the issue of whether the Foley Letter complies with clause 7(c) of the Policy. As noted, the test is an objective one having regard to the wording of the Policy. What is relevant is the information contained in the notice. As a result, it is immaterial whether the Plaintiffs were in possession of more information than was supplied to American Home. See: *Continental Ins. Co. v. Metro-Goldwyn-Mayer, Inc.* 107F.3d 1344.

154 The Defendants further submit that based on the testimony of the Aon representatives on the motions, it is clear that when Aon provided the Foley Letter to American Home on November 28, 2003, it was intended as "notice of circumstances" under clause 7(c) of the 2002-2003 D&O Policy.

155 Once again, because the test as to whether the Foley Letter complies with the provisions of clause 7(c) of the 2002-2003 D&O Policy is an objective one, based on the wording of the Policy, the "intention" of Onex or its representatives is not relevant. The sufficiency of the Foley Letter must be considered objectively having regard to the wording of clause 7(c).

156 For the above reasons, therefore, it is my view that the Foley Letter, when viewed objectively as a whole, contains sufficient particulars of the dates, persons and entities involved to comply with clause 7 (c) of the 2002-2003 D&O Policy.

The Claims in the Kipperman Action Must Be The Same or Related to the Wrongful Acts alleged in the Notice

157 In my view, it is clear from a review of the Foley Letter and the complaint in the Kipperman Action that the claims being advanced in the Kipperman Action are "the same as or related to" the claims asserted in the Foley Letter.

158 The Foley Letter referred to claims arising out of transactions in May 1999, September 1999 and March 2000. The Kipperman Action is based on the acquisition of American Building Company by Magnatrax in May 1999, the acquisition of Republic Builders Products in August 1999 and the acquisition of Janock, Ltd. in March 2000.

159 Further, the claims asserted in the Kipperman Action against the individual Plaintiffs are breach of fiduciary duty; aiding and abetting breach of fiduciary duty; civil conspiracy; and unjust enrichment.

The Foley Letter sets out a number of claims including breach of fiduciary duty, aiding and abetting breach of fiduciary duty and unjust enrichment. It is clear, therefore, that the Foley Letter alleges the same or related claims against Onex and its directors and officers that are alleged in the Kipperman Action.

160 Nor does any issue arise from the fact that the Foley Letter was sent on behalf of the Creditors Committee and the Kipperman Action is brought by the Trustee on behalf of the Litigation Trust. The Litigation Trust was created as part of the Magnatrax Plan of Reorganization in the US bankruptcy proceedings in order to advance the claims alleged by the Creditors Committee against the defendants in the Kipperman Action for the benefit of the creditors of Magnatrax and its subsidiaries.

161 For the above reasons, therefore, it is my view that the Foley Letter clearly meets the requirements of clause 7(c) of the 2002-2003 Onex Policy such that the Kipperman Action constitutes a Claim made during Policy Period of the 2002-2003 Onex Policy.

Do any of the Exclusions or Limitations of the 2002-2003 D&O Policy and/or the 2004-2005 D&O Policy Operate to Exclude coverage of the Kipperman Action?

a) 2004-2005 D&O Policy

162 Clause 4 of both the 2002-2003 D&O Policy and the 2004-2005 D&O Policy sets out the exclusions from the Policies. Specifically, clause 4(d) provides as follows:

> 4. EXCLUSIONS
>
> The Insurer shall not be liable to make any payment for Loss in connection with any Claim made against an Insured:
>
> (d) Alleging, arising out of, based upon or attributable to the facts alleged, or to the same or related Wrongful Acts alleged or contained in any Claim which has been reported, or in any circumstances of which notice has been given, under any policy of which this policy is a renewal or replacement or which it may succeed in time;

163 Recognising that exclusions are construed narrowly, in my view, the wording of clause 4(d) is clear and straightforward. Claims covered by prior D&O Policies are excluded from coverage under the current D&O Policy.

164 As I have already found, based on the notice provided to American Home by the Foley Letter on November 28, 2003, the claims in the Kipperman Action are claims made during the currency of the 2002-2003 D&O Policy in accordance with the provisions of clause 7(c) thereof. The 2004-2005 D&O Policy is a renewal of the 2003-2004 D&O Policy which is, in turn, a renewal of the 2002-2003 D&O Policy. While, therefore, the 2004-2005 D&O Policy is not a direct renewal of the 2002-2003 D&O Policy, it certainly succeeds it in time.

165 In my view, therefore, Exclusion 4(d) of the 2004-2005 D&O Policy operates to exclude American Home from having to pay for any Loss in connection with the Kipperman Action. It follows that, because the Excess Insurers agreed to follow the form of the American Home 2004-2005 D&O Policy, they are also excluded from any liability under the excess policies for any Loss in respect of the Kipperman Action. The Action should be dismissed against them.

b) 2002-2003 D&O Policy

166 American Home submits that based on the wording of Endorsement #14 of the 2002-2003 D&O Policy, the specific entity exclusion in respect of Magnatrax, it is not liable under the 2002-2003 D&O Policy for any Loss arising out of the Kipperman Action.

167 Endorsement #14 was added the 2002-2003 D&O Policy at the time of the inception of the Magnatrax Run-Off Policy on May 12, 2003. It is entitled: Specific Entity/Subsidiary Exclusion (Claims brought by or against it). It reads as follows:

> In consideration of the premium charged, it is hereby understood and agreed that the **Insurer** shall not be liable for **Loss** alleging, arising out of, based upon or attributable to or in connection with any **Claim** brought by or made against the **Entity** listed below and/or any **Insureds** thereof.
>
> 1. MAGNATRAX Corporation (including any subsidiary or affiliate thereof)
>
> It is further understood and agreed that the Definition of Subsidiary shall not include MAGNATRAX Corporation. Further, the Insurer shall not be liable to make any payment for Loss in connection with any Claim made against an insured alleging, arising out of, based upon or attributable to any breach of duty, act, error or omission of MAGNATRAX Corporation, or any director, officer, member of the board of managers or employee thereof.

168 Both American Home and the Excess Insurers submit that Endorsement #14 is an "absolute" exclusion clause which provides a total exclusion of all claims related to or involving Magnatrax.

169 Once again, I am of the view that the wording of Endorsement #14 is clear and unambiguous. While I agree that Exclusion #14, by its wording, is an exclusion provision, I do not agree that it operates as an "absolute" exclusion in respect of all claims against Onex's directors and officers relating to Magnatrax.

170 The first paragraph of Endorsement #14 relieves the Insurer from liability under the Policy for any Loss arising from, based upon or attributable to or in connection with any Claim brought by or made against Magnatrax and/or any officer, director or employee of Magnatrax. The wording is clear and straightforward. Any Claim brought by Magnatrax and/or its officers and directors against Onex and its directors and officers is excluded. Likewise, any Claim made against Magnatrax and/or its officers and directors is also excluded.

171 The second paragraph of Endorsement #14 begins by removing Magnatrax from the definition of Subsidiary under the Policy. This effectively reiterates that American Home is relieved from liability under the Policy in respect of Claims against Magnatrax and it officers and directors.

172 The final sentence of paragraph two of Endorsement #14 further relieves the insurer of liability under the Policy in connection with any Claim made against an Insured (an officer or director of Onex or its listed subsidiaries) "alleging, arising out of, based upon or attributable to any breach of duty, act, error or omission of" Magnatrax or any director, officer, member of the board of managers or employee of Magnatrax.

173 Accordingly, when read in its entirety, Endorsement #14 operates to remove Magnatrax (and any subsidiary or affiliate) from coverage under the 2002-2003 D&O Policy and exclude any claim against Onex directors and officers by or against Magnatrax or arising out of, based upon or attributable to any act on the part of Magnatrax or its directors and officers. What Endorsement #14 does not exclude, in

my view, is any claim by a third party against Onex's directors and officers in their capacity as such for their wrongful acts in relation to Magnatrax.

174 Based on the above interpretation of Endorsement #14, it is my view that the Kipperman Action is not excluded from coverage under the 2002-2003 D&O Policy. As has been previously discussed, the Kipperman Action asserts claims against the individual Plaintiffs in their capacity as directors and/or officers of Onex relating to Magnatrax. The claims are not based upon or attributable to any act on the part of Magnatrax or its directors and officers.

175 Nor is the Kipperman Action brought by Magnatrax. As noted earlier, the Kipperman Action is brought by the Trustee of the Magnatrax Litigation Trust. The Magnatrax Litigation Trust was established pursuant to s. 4.21 of the Magnatrax Plan of Reorganization which was approved by the US Bankruptcy Court in the Magnatrax bankruptcy proceedings. It is clear, however, from both the Foley Letter and the Complaint in the Kipperman Action that the claims being advanced in the Kipperman Action are claims which, up until their assignment to the Litigation Trust pursuant to the Magnatrax Plan of Reorganization, belonged entirely to Magnatrax and its subsidiaries.

176 The Foley Letter seeks immediate confirmation from Magnatrax and its subsidiaries in bankruptcy that it will pursue the claims identified against the entities and the individuals named, failing which it requested confirmation that the Creditors' Committee could pursue the claims of Magnatrax and its subsidiaries on their behalf.

177 The Complaint in the Kipperman Action asserts various causes of action against the individual Plaintiffs based on their alleged actions in respect of certain acquisitions by Magnatrax and its subsidiaries in 1999 and 2000 which caused those companies significant damage, resulting in their bankruptcy. The causes of action initially belonged to Magnatrax and its subsidiaries. The entitlement to pursue such causes of action by way of their transfer and assignment to the Magnatrax Litigation Trust in the Magnatrax bankruptcy proceedings is set forth in paragraphs 125 to 130 of the Complaint in the Kipperman Action.

178 Notwithstanding that the claims which are asserted against Swartz, Govan, Wright and Hilson in the Kipperman Action are derivative claims which initially belonged to Magnatrax and its subsidiaries, in my view, they are not brought by Magnatrax. The exclusion in the first paragraph of Endorsement #14 of the 2002-2003 D&O Policy is clear. It applies to "any Claim brought by ..." Magnatrax or any subsidiary or affiliate thereof. While the Kipperman Action asserts claims which originally belonged to Magnatrax and its subsidiaries, it is brought by the Trustee on behalf of the Magnatrax Litigation Trust and not Magnatrax.

179 As noted earlier, exclusions are to be interpreted narrowly. In the absence of more expansive wording in Endorsement #14 to exclude derivative claims, the words: "any Claim brought by or made against [Magnatrax, its subsidiaries and affiliates]" restrict the application of the exclusion to claims brought by Magnatrax, its subsidiaries and affiliates. As the Kipperman Action is not such a Claim, Endorsement #14 does not exclude it from coverage.

180 Nor, in my view, can American Home rely on Endorsement #10 of the 2002-2003 D&O Policy which excludes claims against any Insured where the claim is brought in any bankruptcy proceeding by or against an Organization when the claim is brought by, among others, the creditors' committee or trust. Endorsement #14 removed Magnatrax as a subsidiary thereby excluding it from the definition of Organization under the 2002-2003 D&O Policy.

181 Accordingly, for the above reasons, it is my view that American Home is required to indemnify the individual Plaintiffs for their defence costs in respect of the Kipperman Action pursuant to the

provisions of the 2002-2003 D&O Policy.

182 American Home submits that pursuant to the Magnatrax Run-Off Policy it is only liable for one US $15 million limit in respect of pre-May 12, 2003 Magnatrax related claims and it has already paid that amount on account of the Kipperman Action pursuant to the Magnatrax Run-Off Policy. In other words, American Home submits that the Plaintiffs are not entitled to double recovery.

183 In support of its submission, American Home relies on Endorsement #16 of the Magnatrax Run-Off Policy:

> In consideration of the premium charged, it is hereby understood and agreed that, with respect to any Claim under this policy for which coverage is provided by one or more other policies issued by the Insurer or any other member of the American International Group (AIG), (or would be provided but for the exhaustion of the limit of liability, the applicability of the retention/deductible amount or coinsurance amount, or the failure of the Insured to submit a notice of Claim) the Limit of Liability provided by virtue of this policy shall be reduced by the limit of liability provided by said other AIG policy.

184 Endorsement #16 applies to the Magnatrax Run-Off Policy. It operates to reduce the limit of liability of the Magnatrax Policy Run-Off Policy by the limit of liability of any other American Home or AIG policy that provides coverage for the claim. Although at the time the Magnatrax Run-Off Policy was entered into the parties agreed to add an endorsement to the 2002-2003 D&O Policy providing for non-pyramiding of limits, no such provision was ever added. In the absence of a provision in the 2002-2003 D&O Policy similar to Endorsement #16 in the Magnatrax Run-Off Policy, there is no basis for reducing the amount required to be paid pursuant to that Policy in respect of the Kipperman Action.

185 As noted, American Home paid the full extent of its liability of US $15 million under the Magnatrax Run-Off Policy on account of defence costs incurred in the Kipperman Action. Messrs Ammerman and Blackmon, who were directors and officers of Magnatrax received US $1,118,008.10 on account of their defence costs and the individual Plaintiffs received US $13,881,991.90 in respect of their defence costs. American Home's liability under the 2002-2003 D&O Policy does not extend to paying the Plaintiffs for defence costs already reimbursed. It does extend, however, to any defence costs incurred by the individual Plaintiffs in respect of their defence of the Kipperman Action.

186 In reaching my decision that American Home is required to indemnify the individual Plaintiffs in respect of defence costs incurred in the defence of the Kipperman Action pursuant to the 2002-2003 D&O Policy, I wish to make it clear that I have not considered the effect of such decision on the Magnatrax Run-Off Policy, having particular regard to Clause 8 and Endorsement #16 of that Policy and the amounts previously paid to the individual Plaintiffs pursuant to it. Those issues were never raised by the parties on the motions and were not argued before me.

Conclusion

187 For the reasons set out in the Introduction, on the consent of the parties, the Plaintiffs' summary judgment motion and the Action are dismissed against the Defendants Liberty Mutual Insurance Company and Houston Casualty Company. It follows that the cross-motions of the said defendants are dismissed as well.

188 Further, and for the above reasons, the Plaintiffs' summary judgment motion is dismissed against the remaining Excess Insurers, the Defendants Brit Syndicates Ltd. (Lloyd's Syndicate 2987), Heritage Managing Agency Limited (Lloyd's Syndicate 3245) and XL Company Limited and their cross-

summary judgment motions are allowed and the Action is dismissed against those Defendants in its entirety.

189 The Plaintiffs' summary judgment motion is allowed against American Home in accordance with paragraphs (b) of their Amended Notice of Motion dated November 30, 2009 granting the Plaintiffs a declaration that American Home is required by the terms and conditions of the 2002-2003 D&O Policy to indemnify the plaintiffs as their interests may appear in respect of defence expense incurred and ongoing on behalf of the individual Plaintiffs in defence of the Kipperman Action to the extent that such expenses were not covered under the Magnatrax Run-Off Policy and judgment against American Home consequential to such declaration in an amount to be determined by the court.

190 American Home's cross-summary judgment motion is dismissed.

191 In the event that the parties are unable to agree on costs within 30 days from the date of this judgment, they should arrange a conference call through my assistant to agree on a procedure to resolve costs.

L.A. PATTILLO J.

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TAB 4

Publisher's Note

2014 — Release 8

Previous release was 2014-7

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Craig Brown

Insurance Law in Canada

This work provides a complete treatment of insurance law in Canada, combining a scholarly treatment of general principles with a practical treatment of the issues arising in specific types of insurance practice. Chapters 1 through 15 contain the established text on the subject, Insurance Law in Canada. Chapters 16 through 20 are authored by practitioners who are experts in their respective fields: accident and sickness insurance; automotive insurance; liability insurance; marine insurance; and property insurance. The service gives you practical coverage of the issues arising in practice, combined with trusted coverage of first principles, all at your fingertips. The authors deal with legislation and case law from all across Canada. The work is published in a looseleaf format, ensuring currency through regular updates.

This release adds case citations throughout the text and additional valuable commentary. A new "Issues in Focus" article dealing with the scope of the insurer's duty of good faith in light of *Mandevillve v. Manulife*.

Highlights

Issues in Focus — The Scope of an Insurer's Duty of Good Faith - *Mandeville* v. *The Manufacturers Life Insurance Co.* was decided purely as a negligence case without reference to the law relating to insurers' duty of good faith in dealings with policyholders. In my view, the good faith duty could have arguably factored into the analysis in two separate but connected ways. This is not to say that acceptance of

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INSURANCE LAW IN CANADA

Volume 2

It would seem advantageous for the Organization to refuse to indemnify the directors and officers, so as to avoid having to pay the retention amount applicable to Coverage B. Many policies therefore contain a "presumptive indemnification" clause stating that the Coverage B retention applies where the Organization fails or refuses to indemnify the Insured Persons to the fullest extent permitted by law. This clause usually contains an exception for situations where the Organization is unable to indemnify because of insolvency.

The purpose of a presumptive indemnification clause is obvious. From the insurer's perspective, D&O coverage is not intended to be the first source of recovery. The directors are to turn first to the Organization for indemnification. The retention amount, particularly where it is large, encourages the Organization to settle the claim within the retention amount, or to otherwise deal with it efficiently, as it is using its own money up to the level of the retention.

Third, the policy usually has a related claim provision stating that all claims arising out of the same *Wrongful Act* shall be considered a single claim. It also usually provides that such related claims are deemed to have been made on the earliest date on which the claim was first made. This way only one retention amount and one limit of liability applies if there are a number of claims arising out of the same act.[77]

(l) Defence Costs and Settlement

(i) *Reimbursement for Defence Costs*

As discussed above,[78] the insurer usually has no duty to defend a claim pursuant to a D&O policy. Rather, the policy typically provides that the insurer will reimburse the insured for the defence costs incurred.[78a]

This creates a very important distinction from general liability policies. In the CGL policy, the insurer usually has a contractual duty to defend any claim that is potentially covered by the policy. The courts look to the pleadings to determine whether the claim alleges facts that, if proven, would be covered by the policy.

D&O policies are different. As discussed above,[79] they are indemnity policies, not liability policies. The policy does not cover the insured's legal liability. Instead, it

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77 See section 18.16(a)(iii).

78 See above, note 40 and accompanying text.

78a Where there are layers of insurance, an excess insurer may have a duty to defend as opposed merely to having to pay excess defence costs. In *Goodman* v. *AIG Commercial Ins. Co.* (2010), 85 C.C.L.I. (4th) 1 (Ont. C.A.), the Ontario Court of Appeal held that the excess insurer, whose policy provided a duty to defend "if defence is not provided by . . . any underlying insurance". Although the excess policy contained a "follow form" clause, the court said that it applied only to indemnity and not defence costs. Accordingly, the excess insurer could not invoke the "no duty to defend" clause in the underlying policy. For comment on this case, see Palmay and Waterman, "Lawyers serving as directors get less coverage despite extra premium," Law Times, Sept. 13, 2010, p. 7.

reimburses for "Loss", which is defined to include the costs of defence. Unless the policy specifically provides otherwise, the general rule is that the policy only covers the cost of defending claims (or those portions of claims) that are actually covered by the policy.[79a]

As noted above, the policy often defines a *Wrongful Act* as an actual or *alleged* error, misstatement, etc. Accordingly, the cost of defending *alleged* Wrongful Acts will be covered, subject to the other policy terms, regardless of whether the director or officer is found liable.

(ii) *Advancement of Defence Costs*

Whether the insurer must advance defence costs prior to the resolution of the claim in the absence of a contractual provision to that effect is a contentious issue. Some cases note that coverage for defence costs can only be determined once the claim is finally resolved, so the insurer is not required to advance defence costs prior to resolution. Other courts hold that defence costs must be advanced prior to resolution, because the policy covers the legal obligation to pay Loss, which includes defence costs. The rationale is that the directors and officers have a legal obligation to pay the defence costs as soon as the accounts are rendered by defence counsel.

Some policies avoid this problem with a contractual provision.[79b] The clause typically states that the insurer will advance the costs of defence prior to the resolution of the claim. The advancement clause is inserted in the policy to make it more marketable. It is obviously beneficial to have defence costs advanced prior to resolution, as the cost of defending can bankrupt individuals and sometimes even corporations.

The advancement clause may impose certain conditions before any advancement of defence costs can take place. The most usual condition is that the insureds agree to repay the advanced funds in the event it is finally established that the insurer has no liability under the policy. The policy may also require that the appropriate retention be satisfied and that the insurer and insureds have agreed on an appropriate allocation of defence costs between covered and uncovered claims.

(iii) *Conduct of the Defence and Selection of Counsel*

The policy usually states that the insured, and not the insurer, has the duty to defend any Claims. This generally permits the insureds to retain and instruct counsel of their choice to defend. Many policies, however, stipulate that the insurer must

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79 See above, note 38 and accompanying text.

79a See *Dunn* v. *Chubb Ins. Co.* (2009), 97 O.R. (3d) 701 (Ont. C.A.); *Aviva Ins. Co.* v. *Real Estate Errors and Omissions Ins. Corp.* (2009), 79 C.C.L.I. (4th) 148 (B.C. S.C.); *Coventree Inc.* v. *Lloyds Syndicate 1221* (2011), 4 C.C.L.I. (5th) 47 (Ont. S.C.J.).

79b See e.g. *Onex Corp.* v. *American Home Assur. Co.* (2011), 98 C.C.L.I. (4th) 229 (Ont. S.C.J.).

TAB 5

Courts of Justice Act

R.S.O. 1990, CHAPTER C.43

PART VII
COURT PROCEEDINGS

Declaratory orders

97. The Court of Appeal and the Superior Court of Justice, exclusive of the Small Claims Court, may make binding declarations of right, whether or not any consequential relief is or could be claimed. 1994, c. 12, s. 39; 1996, c. 25, s. 9 (17).

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

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

Court File No. CV-11-431153-00CP

THE TRUSTEES OF THE LABOURER'S PENSION FUND OF CENTRAL AND EASTERN CANADA et al
Plaintiffs

v.

SINO-FOREST CORPORATION et al
Defendants

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

Proceeding commenced at Toronto

Proceeding under the *Class Proceedings Act*, 1992

BOOK OF AUTHORITIES OF THE APPLICANT, CHUBB INSURANCE COMPANY OF CANADA (Motion Returnable April 20, 2015)

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